# CU INC.
# CONSOLIDATED FINANCIAL STATEMENTS

**FOR THE YEAR ENDED DECEMBER 31, 2016**

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# MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

Management is responsible for preparing the consolidated financial statements in accordance with International Financial Reporting Standards, which include amounts based on estimates and judgments. Management is also responsible for the preparation of the Management's Discuss and Analysis and ensures that it is consistent with the consolidated financial statements.

Management has established internal accounting and financial reporting control systems, which are subject to periodic review by the Company’s internal auditors, to meet its responsibility for reliable and accurate reporting. Integral to these control systems are a code of ethics and management policies that provide guidance and direction to employees, as well as a system of corporate governance that provides oversight to the Company’s operating, reporting and risk management activities.

The consolidated financial statements are approved by the Board of Directors on the recommendation of the Audit Committee. The Audit Committee is comprised entirely of independent Directors. The Audit Committee meets regularly with management and the independent auditors to review significant accounting and financial reporting matters, to assure that management is carrying out its responsibilities and to review and approve the consolidated financial statements.

PricewaterhouseCoopers LLP, our independent auditors, are engaged to perform an audit of the consolidated financial statements and expresses a professional opinion on the results. The Independent Auditor's Report to the Share Owner appears on the following page. PricewaterhouseCoopers LLP have full and independent access to the Audit Committee and management to discuss their audit and related matters.

[Original signed by N.C. Southern]
Chair & Chief Executive Officer

[Original signed by B.R. Bale]
Senior Vice President & Chief Financial Officer

March 2, 2017

**Independent Auditor's Report**

**To the Share Owner of CU Inc.**

We have audited the accompanying consolidated financial statements of CU Inc. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2016 and December 31, 2015 and the consolidated statements of earnings, comprehensive income, changes in equity and cash flow for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

**Management's responsibility for the consolidated financial statements**
Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's responsibility**
Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated 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 consolidated financial statements.

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

**Opinion**
In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of CU Inc. and its subsidiaries as at December 31, 2016 and December 31, 2015 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

**Chartered Professional Accountants**
Calgary, Alberta

*PricewaterhouseCoopers LLP*
*111 5th Avenue SW, Suite 3100, Calgary, Alberta, Canada T2P 5L3*
*T: +1 403 509 7500, F: +1 403 781 1825, www.pwc.com/ca*

# CONSOLIDATED STATEMENT OF EARNINGS

| *(millions of Canadian Dollars)* | Note | Year Ended December 31 2016 | 2015 |
|---|---|---|---|
| **Revenues** | | | |
| Rendering of services | | **2,573** | 2,371 |
| **Costs and expenses** | | | |
| Salaries, wages and benefits | | **(266)** | (336) |
| Energy transmission and transportation | | **(197)** | (176) |
| Plant and equipment maintenance | | **(163)** | (197) |
| Fuel costs | | **(12)** | (14) |
| Purchased power | | **(68)** | (69) |
| Depreciation and amortization | 8,9 | **(460)** | (389) |
| Franchise fees | | **(205)** | (201) |
| Property and other taxes | | **(60)** | (54) |
| Other | 4 | **(182)** | (193) |
| | | **(1,613)** | (1,629) |
| **Operating profit** | | **960** | 742 |
| Interest income | | **16** | 14 |
| Interest expense | 5 | **(343)** | (245) |
| **Net finance costs** | | **(327)** | (231) |
| **Earnings before income taxes** | | **633** | 511 |
| **Income taxes** | 6 | **(172)** | (199) |
| **Earnings for the year** | | **461** | 312 |

*See accompanying Notes to Consolidated Financial Statements.*

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| *(millions of Canadian Dollars)* | Note | Year Ended December 31<br>2016 | 2015 |
|---|---|---|---|
| **Earnings for the year** | | **461** | 312 |
| **Other comprehensive income, net of income taxes** | | | |
| Items that will not be reclassified to earnings: | | | |
| Re-measurement of retirement benefits (1) | 11 | **3** | 2 |
| **Comprehensive income for the year** | | **464** | 314 |

*(1) Net of income taxes of $(1) million for the year ended December 31, 2016 (2015 - $(1) million).*

*See accompanying Notes to Consolidated Financial Statements.*

# CONSOLIDATED BALANCE SHEET

| *(millions of Canadian Dollars)* | Note | December 31 2016 | 2015 |
|---|---|---|---|
| **ASSETS** | | | |
| **Current assets** | | | |
| Cash | | **25** | 18 |
| Accounts receivable | | **331** | 292 |
| Accounts receivable from parent and affiliate companies | 23 | **28** | 23 |
| Inventories | 7 | **24** | 31 |
| Prepaid expenses and other current assets | | **17** | 18 |
| | | **425** | 382 |
| **Non-current assets** | | | |
| Property, plant and equipment | 8 | **14,040** | 13,475 |
| Intangibles | 9 | **485** | 457 |
| Long-term advances to affiliate company | 23 | **130** | 130 |
| Other assets | | **13** | 13 |
| **Total assets** | | **15,093** | 14,457 |
| **LIABILITIES** | | | |
| **Current liabilities** | | | |
| Bank indebtedness | | **1** | 1 |
| Short-term advances from parent company | 23 | **–** | 26 |
| Accounts payable and accrued liabilities | | **427** | 562 |
| Accounts payable to parent and affiliate companies | 23 | **10** | 12 |
| Other current liabilities | | **7** | 8 |
| Long-term debt | 10 | **150** | – |
| | | **595** | 609 |
| **Non-current liabilities** | | | |
| Deferred income tax liabilities | 6 | **1,076** | 934 |
| Retirement benefit obligations | 11 | **142** | 141 |
| Deferred revenues | 12 | **1,652** | 1,587 |
| Other liabilities | | **4** | 4 |
| Long-term debt | 10 | **7,139** | 6,916 |
| **Total liabilities** | | **10,608** | 10,191 |
| **EQUITY** | | | |
| Equity preferred shares | 13 | **187** | 187 |
| Equity preferred shares to parent company | 13,23 | **79** | 79 |
| **Class A and Class B share owner's equity** | | | |
| Class A and Class B shares | 14 | **1,056** | 1,056 |
| Retained earnings | | **3,163** | 2,944 |
| | | **4,219** | 4,000 |
| **Total equity** | | **4,485** | 4,266 |
| **Total liabilities and equity** | | **15,093** | 14,457 |

*See accompanying Notes to Consolidated Financial Statements.*

[Original signed by N.C. Southern]
DIRECTOR

[Original signed by R.J. Urwin]
DIRECTOR

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| *(millions of Canadian Dollars)* | Note | Class A and Class B Shares | Equity Preferred Shares | Retained Earnings | Accumulated Other Comprehensive Income | Total Equity |
|---|---|---|---|---|---|---|
| December 31, 2014 | | 1,056 | 266 | 2,896 | – | 4,218 |
| Earnings for the year | | – | – | 312 | – | 312 |
| Other comprehensive income | | – | – | – | 2 | 2 |
| Gains on retirement benefits transferred to retained earnings | 11 | – | – | 2 | (2) | – |
| Dividends | 13,14 | – | – | (266) | – | (266) |
| December 31, 2015 | | 1,056 | 266 | 2,944 | – | 4,266 |
| Earnings for the year | | – | – | **461** | – | **461** |
| Other comprehensive income | | – | – | – | **3** | **3** |
| Gains on retirement benefits transferred to retained earnings | 11 | – | – | **3** | **(3)** | – |
| Dividends | 13,14 | – | – | **(245)** | – | **(245)** |
| December 31, 2016 | | **1,056** | **266** | **3,163** | – | **4,485** |

*See accompanying Notes to Consolidated Financial Statements.*

# CONSOLIDATED STATEMENT OF CASH FLOW

| *(millions of Canadian Dollars)* | Note | Year Ended December 31<br>2016 | 2015 |
|---|---|---|---|
| **Operating activities** | | | |
| Earnings for the year | | **461** | 312 |
| Adjustments to reconcile earnings to cash flows from operating activities | 15 | **999** | 933 |
| Changes in non-cash working capital | 15 | **(72)** | 52 |
| **Cash flows from operating activities** | | **1,388** | 1,297 |
| **Investing activities** | | | |
| Additions to property, plant and equipment | | **(966)** | (1,207) |
| Proceeds on disposal of property, plant and equipment | | **7** | 9 |
| Additions to intangibles | | **(74)** | (112) |
| Changes in non-cash working capital | 15 | **(111)** | (87) |
| Other | | **–** | 1 |
| **Cash flows used in investing activities** | | **(1,144)** | (1,396) |
| **Financing activities** | | | |
| Issue of long-term debt | 10 | **375** | 650 |
| Dividends paid on equity preferred shares | 13 | **(10)** | (11) |
| Dividends paid to Class A and Class B share owner | 14 | **(235)** | (255) |
| Interest paid | | **(350)** | (322) |
| Interest received from affiliate company | 23 | **12** | 12 |
| Other | | **(3)** | (6) |
| **Cash flows (used in) from financing activities** | | **(211)** | 68 |
| **Increase (decrease) in cash position** | | **33** | (31) |
| Beginning of year | | **(9)** | 22 |
| **End of year** | 15 | **24** | (9) |

*See accompanying Notes to Consolidated Financial Statements.*

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**DECEMBER 31, 2016**

*(Tabular amounts in millions of Canadian Dollars, except as otherwise noted)*

## 1. THE COMPANY AND ITS OPERATIONS

CU Inc. was incorporated under the laws of Canada and its debt and equity preferred shares are listed on the Toronto Stock Exchange. Its head office and registered office is at 700, 909 - 11th Avenue SW, Calgary, Alberta, T2R 1N6. The Company is controlled by Canadian Utilities Limited, which in turn is principally controlled by ATCO Ltd. and its controlling share owner, the Southern family.

