Kögun hf.

Consolidated Financial Statements
for the year 2006

Kögun hf.
Lynghálsi 9
110 Reykjavík

Reg. no. 490389-2619

Contents

Endorsement and Signatures of the Board of Directors and the CEO

The financial statements of Kögun hf. have been prepared in accordance with International Financial Reporting Standards (IFRS). The financial statements comprise the consolidated financial statements of Kögun hf. and its subsidiaries.

In the beginning of the year Kögun established the subsidiary Kögun USA inc. Kögun USA Inc. then acquired all the shares in the American company Specialists in Custom Software Inc. In March Kögun purchased 58,7% share in EJS hf. through its subsidiary Skýrr hf. In December EJS hf. was moved under direct ownership of Kögun which then also purchased the remaining 41,3% of EJS hf. As of 1 October Kögun hf. merged with ist subsidiary Verk- og kerfisfræðistofan ehf.

In September the Board of Directors approved a motion to recommend at a shareholders' meeting the merger of Kögun hf. and it's parent company Skoðun ehf. and the division of Kögun hf. into two separate entities, Kögun hf. and Hands Holding hf. The motion was approved at a shareholders' meeting on 17 November 2006 and was effective from 1 October 2006.

According to the income statement, loss for the year amounted to ISK 982 million. Loss from continuing operations amounted to ISK 39 million. The Company's equity amounted to ISK 2.748 million at the end of the year according to the balance sheet.

The Board of Directors and the CEO of Kögun hf. hereby confirm the Company's consolidated financial statements for the year 2006 by means of their signatures.

Reykjavík, 15 February 2007.

The Board of Directors:

Árni Pétur Jónsson

Ólafur Þór Jóhannesson

Örn Karlsson

CEO:

Bjarni Birgisson

Independent Auditor's Report

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Kögun hf., which comprise the consolidated balance sheet as at December 31, 2006, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement 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 as adopted by EU. 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 consolidated 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 consider 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 consolidated financial statements give a true and fair view of the financial position of Kögun hf. as of December 31, 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by EU.

Reykjavík, 15 February 2007.

KPMG hf.
Margret G. Flóvenz

Consolidated income statement for the year 2006

	Note	2006	2005 Restated*
Continuing operations			
Sales		7.311.543	3.680.213
Cost of sales		(5.408.123)	(2.467.420)
Gross profit		1.903.420	1.212.793
Other income	10	687.764	0
Sales expenses		(316.825)	(45.149)
Administrative expenses		(1.107.252)	(615.959)
Impairment losses on intangible assets	16	(18.560)	0
Results from operating activities		1.148.547	551.685
Finance income		233.234	385.262
Finance expenses		(1.372.446)	(518.617)
Net finance costs	13	(1.139.212)	(133.355)
Share of profit of associates		0	9.316
Profit before income tax		9.335	427.646
Income tax	14	(48.150)	(99.891)
(Loss) profit from continuing operations		(38.815)	327.755
Discontinued operations			
(Loss) profit from discontinued operations	7	(943.725)	308.206
(Loss) profit for the year		(982.540)	635.961
Attributable to:			
Equity holders of the parent		(853.945)	637.154
Minority interest		(128.595)	(1.193)
(Loss) profit for the year		(982.540)	635.961
(Loss) earnings per share:			
Basic (loss) earnings per share of ISK 1	25	(5,18)	3,35
Continuing operations:			
Basic (loss) earnings per share of ISK 1		(0,20)	1,72

* See discontinued operations (note 7).

The notes on pages 10 to 30 are an integral part of these consolidated financial statements.

In ISK thousands

Consolidated balance sheet as at 31 December 2006

	Note	2006	2005
Assets:			
Operating assets	15	467.736	999.807
Intangible assets	16	8.338.969	11.960.963
Investments in other companies	18	33.984	33.461
Long-term receivables	19	7.419.774	4.921
Deferred tax asset		0	455.454
Total non-current assets		16.260.463	13.454.606
Inventories and work in progress	20	245.792	318.294
Trade and other receivables	21	2.932.882	4.032.419
Cash and cash equivalents	22	377.935	2.850.562
Total current assets		3.556.609	7.201.275
Total assets		19.817.072	20.655.881
Equity:			
Share capital	23	183.000	189.829
Share premium	24	2.519.551	3.794.090
Legal reserve	24	45.750	48.250
Translation reserve		0	(138.141)
Retained earnings		0	1.723.565
Total equity attributable to equity holder of the parent		2.748.301	5.617.593
Minority interest		0	712.725
Total equity		2.748.301	6.330.318
Liabilities:			
Loans and borrowings	26	14.618.927	8.156.286
Deferred income tax liability	28	21.707	0
Total non-current liabilities		14.640.634	8.156.286
Loans and borrowings	26	215.624	2.313.293
Trade and other payables	29	2.212.513	3.855.984
Total current liabilities		2.428.137	6.169.277
Total liabilities		17.068.771	14.325.563
Total equity and liabilities		19.817.072	20.655.881

The notes on pages 10 to 30 are an integral part of these consolidated financial statements.

