

HS Orka hf.

Condensed Interim Financial Statements
six months ended 30 June 2012
ISK

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Endorsement by the Board of Directors and the Management

The condensed interim financial statements of HS Orka hf. (the Company) for the period from 1 January to 30 June 2012 are prepared in accordance with the International Accounting Standard, IAS 34, *Interim Financial Reporting*.

According to the statement of comprehensive income, the Company's operating revenue amounted to ISK 3,466 million for the first six months of 2012 (2011: ISK 3,803 million) and the loss for the period amounted to ISK 701 million (2011: ISK 754 million profit). Total comprehensive loss amounted to ISK 700 million (2011: comprehensive income ISK 780 million). According to the statement of financial position, the Company's assets amounted to ISK 43,046 million at the end of June 2012 (at year end 2011: ISK 39,904 million). Equity amounted to ISK 20,395 million at the end of June 2012 (at year end 2011: ISK 16,397 million) or 47.4% of total capital (at year end 2011: 41.1%).

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

To the best knowledge of the Board of Directors and the Management, the Company's condensed interim financial statements are in accordance with International Financial Reporting Standards as adopted by the EU and it is the opinion of the Board of Directors and the Management that the condensed interim financial statements give a true and fair view of the Company's assets, liabilities and financial position as at 30 June 2012, its financial performance, and the changes in cash flows in the period from 1 January to 30 June 2012.

Furthermore, it is the opinion of the Board of Directors and the Management that the condensed interim financial statements and endorsement by the Board of Directors and the Management contain a fair overview of the Company's financial development and performance, its position and describe the main risk factors and uncertainties faced by the Company.

The Board of Directors and the Management of HS Orka hf. have today approved the Company's condensed interim financial statements for the period from 1 January to 30 June 2012 and confirmed by means of their signatures.

Reykjanesbær, 13 August 2012.

The Board of Directors:

Managing Director:

Assistant Managing Director:

Independent Auditors' Review Report

To the Board of Directors of HS Orka hf.

We have reviewed the accompanying condensed statement of financial position of HS Orka hf. as of 30 June 2012 and the related condensed statements of comprehensive income, changes in equity and cash flows for the six-month period then ended and a summary of significant accounting policies and other explanatory information. Management is responsible for the preparation and presentation of this condensed interim financial information in accordance with IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on this condensed 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 condensed interim financial information is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting*.

Reykjavík, 13 August 2012

KPMG ehf.

Condensed Statement of Comprehensive Income for the six months ended 30 June 2012

	Note	2012 Q2	2011 Q2	2012 H1	2011 H1
Operating revenue	5	1.624.361	1.849.929	3.465.830	3.802.882
Production cost and cost of sales		(1.131.387)	(1.148.883)	(2.324.234)	(2.430.970)
Gross profit		492.974	701.046	1.141.596	1.371.912
Other operating expenses	6	(137.017)	(188.528)	(248.139)	(353.408)
Results from operating activities		355.957	512.518	893.457	1.018.504
Finance income		663.906	45.206	141.833	72.569
Finance costs		(171.336)	(907.407)	(514.320)	(1.377.329)
Changes in fair value of derivatives		158.011	(95.143)	63.807	23.116
Changes in fair value of embedded derivatives in sales contracts		(1.989.779)	(1.481.875)	(1.527.918)	1.125.869
Net finance expenses	7	(1.339.198)	(2.439.219)	(1.836.598)	(155.775)
Share of profit of associates		93.932	64.423	53.470	63.740
(Loss) profit before income tax		(889.309)	(1.862.278)	(889.671)	926.469
Income tax		196.648	385.203	188.628	(172.546)
(Loss) profit for the period		(692.661)	(1.477.075)	(701.043)	753.923
Other comprehensive income					
Foreign currency translation difference of associates		(24.579)	7.644	649	26.045
Other comprehensive income for for the period, net of income tax		(24.579)	7.644	649	26.045
Total comprehensive income for the period		(717.240)	(1.469.431)	(700.394)	779.968
Earnings per share					
Basic and diluted (loss) earnings per share		(0,09)	(0,21)	(0,09)	0,11