CU Inc. is engaged in the following business activities:

- Electricity (electricity distribution, transmission and infrastructure development); and
- Pipelines & Liquids (natural gas transmission, distribution and infrastructure development).

The consolidated financial statements include the accounts of CU Inc. and its subsidiaries (see Note 20). In these financial statements, "the Company" means CU Inc. and its subsidiaries.

## 2. BASIS OF PRESENTATION

### STATEMENT OF COMPLIANCE

The consolidated financial statements are prepared according to International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and interpretations of the IFRS Interpretations Committee (IFRIC).

The Board of Directors (Board) authorized these consolidated financial statements for issue on March 2, 2017.

### BASIS OF MEASUREMENT

The consolidated financial statements are prepared on a historic cost basis, except for retirement benefit obligations and cash-settled share-based compensation liabilities which are carried at remeasured amounts or fair value. The Company's significant accounting policies are described in Note 24.

Certain comparative figures have been reclassified to conform to the current presentation.

### FUNCTIONAL AND PRESENTATION CURRENCY

The consolidated financial statements are presented in Canadian dollars. Each entity within the Company determines its own functional currency based on the primary economic environment in which it operates.

### USE OF ESTIMATES AND JUDGEMENTS

Management makes estimates and judgments that could significantly affect how policies are applied, amounts in the consolidated financial statements are reported, and contingent assets and liabilities are disclosed. Most often these estimates and judgments concern matters that are inherently complex and uncertain. Judgments and estimates are reviewed on an on-going basis; changes to accounting estimates are recognized prospectively. The significant judgments, assumptions and estimates are described in Note 19.

## 3. SEGMENTED INFORMATION

The Company's operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision Maker (CODM). The CODM is comprised of the Chair and Chief Executive Officer, and five other senior executives.

The accounting policies applied by the segments are the same as those applied by the Company, except for those used in the calculation of adjusted earnings. Intersegment transactions are measured at the exchange amount, as agreed to by the related parties.

Management has determined that the operating subsidiaries in the reportable segments below share similar economic characteristics, as such, they have been aggregated.

### SEGMENT DESCRIPTIONS AND PRINCIPAL OPERATING ACTIVITIES

| | |
|---|---|
| **Electricity** | The Electricity segment includes ATCO Electric Transmission and ATCO Electric Distribution. These business provide regulated electricity transmission, distribution and related infrastructure development in northern and central east Alberta, the Yukon, the Northwest Territories. |
| **Pipelines & Liquids** | The Pipelines & Liquids segment includes ATCO Gas and ATCO Pipelines. These businesses provide integrated natural gas transmission, distribution and related infrastructure development throughout Alberta and in the Lloydminster area of Saskatchewan. |

### SEGMENTED RESULTS

Results by operating segment for the year ended December 31 is shown below.

| **2016**<br>**2015** | **Electricity** | **Pipelines & Liquids** | **Corporate & Other** | **Intersegment Eliminations** | **Consolidated** |
|---|---|---|---|---|---|
| Revenues - external | **1,370** | **1,203** | – | – | **2,573** |
| | 1,245 | 1,126 | – | – | 2,371 |
| Revenues - intersegment | – | – | – | – | – |
| | – | 1 | – | (1) | – |
| Revenues | **1,370** | **1,203** | – | – | **2,573** |
| | 1,245 | 1,127 | – | (1) | 2,371 |
| Operating expenses (1) | **(441)** | **(712)** | – | – | **(1,153)** |
| | (520) | (721) | – | 1 | (1,240) |
| Depreciation and amortization | **(289)** | **(171)** | – | – | **(460)** |
| | (234) | (155) | – | – | (389) |
| Net finance costs | **(219)** | **(108)** | – | – | **(327)** |
| | (132) | (99) | – | – | (231) |
| Earnings before income taxes | **421** | **212** | – | – | **633** |
| | 359 | 152 | – | – | 511 |
| Income taxes | **(114)** | **(58)** | – | – | **(172)** |
| | (136) | (63) | – | – | (199) |
| Earnings for the year | **307** | **154** | – | – | **461** |
| | 223 | 89 | – | – | 312 |
| Adjusted earnings | **317** | **184** | – | – | **501** |
| | 248 | 147 | – | – | 395 |
| Total assets | **9,883** | **5,157** | **134** | **(81)** | **15,093** |
| | 9,612 | 4,715 | 131 | (1) | 14,457 |
| Capital expenditures (2) | **470** | **588** | – | – | **1,058** |
| | 826 | 588 | – | – | 1,414 |

*(1) Includes total costs and expenses, excluding depreciation and amortization expense.*

*(2) Includes additions to property, plant and equipment and intangibles and $18 million of interest capitalized during construction for the year ended December 31, 2016 (2015 - $95 million).*

## ADJUSTED EARNINGS

Adjusted earnings are earnings attributable to Class A and Class B shares after adjusting for:

- the timing of revenues and expenses for rate-regulated activities,
- dividends on equity preferred shares of the Company,
- one-time gains and losses,
- significant impairments, and
- items that are not in the normal course of business or a result of day-to-day operations.

Adjusted earnings are a key measure of segment earnings used by the CODM to assess segment performance and allocate resources. Other accounts in the consolidated financial statements have not been adjusted as they are not used by the CODM for those purposes.

The reconciliation of adjusted earnings and earnings for the year ended December 31 is shown below.

| **2016**<br>**2015** | **Electricity** | **Pipelines & Liquids** | **Corporate & Other** | **Intersegment Eliminations** | **Consolidated** |
|---|---|---|---|---|---|
| Adjusted earnings | **317** | **184** | **–** | **–** | **501** |
| | 248 | 147 | – | – | 395 |
| Restructuring costs | **(4)** | **(5)** | **–** | **–** | **(9)** |
| | (25) | (31) | – | – | (56) |
| Rate-regulated activities | **(11)** | **(30)** | **–** | **–** | **(41)** |
| | (6) | (32) | – | – | (38) |
| Dividends on equity preferred shares | **5** | **5** | **–** | **–** | **10** |
| of the Company | 6 | 5 | – | – | 11 |
| Earnings for the year | **307** | **154** | **–** | **–** | **461** |
| | 223 | 89 | – | – | 312 |

***Restructuring costs***

In 2016, the Company recorded restructuring costs of $9 million, after-tax, that were not in the normal course of business (2015 - $56 million). These costs were primarily related to severance costs associated with staff reductions and lease termination costs.

***Rate-regulated activities***

ATCO Electric and its subsidiaries, ATCO Electric Yukon, Northland Utilities (NWT) and Northland Utilities (Yellowknife), as well as ATCO Gas and ATCO Pipelines are collectively referred to in the consolidated financial statements as utilities.

There is currently no specific guidance under IFRS for rate-regulated entities that the Company is eligible to adopt. In the absence of this guidance, the utilities do not recognize assets and liabilities from rate-regulated activities as may be directed by regulatory decisions. Instead, the utilities recognize revenues in earnings when amounts are billed to customers, consistent with the regulator-approved rate design. Operating costs and expenses are recorded when incurred. Costs incurred in constructing an asset that meet the asset recognition criteria are included in the related property, plant and equipment or intangible asset.

The Company uses standards issued by the Financial Accounting Standards Board (FASB) in the United States as another source of generally accepted accounting principles (GAAP) to account for rate-regulated activities in its internal reporting provided to the CODM. The CODM believes that earnings presented in accordance with the FASB standards are a better representation of the operating results of the Company's rate-regulated activities. Therefore, the Company presents adjusted earnings as part of its segmented disclosures on this basis. Rate-regulated accounting (RRA) standards impact the timing of how certain revenues and expenses are recognized  when compared to non-rate regulated activities, to appropriately reflect the economic impact of a regulators' decisions on revenues.