In ISK thousands

Consolidated statement of changes in Equity for the year 2006

	Share capital	Share premium	Legal reserve	Translation reserve	Retained earnings	Total	Minority interest	Total equity
Equity at 1.1.2005	190.366	3.850.726	48.250	(11.476)	1.143.921	5.221.787		5.221.787
Translation difference				(126.665)		(126.665)	(9.242)	(135.907)
Profit for the year					637.154	637.154	(1.193)	635.961
Total profit for the year				(126.665)	637.154	510.489	(10.435)	500.054
Dividends (ISK 0.30 per share)					(57.510)	(57.510)		(57.510)
Own shares, change	(537)	(56.636)				(57.173)		(57.173)
Minority interest, change							723.160	723.160
Equity at 31.12.2005	189.829	3.794.090	48.250	(138.141)	1.723.565	5.617.593	712.725	6.330.318
Equity at 1.1.2006	189.829	3.794.090	48.250	(138.141)	1.723.565	5.617.593	712.725	6.330.318
Translation difference 1.1. - 30.9.				188.847		188.847	30.728	219.575
Loss for the period 1.1.-30.9.					(855.977)	(855.977)	(207.720)	(1.063.697)
Total profit and loss for the period 1.1.-30.9.				188.847	(855.977)	(667.130)	(176.992)	(844.122)
Dividends (ISK 0.40 per share)					(77.200)	(77.200)		(77.200)
Own shares, change	3.171	202.598				205.769		205.769
Acquisition of minority interest							316.053	316.053
Minority interest, change					(43.411)	(43.411)	(69.399)	(112.810)
Dividends to minority interest							(11.564)	(11.564)
Equity at 30.9.2006	193.000	3.996.688	48.250	50.706	746.977	5.035.621	770.823	5.806.444
Effects of merger (see note 6)					1.339.973	1.339.973		1.339.973
Effects of division (see note 7)	(10.000)			(6.484)	(3.555.069)	(3.571.553)	(504.926)	(4.076.479)
Equity at 1.10.2006	183.000	3.996.688	48.250	44.222	(1.468.119)	2.804.041	265.897	3.069.938
Profit for the period 1.10.-31.12.					2.032	2.032	79.125	81.157
Acquisition of minority interest					(57.772)	(57.772)	(345.022)	(402.794)
Transferred to retained earnings		(1.477.137)	(2.500)	(44.222)	1.523.859			
Equity at 31.12.2006	183.000	2.519.551	45.750	0	0	2.748.301	0	2.748.301

The notes on pages 10 to 30 are an integral part of these consolidated financial statements.

In ISK thousands

Consolidated statement of Cash Flows for the year 2006

	Note	2006	2005
Cash flows from operating activities:			
(Loss) profit for the year		(982.540)	635.961
Adjustments for:			
Depreciation and amortisation		480.086	274.303
Impairment losses on goodwill		1.018.560	0
Finance expense		1.744.122	796.414
Share of profit of associates		0	(9.316)
Gain on sale of operating assets		(671.387)	(13.746)
Income tax expense		32.700	154.408
		1.621.541	1.838.024
Change in operational assets and liabilities		(1.243.248)	(152.602)
		378.293	1.685.422
Interest paid		(806.665)	(441.426)
Income tax paid		(110.898)	(72.349)
Net cash (used in) from operating activities		(539.270)	1.171.647
Cash flows from investing activities:			
Dividends received		54.500	0
Proceeds from sale of operating assets		0	11.683
Proceeds from sale of other companies		27.000	119.775
Cash disposed of due to division	7	(425.930)	0
Aquisition of subsidiaries, net of cash acquired	8,9	(1.602.253)	(1.777.401)
Acquisition of operating assets		(297.010)	(260.259)
Acquisition of intangible assets		(77.680)	(63.144)
Change in receivables		(1.125.537)	(201.571)
Net cash used in investing activities		(3.446.910)	(2.170.917)
Cash flows from financing activities:			
Proceeds from issue of share capital from minority interest		0	659.153
Proceeds from loans and borrowings		2.135.206	3.212.590
Change in own shares		(40.046)	(57.172)
Repayment of loans and borrowings		(977.070)	(1.087.699)
Change in current borrowings		472.663	45.648
Dividends paid		(77.200)	(57.510)
Net cash from financing activities		1.513.553	2.715.010
Net change in cash and cash equivalents		(2.472.627)	1.715.740
Cash and cash equivalents at 1 January		2.850.562	1.134.822
Cash and cash equivalents at 31 December		377.935	2.850.562