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

Statement of Financial Position as at 30 June 2012

Assets	Note	30.6.2012	31.12.2011
Operating assets		25.434.354	25.803.349
Operating assets under construction		3.595.779	3.544.465
Intangible assets		987.400	982.699
Investments in associates		558.515	655.608
Investments in other companies		27.075	27.075
Bonds		429.781	405.201
Embedded derivatives in power purchase agreements		2.893.648	4.294.623
Deferred tax asset		688.109	499.481
Prepaid lease and royalty fee		470.597	454.676
Long term receivable		275.215	200.926
Total non-current assets		35.360.473	36.868.103
Inventories		378.030	368.386
Bonds		74.700	70.428
Trade and other receivables		1.088.068	1.125.599
Embedded derivatives in power purchase agreements		39.841	166.784
Short term investments	8	552.103	0
Cash and cash equivalents	9	5.553.258	1.304.713
Total current assets		7.686.000	3.035.910
Total assets		43.046.473	39.904.013
	Note	30.6.2012	31.12.2011
Equity			
Share capital	11	7.841.124	6.962.919
Share premium	11	7.038.856	3.218.660
Translation reserve		298.191	297.542
Revaluation reserve		1.609.051	1.647.187
Retained earnings		3.608.052	4.270.960
Total equity		20.395.274	16.397.268
Liabilities			
Loans and borrowings		16.706.749	17.476.628
Pension obligations		1.701.300	1.576.500
Currency and interest rate swap contracts		661.343	761.614
Total non-current liabilities		19.069.392	19.814.742
Loans and borrowings		2.286.018	2.101.388
Trade and other payables		902.985	1.234.276
Currency and interest rate swap contracts		392.804	356.339
Total current liabilities		3.581.807	3.692.003
Total liabilities		22.651.199	23.506.745
Total equity and liabilities		43.046.473	39.904.013

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

Statement of Changes in Equity for the six months ended 30 June 2012

	Share capital	Share premium	Translation reserve	Revaluation reserve	Reserve for shares in associate	Retained earnings	Total
H1 2011							
Equity at 1 January 2011	6.962.919	3.218.660	296.634	1.723.505	(37.157)	5.131.395	17.295.956
Total comprehensive income			26.045	0	0	753.923	779.968
Revaluation reserve transferred to retained earnings				(38.159)		38.159	0
Equity at 30 June 2011	<u>6.962.919</u>	<u>3.218.660</u>	<u>322.679</u>	<u>1.685.346</u>	<u>(37.157)</u>	<u>5.923.477</u>	<u>18.075.924</u>
H1 2012							
Equity at 1 January 2012	6.962.919	3.218.660	297.542	1.647.187	0	4.270.960	16.397.268
Total comprehensive loss			649	0	0	(701.043)	(700.394)
Revaluation reserve transferred to retained earnings				(38.136)		38.136	0
Share capital increase	878.205	3.820.196					4.698.401
Equity at 31 June 2012	<u>7.841.124</u>	<u>7.038.856</u>	<u>298.191</u>	<u>1.609.051</u>	<u>0</u>	<u>3.608.052</u>	<u>20.395.274</u>