Rate-regulated accounting differs from IFRS in the following ways:

| | Timing Adjustment | Items | RRA Treatment | IFRS Treatment |
|---|---|---|---|---|
| 1. | Additional revenues billed in current period | Future removal and site restoration costs, finance costs on major transmission capital projects and impact of colder temperatures. | The Company defers the recognition of cash received in advance of future expenditures. | The Company recognizes revenues when amounts are billed to customers and costs when they are incurred. |
| 2. | Revenues to be billed in future periods | Deferred income taxes, transmission access payments, transmission capital deferral and impact of warmer temperatures. | The Company recognizes revenues associated with recoverable costs in advance of future billings to customers. | The Company recognizes costs when they are incurred, but does not recognize their recovery until customer rates are changed and amounts are collected through future billings. |
| 3. | Regulatory decisions received | Regulatory decisions received which relate to current and prior periods. See regulatory decisions below. | The Company recognizes the earnings from a regulatory decision pertaining to current and prior periods when the decision is received. | The Company does not recognize earnings from a regulatory decision when it is received as regulatory assets and liabilities are not recorded under IFRS. |
| 4. | Settlement of regulatory decisions and other items | Settlement of amounts receivable or payable to customers and other items. | The Company recognizes the amount receivable or payable to customers as a reduction in its regulatory assets and liabilities when collected or refunded through future billings. | The Company recognizes earnings when customer rates are changed and amounts are recovered or refunded to customers through future billings. |

The significant timing adjustments as a result of the differences between rate-regulated accounting and IFRS are as follows:

| | 2016 | 2015 |
|---|---|---|
| *Additional revenues billed in current period* | | |
| Future removal and site restoration costs (1) | **60** | 35 |
| Finance costs on major transmission capital projects (2) | **–** | 62 |
| *Revenues to be billed in future periods* | | |
| Deferred income taxes (3) | **(87)** | (158) |
| Impact of temperatures on revenues (4) | **(28)** | (20) |
| *Regulatory decisions received* | **18** | 67 |
| *Settlement of regulatory decisions and other items* | **(4)** | (24) |
| | **(41)** | (38) |

*(1) Removal and site restoration costs are billed to customers over the estimated useful life of the related assets based on forecast costs to be incurred in future periods.*

*(2) Finance costs incurred by ATCO Electric during construction of major transmission capital projects are billed to customers when incurred.*

*(3) Income taxes are billed to customers when paid by the Company.*

*(4) ATCO Gas' customer rates are based on a forecast of normal temperatures. Fluctuations in temperatures may result in more or less revenue being recovered from customers than forecast. Revenues above or below the normal in the current period are refunded to or recovered from customers in future periods.*

**Regulatory decisions received**

Under rate-regulated accounting, the Company recognizes earnings from a regulatory decision pertaining to current and prior periods when the decision is received. A description of the significant regulatory decisions recognized in adjusted earnings in 2016 and 2015 are provided below.

| | Decision | Timing | Amount | Description |
|---|---|---|---|---|
| 1. | ATCO Electric General Tariff Application (GTA) | October 2016 | (19) | The GTA decision covers the operations of ATCO Electric Transmission for 2015, 2016 and 2017 and resulted in final rates that are lower than the approved interim rates from 2015, mainly due to lower approved operating costs. |
| 2. | 2016-2017 Generic Cost of Capital Decision (GCOC) | August 2016 | 1 | The GCOC decision established the return on equity (ROE) and deemed common equity ratios for the utilities for 2016 and 2017. For ATCO Electric Distribution and ATCO Gas, the 2016 GCOC decision only applies to the K factor mechanism and does not apply to the base performance based regulation formula. |
| 3. | 2013-2015 Generic Cost of Capital Decision (2013 GCOC) | March 2015 | (51) | The 2013 GCOC decision established the ROE and deemed common equity ratios for the utilities for 2013 to 2015. The ROE was reduced from 8.75 per cent to 8.30 per cent and the deemed common equity ratios were reduced by one per cent from what was previously approved. |
| 4. | Capital Tracker Decision | March 2015 | (16) | Decisions for the 2013, 2014 and 2015 Capital Tracker applications included approval of incremental funding for substantially all of the Company's applied for Capital Tracker programs. However, the decisions resulted in lower Capital Tracker rates than previously approved due to the AUC requiring the utilities to use the actual cost of debt in the rate determinations, which was lower than the forecast cost of debt that was previously being used. |

## 4. OTHER COSTS AND EXPENSES

Other costs and expenses include rent, utilities and goods and services such as professional fees, contractor costs, technology related expenses, advertising and other general and administrative expenses.

## 5. INTEREST EXPENSE

Interest expense primarily arises from interest on long-term debentures. The components of interest expense are summarized below.

| | 2016 | 2015 |
|---|---|---|
| Long-term debt | **350** | 330 |
| Retirement benefits net interest expense | **3** | 3 |
| Amortization of deferred financing charges | **1** | 1 |
| Other | **7** | 6 |
| | **361** | 340 |
| Less: interest capitalized *(Note 8)* | **(18)** | (95) |
| | **343** | 245 |

Borrowing costs capitalized to property, plant and equipment during 2016 were calculated by applying interest rates ranging from 4.71 per cent to 5.30 per cent to expenditures on qualifying assets (2015 - 4.63 per cent to 5.50 per cent).

## 6. INCOME TAXES

### INCOME TAX EXPENSE

The components of income tax expense are summarized below.

| | 2016 | 2015 |
|---|---|---|
| **Current income tax expense** | | |
| Expenses for the year | **32** | 10 |
| Adjustment in respect of prior years | **(1)** | (1) |
| | **31** | 9 |
| **Deferred income tax expense** | | |
| Reversal of temporary differences | **139** | 123 |
| Amounts relating to change in tax rates | **–** | 67 |
| Adjustment in respect of prior years | **2** | – |
| | **141** | 190 |
| | **172** | 199 |

The reconciliation of statutory and effective income tax expense is as follows:

| | | 2016 | | 2015 |
|---|---|---|---|---|
| Earnings before income taxes | **633** | **%** | 511 | % |
| Income taxes, at statutory rates | **171** | **27.0** | 133 | 26.0 |
| Change in deferred income taxes resulting from increase in provincial corporate tax rate | **–** | **–** | 67 | 13.1 |
| Other | **1** | **0.2** | (1) | (0.2) |
| | **172** | **27.2** | 199 | 38.9 |

#### INCOME TAX ASSETS AND LIABILITIES

Income tax assets and liabilities in the consolidated balance sheet at December 31 are summarized below.

| | Balance Sheet Presentation | 2016 | 2015 |
|---|---|---|---|
| **Income tax assets** | | | |
| Current | Prepaid expenses and other current assets | **5** | 9 |
| **Income tax liabilities** | | | |
| Deferred | Deferred income tax liabilities | **1,076** | 934 |

#### DEFERRED INCOME TAX

The changes in deferred income tax liabilities are as follows:

| Movements | Property, Plant and Equipment | Intangibles | Tax Loss Carry Forwards and Tax Credits | Retirement Benefit Obligations | Other | Total |
|---|---|---|---|---|---|---|
| December 31, 2014 | 719 | 85 | (34) | (34) | 7 | 743 |
| Charge (credit) to earnings | 205 | 16 | (57) | (4) | 30 | 190 |
| Charge to other comprehensive income | – | – | – | 1 | – | 1 |
| Other | – | – | – | 1 | (1) | – |
| December 31, 2015 | 924 | 101 | (91) | (36) | 36 | 934 |
| Charge (credit) to earnings | **120** | **15** | **15** | **(1)** | **(8)** | **141** |
| Charge to other comprehensive income | – | – | – | **1** | – | **1** |
| December 31, 2016 | **1,044** | **116** | **(76)** | **(36)** | **28** | **1,076** |

The Company does not expect any of its deferred income tax liabilities to reverse within the next twelve months.

At the end of 2016, the Company had $281 million of non-capital tax losses and credits which expire between 2033 and 2036. The Company recognized deferred income tax assets of $76 million for these losses and credits.

## 7. INVENTORIES

Inventories at December 31 are comprised of:

| | 2016 | 2015 |
|---|---|---|
| Natural gas and fuel in storage | **9** | 15 |
| Raw materials and consumables | **14** | 15 |
| Work-in-progress | **1** | 1 |
| | **24** | 31 |

For the year ended December 31, 2016, inventories recognized as an expense were $5 million (2015 - $6 million).

## 8. PROPERTY, PLANT AND EQUIPMENT

The Company continues to invest in utility infrastructure in Alberta, particularly in electricity transmission facilities. A reconciliation of the changes in the carrying amount of property, plant and equipment is as follows:

| | Utility Transmission & Distribution | Land and Buildings | Construction Work-in-Progress | Other | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| December 31, 2014 | 12,479 | 547 | 2,305 | 565 | 15,896 |
| Additions | 285 | 10 | 1,016 | – | 1,311 |
| Transfers | 2,710 | 37 | (2,794) | 47 | – |
| Retirements and disposals | (73) | (4) | – | (13) | (90) |
| Transfer to affiliate | – | (10) | (4) | – | (14) |
| December 31, 2015 | 15,401 | 580 | 523 | 599 | 17,103 |
| Additions | **354** | **2** | **690** | **1** | **1,047** |
| Transfers | **688** | **8** | **(736)** | **40** | – |
| Retirements and disposals | **(153)** | **(5)** | **(1)** | **(16)** | **(175)** |
| Transfer to affiliate | – | **(5)** | – | – | **(5)** |
| December 31, 2016 | **16,290** | **580** | **476** | **624** | **17,970** |
| **Accumulated depreciation** | | | | | |
| December 31, 2014 | 3,034 | 122 | – | 204 | 3,360 |
| Depreciation | 327 | 8 | – | 27 | 362 |
| Retirements and disposals | (73) | (4) | – | (13) | (90) |
| Transfer to affiliate | – | (4) | – | – | (4) |
| December 31, 2015 | 3,288 | 122 | – | 218 | 3,628 |
| Depreciation | **380** | **15** | – | **31** | **426** |
| Retirements and disposals | **(101)** | **(5)** | – | **(16)** | **(122)** |
| Transfer to affiliate | – | **(2)** | – | – | **(2)** |
| December 31, 2016 | **3,567** | **130** | – | **233** | **3,930** |
| **Net book value** | | | | | |
| December 31, 2015 | 12,113 | 458 | 523 | 381 | 13,475 |
| December 31, 2016 | **12,723** | **450** | **476** | **391** | **14,040** |

The additions to property, plant and equipment included $18 million of interest capitalized during construction for the year ended December 31, 2016 (2015 - $95 million).