Consolidated Financial Statements 31 December 2006 In ISK thousands

Consolidated statement of cash flows for the year 2006, contd.:

Investment and financing activities not affecting cash-flow:

	2006	2005
Sale of operating assets	1.123.788	0
Receivables from parent company	(4.933.060)	0
Proceeds from loans and borrowing	10.232.527	0
Repayment of loans and borrowings (non-current)	(1.435.935)	0
Repayment of loans and borrowings (current)	(4.987.320)	0

The notes on pages 10 to 30 are an integral part of these consolidated financial statements.

In ISK thousands

Notes to the Consolidated Financial Statements

1. Reporting entity

Kögun hf. is a company domiciled in Iceland. The address of the Company's registered office is Lynghåls 9, Reykjavík. The consolidated financial statements of the Company as at and for the year ended 31 December 2006 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group's interest in associates. Kögun hf. was divided into two companies on October 1 2006. The company was delisted from the Icelandic Stock Exchange on 22 May 2006. Kögun hf. is a company active in IT service. Kögun hf. is a subsidiary of Teymi hf.

2. Basis of preparation

a. Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by EU. The financial statements were approved by the Board of Directors on 15 February 2007.

b. Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following:
• derivative financial instruments are measured at fair value
• financial instruments at fair value through profit or loss are measured at fair value

c. Functional and presentation currency

These consolidated financial statements are presented in ISK, which is the Company's functional currency. All financial information presented in ISK has been rounded to the nearest thousand.

d. Use of estimates and judgements

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

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

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by the Group's entities.

a. Basis of consolidation

(i) **Subsidiaries**

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) **Transactions eliminated on consolidation**

Intra-group balances, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

b. Foreign currency

(i) **Foreign currency transactions**

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss.

c. Financial instruments

(i) **Non-derivative financial instruments**

Non-derivative financial instruments comprise investments in equity, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs, except as described below. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

A financial instrument is recognised if the Group becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Group's contractual rights to the cash flows from the financial assets expire or if the Group transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Regular way purchases and sales of financial assets are accounted for at trade date, i.e., the date that the Group commits itself to purchase or sell the asset. Financial liabilities are derecognised if the Group's obligations specified in the contract expire or are discharged or cancelled.

Cash and cash equivalents comprise cash balances and marketable securities that are readily convertible to known amounts of cash and are subject to insignificant risk of change in value.

Accounting for finance income and expense is discussed in note 3.o.

Available-for-sale financial assets

The Group's investments in equity securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses, and foreign exchange gains and losses on available-for-sale monetary items, are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to the income statement.

Other

Other non-derivative financial instruments are mesured at amortised cost using the effective interest method, less any impairment losses.

(ii) **Derivative financial instruments**
The Group holds derivative financial instruments to hedge its interest rate risk exposures.

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for through profit and loss.

Fair value hedges
Changes in the fair value of the derivative hedging instrument designated as a fair value hedge are recognised in profit or loss. The hedged item also is stated at fair value in respect of the risk being hedged, with any gain or loss being recognised in profit and loss.

Hedge accounting is not applied at year end 2006.

(iii) **Share capital**
Ordinary shares
Incremental costs directly attributable to issue of ordinary shares and share options are recognised as a deduction from equity.

Repurchase of share capital
When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity.

d. Operating assets

(i) **Recognition and measurement**
Items of operating assets are measured at cost less accumulated depreciation and impairment losses.

(iii) **Depreciation**

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of operating assets.

The estimated useful lives for the current and comparative periods are as follows:

Machinery and equipment	3-8 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

e. Intangible assets

(i) **Goodwill**

Goodwill arises on the acquisition of subsidiaries and associates.

Acquisitions prior to 1 January 2004

As part of its transition to IFRSs, the Group, elected to restate only those business combinations that occurred on or after 1 January 2004. In respect of acquisitions prior to 1 January 2004, goodwill represents the amount recognised under the Group’s previous accounting framework, Icelandic GAAP.

Acquisitions on or after 1 January 2004

For acquisitions on or after 1 January 2004, goodwill represents the excess of the cost of the acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess is negative (negative goodwill), it is recognised immediately in profit or loss.

Acquisitions of minority interests

Goodwill arising on the acquisition of a minority interest in a subsidiary represents the excess of the cost of the additional investment over the carrying amount of the net assets acquired at the date of exchange.

Subsequent measurement

Goodwill is measured at cost less accumulated impairment losses.