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

Statement of Cash Flows

for the six months ended 30 June 2012

	Note	2012 H1	2011 H1
Cash flows from operating activities			
(Loss) profit for the period .....	(	701.043)	753.923
Adjustments:			
Gain on sale of operating assets .....	(	4.553)	(2.675)
Increase in pension obligations		124.800	104.000
Depreciation and amortization		497.906	486.791
Net finance expenses		1.836.598	155.775
Share of profit of associates .....	(	53.470)	(63.740)
Income tax .....	(	188.628)	172.546
		<u>1.511.610</u>	<u>1.606.620</u>
Inventories, increase .....	(	9.644)	(32.223)
Receivables, decrease (increase)		161.033	(71.745)
Current liabilities, (decrease) increase .....	(	213.727)	50.522
Net cash from operations before interest and taxes		<u>1.449.272</u>	<u>1.553.174</u>
Interest income received		48.575	13.303
Interest and indexation costs paid .....	(	205.797)	(291.502)
Net cash from operating activities		<u>1.292.050</u>	<u>1.274.975</u>
Cash flows from investing activities			
Acquisition of operating assets during the period .....	(	171.759)	(119.313)
Payments for operating assets acquired in prior year .....	(	174.394)	(31.093)
Proceeds from sale of operating assets		5.517	3.200
Acquisition of intangible assets .....	(	14.131)	(7.977)
Acquisition of shares in associates .....	(	10.593)	0
Dividend received from associate		4.855	4.855
Short term investments .....	(	550.000)	0
Proceeds from repayment and sale of bonds		0	634.164
Net cash (used in) provided by investing activities	(	<u>910.505</u>)	<u>483.836</u>
Cash flows from financing activities			
Share capital increase		4.698.401	0
Repayment of borrowings .....	(	863.590)	(941.471)
Net cash provided by (used in) financing activities		<u>3.834.811</u>	<u>(941.471)</u>
Increase in cash and cash equivalents		4.216.356	817.340
Cash and cash equivalents at 1 January		1.304.713	1.043.250
Effect of exchange rate fluctuations on cash held		32.189	6.394
Cash and cash equivalents at 30 June		<u>5.553.258</u>	<u>1.866.984</u>
Investing and financing activities not affecting cash flows			
Acquisition of operating assets		0	(537.187)
Current liabilities		0	537.187
Dividend from associate		156.950	0
Current receivables .....	(	156.950)	0

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

Notes to the Condensed Interim Financial Statements

1. Reporting entity

HS Orka hf. is a limited liability company domiciled in Iceland. The Company's registered office address is Brekkustígur 36, Reykjanesbær, Iceland. The Company generates and sells electricity and hot water for heating. The condensed interim financial statements as at and for the six months ended 30 June 2012 comprises the Company and its interest in associates. The Company is a subsidiary of Magma Energy Sweden AB. The financial statements of the Company are part of the consolidated financial statements of the ultimate parent company Alterra Power Corp., headquartered in Canada.

The Company's financial statements can be found at its website www.hsorka.is and at the website of the Icelandic Stock Exchange; www.nasdaqomxnordic.com.

2. Statement of compliance

This condensed interim financial report has been prepared in accordance with IAS 34 *Interim Financial Reporting*. Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in financial position and performance of the Company since the last annual consolidated financial statements as at and for the year ended 31 December 2011. This condensed consolidated interim financial report does not include all the information required for full annual financial statements prepared in accordance with International Financial Reporting Standards.

These condensed interim financial statements were approved by the Board of Directors on 13. August 2012.

3. Significant accounting policies

The accounting policies applied by the Company in these condensed interim financial statements are the same as those applied by the Company in its financial statements as at and for the year ended 31 December 2011.

These condensed interim financial statements are prepared in Icelandic krona, which is the company's functional currency and all amounts have been rounded to the nearest thousand. They are based on historical cost, except for the following:

- a part of operating assets is recognized at revalued cost, which was the fair value at the revaluation dates of 1.1.2008 and 31.12.2009
- derivative financial instruments are measured at fair value
- embedded derivatives in electric power sales contracts are measured at fair value
- financial instruments at fair value through profit or loss are measured at fair value

4. Use of estimates and judgments

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

In preparing these condensed interim financial statements, the significant judgements made by management in applying the Company's accounting policies and the key source of estimation uncertainty were the same as those that applied to the financial statements as at and for the year ended 31 December 2011.

Notes, continued

5. Segment reporting

The Company has three operating segments that are described below:

Power Production

Includes production and sale of electricity, heating water and fresh water from subterranean steam.

Electricity Sale

Includes purchases and sale of electricity to users other than mass users and power companies.

Other

Includes sale of service, rental of facilities and equipment, and other sales.