As part of the integration of natural gas transmission service in Alberta, ATCO Pipelines and NOVA Gas Transmission Ltd. exchanged ownership of certain natural gas pipelines and related facilities during 2016. The net book value of assets disposed of was $51 million compared to assets acquired of $65 million, resulting in an increase in the net book value of utility, transmission and distribution assets of $14 million. The net assets acquired were settled in cash.

## 9. INTANGIBLES

Intangible assets consist mainly of computer software not directly attributable to the operation of property, plant and equipment and land rights. A reconciliation of the changes in the carrying amount of intangible assets is as follows:

| | Computer Software | Land Rights | Other | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| December 31, 2014 | 418 | 229 | 9 | 656 |
| Additions | 40 | 73 | – | 113 |
| Disposals | (4) | – | – | (4) |
| December 31, 2015 | 454 | 302 | 9 | 765 |
| Additions | **51** | **24** | – | **75** |
| Disposals | – | **(2)** | – | **(2)** |
| December 31, 2016 | **505** | **324** | **9** | **838** |
| **Accumulated amortization** | | | | |
| December 31, 2014 | 239 | 32 | 2 | 273 |
| Amortization | 35 | 3 | 1 | 39 |
| Disposals | (4) | – | – | (4) |
| December 31, 2015 | 270 | 35 | 3 | 308 |
| Amortization | **41** | **4** | – | **45** |
| December 31, 2016 | **311** | **39** | **3** | **353** |
| **Net book value** | | | | |
| December 31, 2015 | 184 | 267 | 6 | 457 |
| December 31, 2016 | **194** | **285** | **6** | **485** |

## 10. LONG-TERM DEBT

Long-term debt outstanding at December 31 is as follows:

| | Effective Interest Rate | 2016 | 2015 |
|---|---|---|---|
| CU Inc. debentures - unsecured | 4.982% (2015 - 5.046%) | **7,325** | 6,950 |
| *(interest is the average effective interest rate weighted by principal amounts outstanding)* | | | |
| CU Inc. other long-term obligation, due June 2018 - unsecured | 2.700% | **3** | 3 |
| Less: deferred financing charges | | **(39)** | (37) |
| | | **7,289** | 6,916 |
| Less: amounts due within one year | | **(150)** | – |
| | | **7,139** | 6,916 |

***Debenture Issuances***

During 2016, the Company issued $375 million of 3.763 per cent debentures maturing on November 19, 2046 (2015 - $400 million of 3.964 per cent debentures maturing on July 27, 2045 and $250 million of 4.211 per cent debentures maturing on October 29, 2055).

## 11. RETIREMENT BENEFITS

The Company, together with Canadian Utilities Limited and its subsidiary companies, maintains registered defined benefit and defined contribution pension plans for most of its employees. It also provides other post-employment benefits, principally health, dental and life insurance, for retirees and their dependents. The defined benefit pension plans provide for pensions based on employees' length of service and final average earnings. As of 1997, new employees automatically participate in the defined contribution pension plan.

The Company, together with Canadian Utilities Limited and its subsidiary companies, also maintains non-registered, non-funded defined benefit pension plans for certain officers and key employees.

Information about the plans as a whole, in aggregate, can be found in the Canadian Utilities Limited consolidated financial statements for the year ended December 31, 2016.

Contributions to the registered group defined benefit pension plan, which is accounted for as a defined contribution pension plan, are expensed as paid. Other post-employment benefit (OPEB) and non-registered defined benefit pension plans, which the Company funds out of general revenues, are administered on a combined basis with Canadian Utilities Limited and its subsidiary companies. For non-registered defined benefit pensions, the Company is assessed a percentage of the total cost of the plans.

### THE COMPANY'S BENEFIT PLANS

Information about the Company's participation in the group benefit plans is as follows:

| | 2016 | | 2015 | |
|---|---|---|---|---|
| | Pension Benefit Plans | OPEB Plans | Pension Benefit Plans | OPEB Plans |
| **Benefit plan cost** | | | | |
| Defined benefit plans cost | **29** | **5** | 37 | 5 |
| Defined contribution plans cost | **21** | **–** | 24 | – |
| Total cost | **50** | **5** | 61 | 5 |
| Less: Capitalized | **28** | **3** | 35 | 3 |
| Net cost recognized | **22** | **2** | 26 | 2 |
| **Accrued benefit obligations** | | | | |
| Beginning of year | 46 | 95 | 44 | 97 |
| Defined benefit plan cost | **29** | **5** | 37 | 5 |
| Benefit payments | **(4)** | **(3)** | (4) | (3) |
| Contributions to defined benefit plans | **(22)** | **–** | (32) | – |
| Actuarial (gains) losses | **(2)** | **(2)** | 1 | (4) |
| End of year | **47** | **95** | 46 | 95 |

#### WEIGHTED AVERAGE ASSUMPTIONS

The significant assumptions used to determine the benefit plan cost and accrued benefit obligation were as follows:

| | 2016 | | 2015 | |
|---|---|---|---|---|
| | Pension Benefit Plans | OPEB Plans | Pension Benefit Plans | OPEB Plans |
| **Benefit plan cost** | | | | |
| Discount rate for the year | **4.10%** | **4.10%** | 4.00% | 4.00% |
| Average compensation increase for the year [(1)] | **1.50%** | **n/a** | 3.25% | n/a |
| **Accrued benefit obligations** | | | | |
| Discount rate at December 31 | **3.90%** | **3.90%** | 4.10% | 4.10% |
| Long-term inflation rate | **2.00%** | **n/a** | 2.00% | n/a |
| Health care cost trend rate: | | | | |
| Drug costs [(2)] | **n/a** | **5.57%** | n/a | 5.70% |
| Other medical costs | **n/a** | **4.50%** | n/a | 4.50% |
| Dental costs | **n/a** | **4.00%** | n/a | 4.00% |

*(1) The assumed average compensation increase is 1.50 per cent for 2016 to 2018 and 2.50 per cent thereafter.*

*(2) The Company uses a graded drug cost trend rate which assumes a rate of 4.50 per cent in 2024.*

#### FUNDING

An actuarial valuation for funding purposes as of December 31, 2015 was completed in 2016 for the registered defined benefit pension plans. The estimated contribution for 2017 is $22 million. The next actuarial valuation for funding purposes must be completed as of December 31, 2018.

## 12. DEFERRED REVENUES

Deferred revenues from customer contributions and other sources are as follows:

| | 2016 | 2015 |
|---|---|---|
| Customer contributions | **1,638** | 1,587 |
| Other | **14** | – |
| | **1,652** | 1,587 |

#### CUSTOMER CONTRIBUTIONS

Customer contributions for extensions to plant are included in deferred revenues and recognized as revenue over the life of the related asset. Changes in deferred customer contribution revenues are summarized below.

| | 2016 | 2015 |
|---|---|---|
| Beginning of year | 1,587 | 1,454 |
| Receipt of customer contributions | **98** | 177 |
| Amortization | **(47)** | (44) |
| End of year | **1,638** | 1,587 |

## 13. EQUITY PREFERRED SHARES AND EQUITY PREFERRED SHARES TO PARENT COMPANY

### EQUITY PREFERRED SHARES

***Authorized and issued***

Authorized: an unlimited number of Preferred Shares, issuable in series.

| | 2016 | | 2015 | |
|---|---|---|---|---|
| **Issued** | **Shares** | **Amount** | **Shares** | **Amount** |
| **Cumulative Redeemable Preferred Shares** | | | | |
| 4.60% Series 1 | **4,600,000** | **115** | 4,600,000 | 115 |
| 2.24% Series 4 (1) | **3,000,000** | **75** | 3,000,000 | 75 |
| Issuance costs | | **(3)** | | (3) |
| | | **187** | | 187 |

*(1) Effective June 1, 2016, the annual dividend rate for the Series 4 Preferred Shares was reset to 2.24 per cent for the five-year period commencing June 1, 2016. Prior to June 1, 2016, the annual dividend rate was 3.80 per cent.*

***Rights and privileges***

| Preferred shares | Redemption Amount (1) | Quarterly Dividend (2) | Reset Premium (3) | Date Redeemable/ Convertible | Convertible To |
|---|---|---|---|---|---|
| Series 1 | 25.00 | 0.2875 | Does not reset | Currently redeemable | Not convertible |
| Series 4 | 25.00 | 0.1401875 | 1.36% | June 1, 2021 (4) | Series 5 (5) |

*(1) Plus accrued and unpaid dividends.*

*(2) Cumulative, payable quarterly as and when declared by the Board.*

*(3) Dividend rate will reset on the date redeemable/convertible and every five years thereafter at a rate equal to the Government of Canada yield plus the reset premium noted.*

*(4) Redeemable by the Company or convertible by the holder on the date noted and every five years thereafter.*

*(5) If converted, holders will be entitled to receive quarterly floating rate dividends equal to the Government of Canada Treasury Bill yield plus the reset premium noted. Holders have the option to convert back to the original preferred shares series on subsequent redemption dates.*

### EQUITY PREFERRED SHARES TO PARENT COMPANY

***Authorized and issued***

Authorized: an unlimited number of Series Second Preferred Shares, issuable in series.

| | 2016 | | 2015 | |
|---|---|---|---|---|
| **Issued** | **Shares** | **Amount** | **Shares** | **Amount** |
| **Perpetual Cumulative Second Preferred Shares** | | | | |
| 4.00% Series V | **3,176,578** | **79** | 3,176,578 | 79 |

***Rights and Privileges***

The Series V Perpetual Cumulative Second Preferred Shares are redeemable at the option of the Company on October 3, 2017, at the stated value plus accrued and unpaid dividends.