(ii) **Other intangible assets**

Other intangible assets that are acquired by the Group, which have finite useful lives, are measured at cost less accumulated amortisation and accumulated impairment losses.

(iii) **Subsequent expenditure**

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in profit or loss when incurred.

(iv) **Amortisation**

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use. The estimated useful lives for the current period are as follows:

Other intangible assets	3-15 years

f. Leased assets

Operating leases are not recognised on the Group's balance sheet.

g. Inventories

Inventories are measured at cost less impairment loss. The cost of inventories is based on the first-in first-out principle, and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition.

h. Impairment

(i) **Financial assets**

A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial asset is calculated by reference to its current fair value.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in profit or loss. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

(ii) **Non-financial assets**

The carrying amounts of the Group's non-financial assets, inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other assets and groups. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

(ii) Contd.:

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. 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.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

i. Interest-bearing loans and borrowings

Interest-bearing loans and borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing loans and borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest basis.

j. Employee benefits

Defined contribution plans

Contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due.

k. Revenue

(i) **Goods sold**

Revenue from the sale of goods is measured at the fair value of the consideration received or receivable, net of returns and allowances, trade discounts and volume rebates. Revenue is recognised when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, and there is no continuing management involvement with the goods.

(iii) **Services**

Revenue from services rendered is recognised in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

l. Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

m. Finance income and expenses

Finance income comprises interest income on funds invested, dividend income, gains on the disposal of available-for-sale financial assets, changes in the fair value of financial assets at fair value through profit or loss, foreign currency gains, and gains on hedging instruments that are recognised in profit or loss. Interest income is recognised as it accrues, using the effective interest method. Dividend income is recognised on the date that the Group's right to receive payment is established.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses, changes in the fair value of financial assets at fair value through profit or loss, impairment losses recognised on financial assets, and losses on hedging instruments that are recognised in profit or loss. All borrowing costs are recognised in profit or loss using the effective interest method.

n. Income tax expense

Income tax expense comprises current and deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that they probably will not reverse in the foreseeable future. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

n. Discontinued operations

A discontinued operation is a component of the Group's business that represents a separate major line of business operations that has been disposed of following the division of Kogun hf. When an operation is classified as a discontinued operation, the comparative income statement is restated as if the operation had been discontinued from the start of the comparative period.

o. Earnings per share

The Group presents basic earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period.

p. Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing related products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Group's primary format for segment reporting is based on business segments.

4. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and / or disclosure purposes based on the following methods. Where applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

b. Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

c. Derivatives

The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds).

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

Segment reporting

5. Segment information is presented in respect of the Group's business segments. The segment format is organized by the nature of the operations and is based on Group's management and internal reporting structure. The Group's operations are solely in Iceland.

   Inter-segment pricing is determined on an arm's length basis.

   Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly interest-bearing loans and borrowings and income tax assets and liabilities.

   Business segments

   Software and related services comprise consultancy services, software development and various related services.

   Hardware and related services comprise retail of goods sold, installation, maintainance and various related services.

   Business segments

	Software	Hardware	Eliminations	Consolidated
Total external revenues	3.970.581	3.340.962		7.311.543
Intersegment revenue	61.499	4.882	(66.381)	0
Total segment revenue	4.032.080	3.345.844	(66.381)	7.311.543
Segment result	597.235	551.312		1.148.547
Discontinued operations				(943.725)
Net finance costs				(1.139.212)
Income tax expense				(48.150)
Loss for the year				(982.540)
Segment assets	15.694.693	4.122.379		19.817.072
Unallocated liabilities				17.068.771

Merger

6. On 1 October 2006 Kögun hf. was merged with its parent company Skoðun ehf.

   Effect of the merger on the financial position of the Group:

Intangible assets	8.980.441
Deferred tax asset	88.924
Trade and other receivables	62.200
Cash and cash equivalents	168.124
Total assets	9.299.689
Loans and borrowings (current)	7.959.716
Total liabilities	7.959.716
Net assets and liabilities	1.339.973

Consolidated Financial Statements 31 December 2006 In ISK thousands

Discontinued operations

7. On 1 October 2006 Kögun hf. was divided in two separate companies; Kögun hf. and Hands Holding hf. Hands Holding hf. took over specific assets and liabilities and a part of equity as specified below. The operations of the part taken over by Hands Holding, for the period 1 January to 30 September 2006, are stated in the income statement as profit or loss from discontinued operations. Comparative figures in the income statement have been restated accordingly.