	Power production	Electricity sale	Other	Total
1 January - 30 June 2012				
External revenue	1.589.936	1.345.325	530.568	3.465.830
Inter-segment revenue	753.260			753.260
Total segment revenue	2.343.196	1.345.325	530.568	4.219.089
Segment operating results	740.508	130.940	22.008	893.457
Unallocated items				
Net finance expenses				(1.836.598)
Share of profit of associates				53.470
Income tax				188.628
Loss for the period				(701.043)
Segment assets	29.400.946	50.132	566.455	30.017.533
Unallocated assets				13.028.940
Total assets				43.046.473
Unallocated liabilities				22.651.199
Capital expenditures	180.005	865	5.020	185.890
Depreciation and amortization	477.921	2.896	17.089	497.906
1 January - 30 June 2011				
External revenue	2.206.987	1.106.275	489.620	3.802.882
Inter-segment revenue	412.224			412.224
Total segment revenue	2.619.211	1.106.275	489.620	4.215.106
Segment operating results	1.032.410	(44.245)	30.339	1.018.504
Unallocated items				
Net finance income				(155.775)
Share of profit of associates				63.740
Income tax				(172.546)
Profit for the period				753.923
Segment assets	30.039.827	54.770	592.126	30.686.723
Unallocated assets				12.418.751
Total assets				43.105.474
Unallocated liabilities				25.029.550
Capital expenditures	655.509	1.968	7.000	664.477
Depreciation and amortization	463.959	2.725	20.107	486.791

Notes, continued

5. Segment reporting, contd.:

Major customers

Revenues from one customer of the Company's Production segment represents approximately ISK 1,058 million of the Company's total revenues during the period (1.1.2011 - 30.6.2011: ISK 1,678 million).

Revenues from HS Veitur hf. represents ISK 996 million during the period (1.1.2011 - 30.6.2011: ISK 852 million) and relates to segments as follows:

	Power production	Electricity sale	Other	Total
Revenues 1.1. - 30.6.2012	362.640	118.881	514.009	995.530
Revenues 1.1. - 30.6.2011	348.092	101.207	402.370	851.669

6. Other operating expenses

Operating expenses specifies as follows:

	2012 Q2	2011 Q2	2012 H1	2011 H1
Salaries and related expenses	35.965	34.722	79.698	72.682
Change in pension fund commitment	52.845	4.178	50.511	40.559
Administrative expenses	44.372	145.341	110.573	231.643
Depreciation and amortization	3.835	4.287	7.357	8.524
Total operating expenses	<u>137.017</u>	<u>188.528</u>	<u>248.139</u>	<u>353.408</u>

7. Net finance (expenses) income

Net finance (expenses) income specifies as follows:

	2012 Q2	2011 Q2	2012 H1	2011 H1
Interest income on loans and receivables	79.960	23.315	112.980	36.355
Interest income on available for sale securities	0	0	0	3.428
Net foreign exchange gain	570.210	0	0	0
Fair value changes on financial assets through profit and loss	13.736	21.891	28.853	32.786
Total finance income	<u>663.906</u>	<u>45.206</u>	<u>141.833</u>	<u>72.569</u>
Interest expense	(119.409)	(150.606)	(266.978)	(303.267)
Indexation	(51.927)	(94.081)	(99.316)	(115.941)
Net foreign exchange loss	0	(662.720)	(148.026)	(958.121)
Total finance costs	<u>(171.336)</u>	<u>(907.407)</u>	<u>(514.320)</u>	<u>(1.377.329)</u>
Fair value changes of currency and interest rate swap contracts	158.011	(95.143)	63.807	23.116
Fair value changes of embedded derivatives in electric power sale contracts	<u>(1.989.779)</u>	<u>(1.481.875)</u>	<u>(1.527.918)</u>	<u>1.125.869</u>
Net finance expenses	<u>(1.339.198)</u>	<u>(2.439.219)</u>	<u>(1.836.598)</u>	<u>(155.775)</u>

Notes, continued

8. Short term investments

The company has invested in short term securities amounting to 552 million at the end of the period.

9. Restricted cash

At the end of June 2012 cash in the amount of ISK 564 million (USD 4.5 million) (at year end 2011: ISK 554 million) was classified as restricted. The cash is dedicated to pay interest and loan payments on none ISK denominated loans in accordance with a collateral agreement concluded in March 2010 with the Company's lenders.

10. Agreement with banks

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

11. New equity

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

12. Other matters

Litigations and claims

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

Trölladyngja

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