**DIVIDENDS**

Cash dividends declared and paid per share are as follows:

| *(dollars per share)* | 2016 | 2015 |
|---|---|---|
| **Cumulative Redeemable Preferred Shares** | | |
| 4.60% Series 1 | **1.1500** | 1.1500 |
| 2.24% Series 4 | **0.7554** | 0.9500 |
| **Perpetual Cumulative Second Preferred Shares** | | |
| 4.00% Series V | **1.0000** | 1.0000 |

The payment of dividends is at the discretion of the Board and depends on the financial condition of the Company and other factors.

On January 12, 2017, the Company declared first quarter eligible dividends of $0.2875 per Series 1 Preferred Share and $0.1402 per Series 4 Preferred Share.

## 14. CLASS A AND CLASS B SHARES

The number and dollar amount of outstanding Class A non-voting and Class B common shares at December 31, 2016 is shown below.

| | Class A Non-Voting | | Class B Common | | Total | |
|---|---|---|---|---|---|---|
| | Shares | Amount | Shares | Amount | Shares | Amount |
| Authorized: | Unlimited | | Unlimited | | | |
| Issued and outstanding: | | | | | | |
| December 31, 2015 and 2016 | **3,570,322** | **654** | **2,188,262** | **402** | **5,758,584** | **1,056** |

Class A and B shares have no par value.

The Company declared and paid cash dividends of $40.81 per Class A non-voting share and Class B common share during 2016 (2015 - $44.28). The payment of dividends is at the discretion of the Board and depends on the financial condition of the Company and other factors.

## 15. CASH FLOW INFORMATION

**ADJUSTMENTS TO RECONCILE EARNINGS TO CASH FLOWS FROM OPERATING ACTIVITES**

Adjustments to reconcile earnings to cash flows from operating activities are summarized below.

| | 2016 | 2015 |
|---|---|---|
| Depreciation and amortization | **460** | 389 |
| Income taxes | **172** | 199 |
| Contributions by utility customers for extensions to plant | **98** | 177 |
| Amortization of customer contributions | **(47)** | (44) |
| Net finance costs | **327** | 231 |
| Income taxes paid | **(27)** | (18) |
| Other | **16** | (1) |
| | **999** | 933 |

#### CHANGES IN NON-CASH WORKING CAPITAL

The changes in non-cash working capital are summarized below.

| | 2016 | 2015 |
|---|---|---|
| **Operating activities** | | |
| Accounts receivable | **(58)** | 22 |
| Accounts receivable from parent and affiliate companies | **(5)** | 7 |
| Inventories | **3** | – |
| Prepaid expenses and other current assets | **(2)** | 1 |
| Accounts payable and accrued liabilities | **(5)** | 14 |
| Accounts payable to parent and affiliate companies | **(2)** | – |
| Other current liabilities | **(3)** | 8 |
| | **(72)** | 52 |
| **Investing activities** | | |
| Inventories | **1** | 29 |
| Accounts payable and accrued liabilities | **(112)** | (116) |
| | **(111)** | (87) |

#### CASH POSITION

Cash position in the consolidated statement of cash flows at December 31 is comprised of:

| | 2016 | 2015 |
|---|---|---|
| Cash | **25** | 18 |
| Bank indebtedness | **(1)** | (1) |
| Short-term advances from parent company | **–** | (26) |
| | **24** | (9) |

## 16. FINANCIAL INSTRUMENTS

#### FAIR VALUE MEASUREMENT

Financial instruments are measured at amortized cost or fair value. Fair value represents the estimated amounts at which financial instruments could be exchanged between knowledgeable and willing parties in an arm's length transaction. Determining fair value requires management judgment. The valuation methods used to determine the fair value of each financial instrument and its associated level in the fair value hierarchy is described below.

| Financial Instruments | Fair Value Method |
|---|---|
| **Measured at Amortized Cost** | |
| Cash, accounts receivable, accounts receivable from parent and affiliate companies, bank indebtedness, short-term advances from parent company, accounts payable and accrued liabilities and accounts payable to parent and affiliate companies | Assumed to approximate carrying value due to their short-term nature. |
| Long-term advances to affiliate company and long-term debt | Determined using quoted market prices for the same or similar issues. Where the market prices are not available, fair values are estimated using discounted cash flow analysis based on the Company's current borrowing rate for similar borrowing arrangements (Level 2). |

The fair values of the Company's financial instruments measured at amortized cost are as follows:

| Recurring Measurements | Note | 2016 Carrying Value | 2016 Fair Value | 2015 Carrying Value | 2015 Fair Value |
|---|---|---|---|---|---|
| **Financial Assets** | | | | | |
| Long-term advances to affiliate company | 23 | **130** | **166** | 130 | 173 |
| **Financial Liabilities** | | | | | |
| Long-term debt | 10 | **7,289** | **8,193** | 6,916 | 7,638 |

**OFFSETTING FINANCIAL ASSETS**

The following financial assets are subject to offsetting, enforceable master netting arrangements and similar agreements:

| Financial Assets | 2016 Gross Amount | 2016 Gross Amount Offset | 2016 Net Amount Recognized | 2015 Gross Amount | 2015 Gross Amount Offset | 2015 Net Amount Recognized |
|---|---|---|---|---|---|---|
| Accounts receivable | **66** | **(19)** | **47** | 64 | (26) | 38 |

## 17. RISK MANAGEMENT

### FINANCIAL RISKS

The Company is exposed to a variety of risks associated with the use of financial instruments: market risk, credit risk and liquidity risk. The Company's Board is responsible for understanding the principal risks of the Company's business, achieving a proper balance between risks incurred and the potential return to share owners, and confirming there are controls in place to effectively monitor and manage those risks with a view to the long-term viability of the Company. The Board established the Audit Committee to review significant risks associated with future performance, growth and lost opportunities identified by management that could materially affect the Company's ability to achieve its strategic or operational targets. This committee is responsible for confirming that management has procedures in place to mitigate identified risks.

The source of risk exposure and how each is managed is outlined below.

### MARKET RISK

***Foreign exchange risk***

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. The Company is exposed to foreign exchange risk from financial instruments denominated in currencies other than the functional currency of an operation. The majority of this currency risk arises from exposure to the U.S. dollar. The Company offsets foreign exchange volatility in part by entering into foreign currency derivative contracts. The Company's risk management policy is to hedge all material transactions with foreign exchange risks arising from the sale or purchase of goods and services where revenue or the costs to be incurred are denominated in a currency other than the functional currency of the transacting company.

### CREDIT RISK

Credit risk is the risk of financial loss due to a counterparties inability to discharge their contractual obligations to the Company. The Company is exposed to credit risk on its cash and accounts receivable. The exposure to credit risk represents the total carrying amount of these financial instruments in the consolidated balance sheet.

The Company manages its credit risk on cash by investing in instruments issued by credit-worthy financial institutions and in short-term instruments issued by the federal government.

The Company does not have a concentration of credit risk with any counterparty. Accounts receivable credit risk is reduced by a large and diversified customer base and credit security such as letters of credit. The utilities are also able to recover an estimate for doubtful accounts through approved customer rates and to request recovery through customer rates for any losses from retailers beyond the retailer security mandated by provincial regulations. At December 31, 2016, the Company held $208 million in letters of credit for certain counterparty receivables (2015 - $205 million). The Company has also entered into guarantee arrangements with Centrica plc. relating to the retail energy supply functions performed by Direct Energy (see Note 21).

Accounts receivable are non-interest bearing and are generally due in 30 to 90 days. The provision for impairment of credit losses was less than $1 million in 2016 and 2015.

The aging analysis of trade receivables that are past due but not impaired at December 31 is as follows:

| | **2016** | **2015** |
|---|---|---|
| 30 to 90 days | **1** | 1 |
| Greater than 90 days | **1** | 1 |
| | **2** | 2 |

No other impairments have been identified within accounts receivable.

## LIQUIDITY RISK

Liquidity risk is the risk that the Company will not be able to meet its financial obligations associated with its financial liabilities that are settled in cash or another financial asset. Liquidity risk arises from the Company's general funding needs and in the management of its assets, liabilities and capital structure. Cash flow from operations provides a substantial portion of the Company’s cash requirements. Additional cash requirements are met with the use of existing cash balances, bank borrowings and issuance of long-term debt and Class A and B shares. Commercial paper borrowings and short-term bank loans are also used under available credit lines to provide flexibility in the timing and amounts of long-term financing.

### *Lines of credit*

The Company has the following lines of credit that enable it to obtain financing for general business purposes:

| | | | **2016** | | | **2015** |
|---|---|---|---|---|---|---|
| | **Total** | **Used** | **Available** | **Total** | **Used** | **Available** |
| Long-term committed | **900** | **–** | **900** | 900 | – | 900 |
| Uncommitted | **128** | **59** | **69** | 128 | 46 | 82 |
| | **1,028** | **59** | **969** | 1,028 | 46 | 982 |

Long-term committed credit facilities have maturities greater than one year. Uncommitted credit facilities have no set maturity and the lender can demand repayment at any time.