(Loss) profit from the discontinued operations specifies as follows:	2006 1.1.-30.9.	2005 1.1.-31.12.
Results of discontinued operations:		
Revenue	12.678.023	13.747.917
Expenses	(13.246.067)	(13.148.705)
Results from operating activities	(568.044)	599.212
Net finance expense	(391.131)	(236.489)
Income tax expense	15.450	(54.517)
Results from operating activities, net of income tax	(943.725)	308.206
Cash flows from discontinued operations:		
Net cash (used in) from operating activities	(529.932)	590.516
Net cash used in investing activities	(455.863)	(6.202.628)
Net cash from financing activities	716.125	6.071.517
Net cash (to) from discontinued operations	(269.670)	459.405

Effect of the division on the financial position of the Group:

Operating assets	239.127
Intangible assets	14.043.163
Investment in other companies	2.054
Deferred tax asset	704.266
Inventories and work in progress	476.632
Trade and other receivables	3.057.935
Cash and cash equivalents	425.930
Total assets	18.949.107
Loans and borrowings (non-current)	6.390.542
Loans and borrowings (current)	5.753.508
Trade and other payables	2.728.578
Total liabilities	14.872.628
Net assets and liabilities	4.076.479

Consolidated Financial Statements 31 December 2006 In ISK thousands

Acquisition of subsidiaries

8. On 1 March 2006 the Group acquired 58,7% of the shares in EJS hf. for ISK 1.232.481 in cash. The acquisition had the following effect on the Group's assets and liabilities on acquisition date:

	Pre-aqcuisition carrying amounts	Fair value adjustments	Recognised values on acquisition
Intangible assets	197.107		197.107
Operating assets	526.425	155.487	681.912
Investment in other companies	33.440		33.440
Long-term receivables	2.500		2.500
Deferred tax asset	45.788		45.788
Inventories	289.963		289.963
Trade and other receivables	632.100		632.100
Cash	158.461		158.461
Minority interest	(869)		(869)
Loans and borrowings (non-current)	(428.257)		(428.257)
Deferred income tax liability	(10.353)	(27.988)	(38.341)
Trade and other payables	(615.914)		(615.914)
Net identifiable assets and liabilities	830.391	127.499	957.890
Minority interest			(316.053)
Goodwill on acquisition			590.644
Consideration paid, satisfied in cash			1.232.481
Cash acquired			(158.461)
Net cash outflow			1.074.020

Pre-acquisition carrying amounts were determined based on applicable IFRSs immediately before the acquisition. The values of assets and liabilities recognised on acquisition are their estimated fair values (see note 4 for methods used in determining fair values).

The goodwill recognised on the acquisition is attributable mainly to the skills and technical talent of the acquired business's work force.

9. On 1 January 2006 Kögun hf. established the subsidiary Kögun USA inc. Kögun USA inc. then acquired all the shares in the American company Specialists in Custom Software Inc. The acquisition had the following effect on the Group's assets and liabilities on acquisition date:

	Recognised values on acquisition
Operating assets	8.638
Trade and other receivables	63.475
Cash	7.816
Trade and other payables	(73.583)
Net identifiable assets and liabilities	6.346
Goodwill on acquisition	591.333
Total purchase price	597.679

Consolidated Financial Statements 31 December 2006 20 In ISK thousands

9. contd.:

Satisfied in cash	536.049
Payable on acquisition date	61.630
Total purchase price	597.679

Net cash outflow:

Satisfied in cash	536.049
Cash acquired	(7.816)
Net cash outflow	528.233

On 1 October 2006 Kögun USA inc. was taken over by Hands Holding hf. following the division of Kögun hf. (see note 7).

Other income

10. Other income is specified as follows:	2006	2005
Gain on sale of operating assets	671.858	0
Other services	15.906	0
Total	687.764	0

Personnel expenses

11. Personnel expenses are specified as follows:

Salaries	2.531.397	1.624.154
Contributions to defined contribution plans	313.785	218.971
Other salary-related expenses	245.082	153.108
Total	3.090.264	1.996.233

Personnel expenses are divided between the following income statement items:

Cost of sales	2.390.338	1.638.907
Sales expenses	220.431	9.964
Administrative expenses	479.495	347.362
Total	3.090.264	1.996.233

Auditors' Fees

12. Auditors' fees are specified as follows:	2006
Audit of the financial statements	7.831
Review of interim financial statements	3.650
Other services	12.880
Total auditors' fees	24.361
Thereof remuneration to others than KPMG Iceland	800

Consolidated Financial Statements 31 December 2006 In ISK thousands

Finance income and expense

13. Finance income and expense are specified as follows:

	2006	2005
Interest income on current assets	191.278	147.573
Interest income on non-current assets	39.956	0
Gain on sale of shares	2.000	14.057
Net foreign exchange gain	0	14.589
Net change in fair value of derivatives at fair value through profit or loss	0	209.043
Finance income	233.234	385.262
Interest expense on financial liabilities	978.739	513.889
Impairment and loss on sale of shares	4.539	4.728
Net foreign exchange loss	45.313	0
Net change in fair value of derivatives at fair value through profit or loss	343.855	0
Finance expenses	1.372.446	518.617
Net finance costs	1.139.212	133.355

Income tax expense

14. Income tax recognised in the income statement is specified as follows:

Current tax expense:		
Current period		10.137
Origination and reversal of temporary differences		38.013
Total income tax expense in income statement		48.150

Reconciliation of effective tax rate:

Profit before income tax		9.335
Income tax using the Company's domestic tax rate	18,0%	1.680
Non-deductible expenses	497,8%	46.470
	515,8%	48.150

In ISK thousands

Operating assets

15. Operating assets and their depreciation is specified as follows:

Gross carrying amount	Buildings	Other operating assets	Total
Balance at 1.1.2005	515.890	1.197.974	1.713.864
Acquired through business combinations		54.013	54.013
Effect of merger		49.240	49.240
Additions	68.003	192.256	260.259
Sales and disposals during the year		(34.921)	(34.921)
Effect of movements in exchange rates		(2.564)	(2.564)
Balance at 31.12.2005	583.893	1.455.998	2.039.891
Acquired through business combinations	412.350	118.497	530.847
Effect of merger		3.045	3.045
Additions during the year	18.775	236.074	254.849
Sales and disposals during the year	(1.015.018)	(285.161)	(1.300.179)
Effect of division		(534.143)	(534.143)
Effect of movements in exchange rates	0	87.345	87.345
Balance 31.12.2006	0	1.081.655	1.081.655
Depreciation and impairment losses			
Balance at 1.1.2005	87.977	775.706	863.683
Depreciation	22.413	157.895	180.308
Sales and disposals		(3.907)	(3.907)
Balance 31.12.2005	110.390	929.694	1.040.084
Depreciation	47.483	263.061	310.544
Sales and disposals during the year	(157.873)	(283.820)	(441.693)
Effect of division	0	(295.016)	(295.016)
Balance 31.12.2006	0	613.919	613.919
Carrying amounts			
1.1.2005	427.913	422.268	850.181
31.12.2005	473.503	526.304	999.807
31.12.2006	0	467.736	467.736
Depreciation ratios	4%	12-33%	

Consolidated Financial Statements 31 December 2006 In ISK thousands

Intangible Assets

16. Intangible assets and their amortisation and impairment losses are specified as follows:

Cost	Goodwill	Other intangible assets	Total
Balance at 1 January 2005	10.173.812	487.902	10.661.714
Acquisitions through business combinations	277.860	125.654	403.514
Additions	2.731.265	63.143	2.794.408
Sales and disposals	(1.241.706)		(1.241.706)
Effect of movements in exchange rates	(286.197)	(5.173)	(291.370)
Balance at 31 December 2005	11.655.034	671.526	12.326.560
Acquisitions through business combinations	1.896.030	137.750	2.033.780
Effect of merger	7.225.524	1.954.465	9.179.989
Additions	65.728	54.286	120.014
Sales and disposals	(204.477)	(151.693)	(356.170)
Effect of division	(14.847.085)	(233.451)	(15.080.536)
Effect of foreign exchange movements	654.678	11.480	666.158
Balance at 31 December 2006	6.445.432	2.444.363	8.889.795
Amortisation and impairment losses			
Balance at 1 January 2005		303.431	303.431
Amortisation for the year		62.166	62.166
Balance at 31 December 2005		365.597	365.597
Acquisitions through business combinations		113.285	113.285
Amortisation for the year		217.720	217.720
Impairment loss	1.018.560		1.018.560
Sales and disposals		(126.963)	(126.963)
Effect of division	(1.000.000)	(37.373)	(1.037.373)
Balance at 31 December 2006	18.560	532.266	550.826
Carrying amounts			
1.1.2005	10.173.812	184.471	10.358.283
31.12.2005	11.655.034	305.929	11.960.963
31.12.2006	6.426.872	1.912.097	8.338.969

17. ***Impairment tests for cash-generating units containing goodwill***

For the purpose of impairment testing, goodwill is allocated to the Group's cash-generating units which represent the lowest level within the Group, at which the goodwill is monitored for inernal management purpose. The aggregate amount of goodwill is ISK 6.427 million.

Consolidated Financial Statements 31 December 2006 In ISK thousands

17. contd.:

The recoverable amount of each cash generating unit was based on its value in use and was determined with the assistance of independent valuers. The recoverable value of the units were not lower than the carrying amounts. Value in use was determined by discounting the future cash flows generated from the continuing use of the unit and was based in the following key assumtions:

Cash flows were projected based on actual operating results and the 5-year business plan. Cash flows for a further infinite period were extrapolated using a constant growth rate.