Lines of credit utilized at December 31 are comprised of:

| | **2016** | **2015** |
|---|---|---|
| Current bank indebtedness | **1** | 1 |
| Letters of credit | **58** | 45 |
| | **59** | 46 |

### *Commercial paper*

The Company is authorized to issue $700 million of commercial paper against its long-term committed credit facilities.

***Maturity analysis of financial obligations***

The table below analyzes the remaining contractual maturities at December 31, 2016, of the Company's financial liabilities based on the contractual undiscounted cash flows.

| | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 and thereafter |
|---|---|---|---|---|---|---|
| Bank indebtedness | 1 | – | – | – | – | – |
| Accounts payable and accrued liabilities | 427 | – | – | – | – | – |
| Accounts payable to parent and affiliate companies | 10 | – | – | – | – | – |
| Long-term debt: | | | | | | |
| Principal | 150 | 3 | 480 | 100 | 160 | 6,435 |
| Interest expense | 361 | 353 | 336 | 321 | 303 | 6,331 |
| | 949 | 356 | 816 | 421 | 463 | 12,766 |

## 18. CAPITAL DISCLOSURES

The Company's objectives when managing capital are to:

1. Safeguard the Company's ability to continue as a going concern so it can continue to provide returns to share owners and benefits for other stakeholders.
2. Maintain strong investment-grade credit ratings in order to provide efficient and cost-effective access to funds required for operations and growth.
3. Remain within the capital structure approved by the AUC for the utilities.

The Company considers the impact of the AUC's decisions with respect to the company's subsidiaries, as well as changes in economic conditions and risks impacting its operations, in managing its capital structure. The Company may adjust the dividends paid to the share owner, issue or purchase Class A and Class B shares, and issue or redeem preferred shares, and long-term debt. Financing decisions are based on assessments by management in line with the Company's objectives, with a goal of managing the financial risk to the Company as a whole.

While the utilities have as their objective to be capitalized according to the AUC-approved capital structure, the Company as a whole is not restricted in the same manner. The Company sets its capital structure relative to risk and to meet financial and operational objectives, while factoring in the decisions of the regulator.

The Company also manages capital to comply with the customary covenants on its long-term debt. A common financial covenant for a large portion of the Company's debentures and credit facilities is that total debt divided by total capitalization must be less than 75 per cent. The Company defines total debt as the sum of bank indebtedness and long-term debt (including current portion). It defines total capitalization as the sum of Class A and Class B shares, retained earnings, equity preferred shares, and total debt. Management maintains the debt capitalization ratio well below 75 per cent to sustain access to cost-effective financing.

Debt capitalization does not have standardized meaning under IFRS and might not be comparable to similar measures presented by other companies. Also, the definitions of total debt and total capitalization vary slightly in the Company's debt-related agreements.

The Company's capitalization at December 31 is as follows:

| | 2016 | 2015 |
|---|---|---|
| Bank indebtedness | **1** | 1 |
| Short-term advances from parent company | **–** | 26 |
| Long-term debt | **7,289** | 6,916 |
| Total debt | **7,290** | 6,943 |
| Class A and Class B shares | **1,056** | 1,056 |
| Retained earnings | **3,163** | 2,944 |
| Equity preferred shares | **187** | 187 |
| Equity preferred shares to parent company | **79** | 79 |
| Total equity | **4,485** | 4,266 |
| Total capitalization | **11,775** | 11,209 |
| Debt capitalization | **62%** | 62% |

For the year ended December 31, 2016, the Company complied with externally imposed requirements on its capital, including covenants related to debentures and credit facilities. The Company will continue to assess its capital structure and objectives in light of any future decisions received from the AUC.

## 19. SIGNIFICANT JUDGMENTS, ESTIMATES AND ASSUMPTIONS

Significant judgments, estimates and assumptions made by the Company are outlined below.

### SIGNIFICANT ACCOUNTING JUDGMENTS

***Impairment of long-lived assets***

Indicators of impairment are considered when evaluating whether or not an asset is impaired. Factors which could indicate an impairment exists include: significant underperformance relative to historical or projected operating results, significant changes in the way in which an asset is used or in the Company's overall business strategy, significant negative industry or economic trends, or adverse decisions by regulators. Events indicating an impairment may be clearly identifiable or based on an accumulation of individually insignificant events over a period of time. The Company continually monitors its operating facilities and the markets and business environment in which it operates. Judgments and assessments about conditions and events are made order to conclude whether a possible impairment exists.

***Property, plant and equipment and intangibles***

The Company makes judgments to: assess the nature of the costs to be capitalized and the time period over which they are capitalized in the purchase or construction of an asset; evaluate the appropriate level of componentization where an asset is made up of individual components for which different depreciation and amortization methods and useful lives are appropriate; distinguish major overhauls to be capitalized from repair and maintenance activities to be expensed; and determine the useful lives over which assets are depreciated and amortized.

***Income taxes***

The Company makes judgments with respect to changes in tax legislation, regulations and interpretations thereof. Judgment is also applied to estimating probable outcomes, when temporary differences will reverse, and whether tax assets are realizable.

When tax legislation is subject to interpretation, management periodically evaluates positions taken in tax filings and records provisions where appropriate. The provisions are management's best estimates of the expenditures required to settle the present obligations at the balance sheet date, using a probability weighting of possible outcomes.

### SIGNIFICANT ACCOUNTING ESTIMATES AND ASSUMPTIONS

***Revenue recognition***

An estimate of usage not yet billed is included in revenues from the regulated distribution of natural gas and electricity. The estimate is derived from unbilled gas and electricity distribution services supplied to customers. This estimate is from the date of the last meter reading and uses historical consumption patterns. Management applies judgment to the measure and value of the estimated consumption.

***Useful lives of property, plant and equipment and intangibles***

Useful lives are estimated based on current facts and past experience taking into account the anticipated physical life of the asset, existing long-term sales agreements and contracts, current and forecast demand, and the potential for technological obsolescence.

***Impairment of long-lived assets***

The Company continually monitors its long-lived assets and the markets and business environment in which it operates for indications of asset impairment. Where necessary, the Company estimates the recoverable amount for the cash generating unit (CGU) to determine if an impairment loss is to be recognized. These estimates are based on assumptions, such as the price for which the assets in the CGU could be obtained or future cash flows that will be produced by the CGU, discounted at an appropriate rate. Subsequent changes to these estimates or assumptions could significantly impact the carrying value of the assets in the CGU.

***Retirement benefits***

The Company consults with qualified actuaries when setting the assumptions used to estimate retirement benefit obligations and the cost of providing retirement benefits during the period. These assumptions reflect management's best estimates of the long-term inflation rate, projected salary increases, retirement age, discount rate, health care costs trend rates, life expectancy and termination rates. The discount rate is determined by reference to market yields on high quality corporate bonds. Since the discount rate is based on current yields, it is only a proxy for future yields. Key assumptions used to determine the retirement benefit cost and obligation are shown in Note 11.

***Income taxes***

Management periodically evaluates positions taken in tax filings where tax legislation is subject to interpretation, and records provisions where appropriate. The provisions are management's best estimates of the expenditures required to settle the present obligations at the balance sheet date measured using a probability weighting of possible outcomes.

## 20. SUBSIDIARIES

Principal operating subsidiaries, all of which are wholly owned, are listed below.

| Principal Operating Subsidiaries | Principal Place of Business | Principal Activity |
|---|---|---|
| ATCO Electric | Canada | Electricity transmission, distribution and related infrastructure development |
| ATCO Gas | Canada | Natural gas distribution and related infrastructure development |
| ATCO Pipelines | Canada | Natural gas transmission and related infrastructure development |

## 21. CONTINGENCIES

Measurement inaccuracies occur from time to time on electricity and gas metering facilities. These measurement adjustments are settled between the parties according to the Electricity and Gas Inspections Act (Canada) and related regulations. The AUC may disallow recovery of a measurement adjustment if it finds that controls and timely follow-up are inadequate.

The Company is party to a number of other disputes and lawsuits in the normal course of business. The Company believes that the ultimate liability arising from these matters will have no material impact on the consolidated financial statements.

In 2004, ATCO Gas and ATCO Electric transferred their retail energy supply businesses to Direct Energy. The legal obligations of ATCO Gas and ATCO Electric for the retail functions transferred to Direct Energy, which include the supply of natural gas and electricity to customers as well as billing and customer care, remain if Direct Energy fails to perform. In certain circumstances, the functions will revert to ATCO Gas and/or ATCO Electric, with no refund of the transfer proceeds to Direct Energy.

Centrica plc., Direct Energy's parent company, provided a $300 million guarantee, supported by a $235 million letter of credit for Direct Energy's obligations to ATCO Gas and ATCO Electric under the transaction agreements. However, there can be no assurance that the coverage under these agreements will be adequate to defray all costs that could arise if the obligations are not met.

## 22. COMMITMENTS

In addition to commitments disclosed elsewhere in the financial statements, the Company has entered into a number of operating leases, operating and maintenance agreements and agreements to purchase capital assets. Approximate future undiscounted payments under these agreements are as follows:

| | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 and thereafter |
|---|---|---|---|---|---|---|
| Operating leases | 19 | 18 | 5 | 4 | 4 | 10 |
| Purchase obligations: | | | | | | |
| Operating and maintenance agreements | 247 | 239 | 211 | 73 | 67 | 170 |
| Capital expenditures | 69 | – | – | – | – | – |
| | 335 | 257 | 216 | 77 | 71 | 180 |

## 23. RELATED PARTY TRANSACTIONS

Transactions between the Company and its subsidiaries have been eliminated on consolidation and are not included in this note.