The anticipated annual revenue growth included in the cash flow projections was 7 to 19 percent for the years 2007 to 2011.

The terminal nominal growth was assumed to be 5 percent per annum. The estimate was based on statistical analysis of long-term market price trends adjusted annually for actual experience.

A pre-tax discount rate of 14 percent wast applied in determining the recoverable amount of the units. The discount rate was estimated based on an industry average weighted average cost of capital.

The above estimates are particularly sensitive in the following areas:

An increase of 1 percentage point in the discount rate used would have resulted in impairment loss of ISK 230 million.

Investment in other companies

18. The Group's investment in other companies is specified as follows:	Share	Carrying amount
TM Software hf., Kópavogi	1,7%	25.240
Other companies (9)		8.744
Total		33.984

Long-term receivables

19. Long-term receivables are specified as follows:	2006	2005
Receivables from parent company	4.933.059	0
Other receivables	2.486.715	4.921
Total	7.419.774	4.921

At 31 December 2006 no allowance was conseded for doubtful receivables. No impairment loss was recognised during the year 2006.

The long-term receivables are interest bearing with undecided repayment date.

In ISK thousands

Inventories

20. Inventories are specified as follows:

	2006	2005
Finished goods	245.792	307.096
Work in progress	0	11.198
Total inventories	245.792	318.294

In 2006 the write-down of inventories to net realisable value amounted to ISK 25.040.

Trade and other receivables

21. Trade and other receivables are specified as follows:

Nominal value of trade receivables	1.301.839	3.678.468
Impairment losses of trade receivables	(39.104)	(122.670)
Receivables from parent company	1.206.270	0
Derivatives at fair value through profit and loss	0	209.043
Other receivables	463.877	267.578
Total	2.932.882	4.032.419

Impairment losses have been recognised for doubtful accounts. Impairment losses are determined by management with reference to past default experience. The impairment losses do not represent a final write-off.

The directors believe that the carrying amounts of trade receivables approximates their fair value.

Cash and cash equivalents

22. Cash and cash equivalents are specified as follows:

Bank balance	176.215	1.259.276
Marketable securities	201.720	1.591.286
Cash and cash equivalents in the statement of cash flows	377.935	2.850.562

Equity

Issued capital

23. The nominal value of issued share capital at the beginning of the year amounted ISK 193 million. Following the division of the company the share capital was decreased by ISK 10 million and amounted ISK 183 million at year end.

Share premium and legal reserve

24. Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the company. According to Icelandic Companies Act, 25% of the nominal value of share capital must be held in reserve which can not be paid out as dividend to shareholders.

Consolidated Financial Statements 31 December 2006 In ISK thousands

Earnings per share

25. Basic earnings per share is based on profit attributable to parent company shareholders and the weighted average of equity during the year and indicates earnings on each krona in shares. Diluted earnings per share are the same as basic earnings per share, where purchases options to employees or other persons have not been issued and the Group has not taken out loans that can be converted into equity.

	Continuing operations	Discontd. operations	2006 Total	Continuing operations	Discontd. operations	2005 Total
(Loss) profit attributable to shareholders	(38.815)	(943.725)	(982.540)	327.755	308.206	635.961

Weighted average number of shares:

	2006	2005
Issued shares at 1 January	189.829	190.366
Effect of own shares	2.466	(268)
Effect of division	(2.500)	0
Weighted average number of outstanding shares at 31 December	189.795	190.098

Loans and borrowings

26. **Non-current liabilities:**

Secured bank loans	6.730.153	4.148.345
Unsecured bank loans	4.136.747	4.007.941
Unsecured loan from parent company	3.752.027	0
Total	14.618.927	8.156.286

Current liabilities:

Current portion of non-current liabilities	195.507	372.607
Bank overdraft and other unsecured bank facility	20.117	1.940.686
Total	215.624	2.313.293

Consolidated Financial Statements 31 December 2006 In ISK thousands

27. **Terms and repayment schedule:**

Terms and conditions of outstanding loans were as follows:

	Currency	Average interest rate	Carrying amount
Secured bank loan	EUR	5,9%	2.719.167
Secured bank loan	CHF	4,3%	2.014.302
Secured bank loan	JPY	2,8%	1.018.796
Secured bank loan	USD	7,5%	685.353
Secured bank loan	CAD	6,5%	338.086
Unsecured bank loans	ISK	5,8%	4.286.703
Unsecured loan from parent company	ISK	3,0%	3.752.027
			14.814.434
Bank overdraft	ISK	17,5%	20.117
Total			14.834.551

Inventories and receivables of the subsidiaries have been pledged against debts amounting to ISK 5.732 million.