### TRANSACTIONS WITH PARENT COMPANY OR ULTIMATE PARENT

| Transaction | Recorded As | 2016 | 2015 |
|---|---|---|---|
| Rent, aircraft usage and | Other expenses | **19** | 17 |
| licensing fees | Property, plant and equipment | **8** | 9 |
| Interest on short-term advances [(1)] | Interest expense | **1** | 1 |
| Equity preferred share dividends *(Note 13)* | Retained earnings | **3** | 3 |

*(1) The interest rates on short-term advances are based on the Bank of Canada overnight rate plus an applicable spread.*

### TRANSACTIONS WITH AFFILIATE COMPANIES

| Transaction | Recorded As | 2016 | 2015 |
|---|---|---|---|
| Natural gas and electricity distribution, and | Revenues | **60** | 30 |
| management, planning and engineering services | Deferred revenues | **(14)** | – |
| Interest on long-term advances | Interest income | **12** | 12 |
| Purchase of natural gas | Fuel costs | **2** | 2 |

Affiliate companies are subsidiaries of the Company's parent or ultimate parent.

These transactions are in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

In August 2016, ATCO Gas transferred land and buildings to ATCO Real Estate Holdings Ltd., a wholly owned subsidiary of Canadian Utilities Limited, the Company's parent. The land and buildings were transfered for cash consideration of $3 million.

In November 2015, ATCO Electric transferred land and buildings to ATCO Real Estate Holdings Ltd., a wholly owned subsidiary of Canadian Utilities Limited, the Company's parent. The land and buildings were transfered for cash consideration of $9 million.

### RELATED PARTY LOANS AND BALANCES

| Balances | Recorded As | 2016 | 2015 |
|---|---|---|---|
| Receivables from related parties [(1)] | Accounts receivable from parent company | **1** | – |
| | Accounts receivable from affiliate companies | **27** | 23 |
| Short-term advances [(2)] | Short-term advances from parent company | – | 26 |
| Long-term advances [(3)] | Long-term advances to affiliate company | **130** | 130 |
| Payables to related parties [(1)] | Accounts payable to parent company | **9** | 12 |
| | Accounts payable to affiliate companies | **1** | – |
| Equity preferred shares *(Note 13)* | Equity preferred shares to parent company | **79** | 79 |

*(1) Generally due within 30 days or less from the date of the transaction. The amounts outstanding are unsecured, bear no interest and will be settled in cash. No provisions are held against receivables from related parties.*

*(2) Short-term advances are obtained in the normal course of business and are generally due within 30 days or less from the date of the transaction.*

*(3) The effective interest rate on long-term advances, weighted by principal amounts outstanding, was 9.102 per cent in 2016 and 2015. The advances are unsecured and will be settled in cash. No provisions are held against the advances.*

#### KEY MANAGEMENT COMPENSATION

Information on management compensation is shown below.

| | 2016 | 2015 |
|---|---|---|
| Salaries and short-term employee benefits | **3** | 3 |
| Retirement benefits | **1** | 1 |
| Share-based compensation | **4** | (2) |
| | **8** | 2 |

Key management personnel comprise members of executive management and the Board, a total of 10 individuals (2015 - 10 individuals).

## 24. ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

Subsidiaries are consolidated from the date control is obtained until the date control ends. Control exists where the Company has power over the investee, exposure or rights to variable returns from the investee and the ability to use its power over the investee to affect returns.

All intra-group balances and transactions are eliminated on consolidation.

#### REVENUE RECOGNITION

Revenues from the regulated distribution of natural gas and the regulated distribution of electricity include variable and fixed charges. Variable charges are recognized using meter readings on delivery of the commodity to customers and include an estimate of usage not yet billed. Fixed charges are based on the distribution service provided during the period.

Revenues for the use of regulated electricity transmission facilities are based on an annual tariff and are recognized evenly throughout the year.

Revenues from the regulated transmission of natural gas are recognized based on AUC-approved revenue requirement (cost of service).

Certain additions to property, plant and equipment, mainly in the utilities, are made with the assistance of non-refundable cash contributions from customers. These contributions are made when the estimated revenue is less than the cost of providing service or where the customer needs special equipment. Since these contributions will provide customers with on-going access to the supply of natural gas or electricity, they are classified as deferred revenues and are recognized in revenues over the life of the related asset.

#### SHORT-TERM EMPLOYEE BENEFITS

Short-term employee benefits are recognized as an expense in salaries, wages and benefits as employees render service. These benefits include wages, salaries, social security contributions, short-term compensated absences, incentives and non-monetary benefits, such as medical care. Costs for employee services incurred in constructing an asset that meet the asset recognition criteria are included in the related property, plant and equipment or intangible asset.

Termination benefits are recognized as an expense in salaries, wages and benefits at the earlier of when the Company can no longer withdraw the offer of those benefits and when the Company recognizes costs for a restructuring that includes the payment of termination benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer.

### FRANCHISE FEES

Municipal governments charge franchise fees to the utilities for the exclusive right to provide service in their community. These costs are charged to customers through rates approved by the regulator. Franchise fee revenues and expenses are, therefore, recognized separately and are not recorded on a net basis.

### INCOME TAXES

Income taxes are the sum of current and deferred taxes. Income tax is recognized in earnings, except to the extent it relates to items recorded in other comprehensive income (OCI) or in equity.

Current tax is calculated on taxable earnings using rates enacted or substantively enacted at the balance sheet date in the jurisdictions in which the Company operates.

The liability method is used to determine deferred income tax on temporary differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Deferred income tax is calculated using the enacted or substantively enacted tax rates that are expected to apply in the period when the liability is settled or the asset is realized. If expected tax rates change, deferred income taxes are adjusted to the new rates.

Deferred income tax assets and liabilities are not recognized if the temporary differences arise from the initial recognition of goodwill or of other assets and liabilities in a transaction, other than a business combination, that does not affect accounting or taxable earnings. The tax effect of temporary differences from investments in subsidiaries are not accounted for where the Company is able to control the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future. Deferred income tax assets are recognized only when it is probable that future taxable earnings will be available against which the temporary differences can be applied.

Current income tax assets and liabilities are offset where the Company has the legally enforceable right to offset and the Company intends to either settle on a net basis or realize the asset and settle the liability simultaneously.

Deferred income tax assets and liabilities are offset where the Company has a legally enforceable right to set off tax assets and liabilities, and when the deferred income tax assets and liabilities relate to income taxes levied by the same tax authority.

### INVENTORIES

Inventories are valued at the lower of cost or net realizable value. The cost of inventories that are interchangeable is assigned using the weighted average cost method. For inventories that are not interchangeable, cost is assigned using specific identification of their individual costs. Net realizable value is the estimated selling price in the ordinary course of business, less variable selling expenses.

The cost of inventories is comprised of all purchase, conversion and other costs to bring inventories to their present condition and location. Purchase costs consist of the purchase price, import duties, non-recoverable taxes, transport, handling and other costs directly attributable to the purchase of finished goods, materials or services. Conversion costs include direct material and labour costs and a systematic allocation of fixed and variable overheads incurred in converting materials into finished goods.

### PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are recorded at cost less accumulated depreciation and any recognized impairment losses. Cost includes expenditures that are directly attributable to the purchase or construction of the asset, such as materials, labour, borrowing costs incurred during construction, and contracted services. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset only when it is probable that future economic benefits will flow to the Company and the cost can be measured reliably.

Borrowing costs attributable to a construction period of substantial duration are added to the cost of the asset. The effective interest method is used to calculate capitalized interest using specified rates for specific borrowings and a weighted average rate for general borrowings. Interest capitalization starts when borrowing costs and expenditures are incurred at the onset of construction and ends when construction is substantially complete.

The Company allocates the amount initially recognized in property, plant and equipment to its significant components and depreciates each component separately. Assets are depreciated mainly on a straight-line basis over their estimated useful lives. No depreciation is provided on land and construction work-in-progress.

The carrying amount of a replaced asset is derecognized when the cost of replacing the asset is capitalized. When an asset is derecognized, any resulting gain or loss is recorded in earnings.

Depreciation periods for the principal categories of property, plant and equipment are shown in the table below.

| | Useful Life | Average Useful Life | Average Depreciation Rate |
|---|---|---|---|
| Utility transmission and distribution: | | | |
| Electricity transmission equipment | 17 to 66 years | 49 years | 2.0% |
| Electricity distribution equipment | 14 to 103 years | 36 years | 2.8% |
| Gas transmission equipment | 3 to 82 years | 38 years | 2.6% |
| Gas distribution plant and equipment | 10 to 57 years | 41 years | 2.5% |
| Buildings | 1 to 50 years | 34 years | 2.9% |
| Other: | | | |
| Other plant, equipment and machinery | 5 to 50 years | 26 years | 3.8% |

Depreciation methods and the estimated residual values and useful lives of assets are reviewed on an annual basis. Any changes in these accounting estimates are recorded prospectively.

## INTANGIBLES

Intangible assets are recorded at cost less accumulated amortization and any recognized impairment losses. The Company amortizes intangible assets on a straight-line basis over their useful lives. Useful life is not longer than 10 years for computer software and between 60 and 100 years for land rights based on the contractual life of the underlying agreements. Software work-in-progress is not amortized as the software is not available for use.

Amortization methods and useful lives of assets are reviewed annually. Any changes in these accounting estimates are recorded prospectively.

## IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLES

Property, plant and equipment and intangible assets with finite lives are tested for recoverability when events or circumstances indicate a possible impairment. Impairment is assessed at the CGU level, which is the smallest identifiable group of assets that generates independent cash inflows. An impairment loss is recognized in earnings when the CGU's carrying value is higher than its recoverable amount. The recoverable amount is the greater of the CGU's fair value less disposal costs and its value in use. An impairment loss may be reversed in whole or in part if there is objective evidence that a change in the estimated recoverable amount is warranted. A reversal of an impairment loss shall not exceed the carrying amount that would have been determined (net of depreciation) had no impairment loss been recognized for the asset in prior years.

## PROVISIONS

The Company recognizes provisions when:

(i) there is a current legal or constructive obligation as a result of a past event,

(ii) a probable outflow of economic benefits will be required to settle the obligation; and

(iii) a reliable estimate of the obligation can be made.

If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. If discounting is used, the increase in the provision due to the passage of time is recognized in interest expense.

## CONTINGENCIES

A contingent liability is a possible obligation, and a contingent asset is a possible asset, that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Company. A contingent liability may also be a present obligation that arises from past events that is not recognized because it is not probable that an outflow of economic resources will be required to settle the obligation or the amount of the obligation cannot be measured reliably.

Neither contingent liabilities nor assets are recognized in the consolidated financial statements. However, a contingent liability is disclosed, unless the possibility of an outflow of resources is remote. A contingent asset is only disclosed where an inflow of economic benefits is probable.

Management evaluates the likelihood of contingent events based on the probability of exposure to potential loss. Actual results could differ from these estimates.

## FINANCIAL INSTRUMENTS

The Company classifies financial assets when they are first recognized as amortized cost or fair value through profit or loss. Classification is determined based on the Company's business model for managing financial assets and the contractual cash flow characteristics of the financial assets. Financial assets are measured at amortized cost if the financial asset is:

(i) held for the purpose of collecting contractual cash flows, and

(ii) the contractual cash flows of the financial asset solely represent payments of principle and interest.

All other financial assets are classified as fair value through profit or loss.

Financial liabilities are classified as amortized cost or fair value through profit or loss.

### *Amortized cost*

Financial instruments classified as amortized cost are initially measured at fair value and subsequently measured at their amortized cost using the effective interest method.

### *Fair value through profit or loss*

Financial instruments classified as fair value through profit or loss are initially measured at fair value with subsequent changes in fair value recognized in earnings.

### *Transaction costs*

Transaction costs directly attributable to the purchase or issue of financial assets or financial liabilities that are not fair value through profit or loss are added to the fair value of such assets or liabilities when initially recognized. Transaction costs for long-term debt are amortized over the life of the respective financial liability using the effective interest method. The Company's long-term debt and equity preferred shares are presented net of their respective transaction costs.

### *Offsetting financial instruments*

Financial assets and financial liabilities are offset and the net amount is reported in the consolidated balance sheet:

(i) if there is a legally enforceable right to offset the recognized amounts, and

(ii) if the Company intends either to settle on a net basis or to realize the assets and settle the liabilities simultaneously.

***Derecognition of financial instruments***

Financial assets are derecognized:

(i) when the right to receive cash flows from the financial assets has expired or been transferred, and

(ii) the Company has transferred substantially all the risks and rewards of ownership.

Financial liabilities are derecognized when the obligation is discharged, cancelled, or expired.

***Fair value hierarchy***

The Company uses quoted market prices when available to estimate fair value. Models incorporating observable market data, along with transaction specific factors, are also used to estimate fair value. Financial assets and liabilities are classified in the fair value hierarchy according to the lowest level of input that is significant to the fair value measurement. Management's judgment as to the significance of a particular input may affect placement within the fair value hierarchy levels.

The hierarchy is as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Company applies settlement date accounting to the purchases and sales of financial assets. Settlement date accounting means recognizing an asset on the day it is received by the Company and recognizing the disposal of an asset on the day it is delivered by the Company. Any gain or loss on disposal is also recognized on that day.

**IMPAIRMENT OF FINANCIAL INSTRUMENTS**

At each reporting date, the Company assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. If such evidence exists, an impairment loss is recognized in earnings.

Impairment losses on financial assets carried at amortized cost are calculated as the difference between the amortized cost and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. Impairment losses on financial assets carried at amortized cost may be reversed in whole or in part if there is objective evidence that a change in the estimated recoverable amount is warranted. The revised recoverable amount cannot exceed the carrying amount had no impairment charge been recognized in previous periods.

**RETIREMENT BENEFITS**

The Company participates, together with Canadian Utilities Limited and its subsidiary companies, in a registered group defined benefit pension plan (the Group Plan). The assets of the Group Plan are not segregated for each participating entity and are used to provide pensions to all members of this plan. In this circumstance, the Company is required to account for the Group Plan as a defined contribution plan whereby contributions are expensed as paid. Contributions related to current service cost are allocated in proportion to capped pensionable earnings for each company. Contributions related to the amortization of the unfunded liability are allocated in proportion to the corresponding going-concern liability for each company which was established based on the actuarial valuations for funding purposes as of December 31, 2015.

The minimum funding requirements for the Group Plan are comprised of the contributions related to current service cost and the amortization of the unfunded liability as determined by the actuary. The Company does not have any liability to the Group Plan other than the minimum funding requirements of its subsidiaries. In the event of a withdrawal from the Group Plan or the termination of the Group Plan, the companies will still be required to contribute to the Group Plan where such contributions are required under pension regulations.

The Company participates, together with Canadian Utilities Limited and its subsidiary companies, in OPEB and non-registered group defined benefit pension plans. These plans are administered on a combined basis, and the Company accrues for its obligations under these plans. Costs of these benefits are determined using the projected unit credit method and reflect management's best estimates of wage and salary increases, age at retirement and expected health care costs. The Company consults with qualified actuaries when setting the assumptions used to estimate benefit obligations and the cost of providing retirement benefits during the period.

Accrued benefit obligations at the balance sheet date are determined using a discount rate that reflects market interest rates. The rates are equivalent to those on high quality corporate bonds that match the timing and amount of expected benefit payments.

For the non-registered defined benefit pension plans, the Company is assessed a percentage of the total cost of the plans.

For the non-registered defined benefit pension plan and the OPEB plans, gains and losses resulting from changes in assumptions, including the liability discount rate and future compensation rates, used to measure the accrued benefit obligations are recognized in OCI in the period in which they occur. Those gains and losses are then transferred directly to retained earnings.

Employer contributions to the defined contribution pension plans are expensed as employees render service.

For non-registered defined benefit pension plans and OPEB plans, service cost is recognized as an expense in salaries, wages and benefits, and net interest expense is recognized in interest expense. The cost of retirement benefits for registered defined benefit pension plans and defined contribution pension plans is recognized as an expense in salaries, wages and benefits. Past service costs are recognized immediately in earnings in the period of a plan amendment or curtailment. When retirement benefit costs for employee services are incurred in constructing an asset and meet asset recognition criteria, they are included in the related property, plant and equipment or intangible asset.

**RELATED PARTY TRANSACTIONS**

Transactions with related parties in the normal course of business are measured at the exchange amount. Transfers of assets between entities under common control are measured at the carrying amount.

**FOREIGN CURRENCY TRANSLATION**

Transactions denominated in foreign currencies are translated at the exchange rate on the date of the transaction.

### ACCOUNTING STANDARDS AND INTERPRETATIONS NOT YET ADOPTED

Certain new or amended standards or interpretations issued by the IASB or IFRIC do not need to be adopted in the current period. Standards issued, but not yet effective, which the Company anticipates may have a material effect on the consolidated financial statements or note disclosures are described below.

| Standard | Description | Effective Date |
|---|---|---|
| IFRS 15 *Revenue from Contracts with Customers* | This standard replaces IAS 18 *Revenue* and related interpretations. It provides a framework to determine when to recognize revenue and at what amount. It applies to new contracts created on or after the effective date and to existing contracts not yet completed as of the effective date.<br><br>The Company is party to numerous contracts with customers that will be impacted by the new standard. The Company has established a working group to review the adoption of IFRS 15 and education sessions have been, and will continue to be, provided for employees, senior management and the Audit Committee to increase knowledge, awareness and impacts of the standard. Positions papers on issue-specific differences in the new standard are substantially complete and are in discussion with the Company's external auditor. The Company is currently evaluating the impact of the new standard on financial reporting computer systems and internal controls over financial reporting. | Effective for annual periods on or after January 1, 2018. The Company will not early adopt this standard. |
| IFRS 16 *Leases* | This standard replaces IAS 17 *Leases* and related interpretations. It introduces a new approach to lease accounting that requires a lessee to recognize assets and liabilities for the rights and obligations created by leases. It brings most leases on-balance sheet for lessees, eliminating the distinction between operating and finance leases. However, lessor accounting remains similar to previous guidance and the distinction between operating and finance leases is retained.<br><br>The Company has developed a detailed project plan to review and implement the new standard and a working group has been formed to assess its impact. | Effective for annual periods on or after January 1, 2019. The Company will not early adopt this standard. |