Repayments of non-current liabilities are specified as follows:

Repayments in 2007	195.507
Repayments in 2008	124.641
Repayments in 2009	3.659.630
Repayments in 2010	142.228
Repayments in 2011	4.000.248
Subsequent repayments	6.692.180
Total	14.814.434

Deferred income tax liabilities and assets

28. Deferred income tax liabilities and tax assets are attributable to the following:

	Liabilities	**Assets**	**Net**
Operating assets	106.562	8.779	115.341
Intangible assets		1.100	1.100
Long term receivables	21.523		21.523
Derivatives	(24.266)		(24.266)
Trade and other receivables	10.071	(956)	9.115
Long term liabilities		(15.852)	(15.852)
Tax loss carry-forwards	(80.832)	(8.280)	(89.112)
Other items	1.647	2.211	3.858
Net tax assets (liabilities)	34.705	(12.998)	21.707

In ISK thousands

Trade and other payables

29. Trade and other payables are specified as follows:

	2006	2005
Trade payables	498.822	285.752
Prepaid income	42.148	39.789
Derivatives at fair value through profit and loss	343.855	0
Other payables	1.327.688	3.530.443
Total trade and other payables	2.212.513	3.855.984

Operating leases

30. ***Lease as lessee***

Operating lease payments are specified as follows:	2006
Less than one year	21.451
Between one and five years	19.980
Total	41.431

The Group leases a number of cars under operating leases. The leases typically run for a period of three years, with an option to renew the lease after that date. Each lease contract is cancellable due to penalty.

Financial instruments and associated risks

31. Exposure to credit, interest rate and currency risk arises in the normal course of the Group's activities. Derivative financial instruments are used to hedge exposure to fluctuation in foreign exchange rates and interest rates.

Credit risk

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis. Credit evaluations are performed periodically and necessary provisions recognised.

Foreign currency risk

The Group is exposed to foreign currency risk on sales of services, purchases of material and supplies, and borrowings that are denominated in a currency other than ISK.

Related parties

32. ***Identity of related parties***

The Group has a related party relationship with its parent company, other subsidiaries of the parent and with its directors and executive officers.

In ISK thousands

32. contd.:

Transactions with management and key personnel

Salaries and benefits of management paid for their work for Group companies, share option agreements and shares in the Company are specified as follows:

	Salaries and benefits
Board of Directors:	
Örn Karlsson, Chairman of the Board	3.100
Vilhjálmur Þorsteinsson	2.000
Gunnlaugur M. Sigmundsson	1.200
Guðmundur Þórðarson	1.200
Ingimundur Sigurpálsson	1.200
Einar Þór Sverrisson	600
Managing directors:	
Bjarni Birgisson	17.724
Gunnlaugur M. Sigmundsson, former MD	24.952
Six other directors	71.930

Other transactions with related parties

During the year ended 31 December 2006, associates (other subsidiaries of the parent company) purchased goods from the Group amounting ISK 165 million and at 31 December 2006 associates owed the Group 1.840 million. The Group purchased services from associates in the amount of ISK 31 million. Receivables from the parent company Teymi amounted to ISK 6.139 million at year end.

Group entities

33. The Company holds three subsidiaries which all are included in the consolidated financial statements. The subsidiaries own three subsidiaries which are also included. The subsidiaries included in the consolidated financial statements are specified as follows:

	Share
Kögurnes ehf., Reykjavík	100,0%
EJS hf., Reykjavík	100,0%
Eskill ehf., Reykjavík	100,0%
Hýsing ehf., Reykjavík	100,0%
Isoft á Íslandi ehf., Reykjavík	100,0%
Skýrr hf., Reykjavík	100,0%

Consolidated Financial Statements 31 December 2006 In ISK thousands

Quarterly Statement

The Group´s quarterly continuing operations were as follows:

	1st quarter	2nd quarter	3rd quarter	4th quarter	Total
Year 2006					
Operating revenues	1.379.523	1.920.448	1.826.990	2.184.582	7.311.543
Operating expenses	(1.196.116)	(1.785.825)	(1.649.834)	(2.218.985)	(6.850.760)
Other income	0	0	470	687.294	687.764
Financial income and expenses.............	(386.113)	(525.628)	273.268	(500.739)	(1.139.212)
Income tax	37.534	67.873	(82.563)	(70.994)	(48.150)
Loss for the year	(165.172)	(323.132)	368.331	81.158	(38.815)
EBITDA	236.521	200.422	244.952	861.068	1.542.963

Consolidated Financial Statements 31 December 2006 In ISK thousands