



2018 ANNUAL
MD&A and Financial Statements

MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL HIGHLIGHTS

	As at and for the year ended December 31,		
	2018	2017	2016
Revenue ^{(1), (2)}	183,629	154,163	172,940
EBITDA ^{(1), (2)}	122,676	110,055	108,249
Net income (loss) ^{(3), (4)}	2,304	117,383	(13,758)
Preferred dividends	2,452	2,452	3,427
Total assets	1,131,928	1,201,910	1,147,017
Total long-term liabilities	806,887	833,882	785,087

- (1) Comparative figures for 2016 have been adjusted to remove amounts from discontinued operations. Without the adjustment, revenue and EBITDA were \$364,255 and \$130,190, respectively.
- (2) Revenue for 2016 includes proceeds awarded of \$33,288 for Cardinal and the Ontario hydro facilities. In addition, EBITDA for 2016 includes \$2,288 of interest income and \$12,049 of associated operating expenses, which is a net impact of \$23,527 in EBITDA.
- (3) Net income (loss) attributable to the common shareholders includes discontinued operations for applicable periods, but excludes non-controlling interests.
- (4) Net income for 2017 includes a \$128,087 gain on the sale of Värmevärden and 2016 includes a \$2,803 loss on the sale of Bristol Water.

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LEGAL NOTICE

This document is not an offer or invitation for the subscription or purchase of or a recommendation of securities. It does not take into account the investment objectives, financial situation and particular needs of any investors. Before making an investment in Capstone Infrastructure Corporation (the "Corporation"), an investor or prospective investor should consider whether such an investment is appropriate to their particular investment needs, objectives and financial circumstances and consult an investment adviser if necessary.

Caution Regarding Forward-Looking Statements

Certain of the statements contained within this document are forward-looking and reflect management's expectations regarding the future growth, results of operations, performance and business of the Corporation based on information currently available to the Corporation. Forward-looking statements are provided for the purpose of presenting information about management's current expectations and plans relating to the future and readers are cautioned that such statements may not be appropriate for other purposes. These statements use forward-looking words, such as "anticipate", "continue", "could", "expect", "may", "will", "intend", "estimate", "plan", "believe" or other similar words, and include, among other things, statements found in "Results of Operations" and "Financial Position Review". These statements are subject to known and unknown risks and uncertainties that may cause actual results or events to differ materially from those expressed or implied by such statements and, accordingly, should not be read as guarantees of future performance or results. The forward-looking statements within this document are based on information currently available and what the Corporation currently believes are reasonable assumptions, including the material assumptions set out in the management's discussion and analysis of the results of operations and the financial condition of the Corporation ("MD&A") for the year ended December 31, 2018 under the headings "Changes in the Business", "Results of Operations" and "Financial Position Review", as updated in subsequently filed MD&A of the Corporation (such documents are available under the Corporation's SEDAR profile at www.sedar.com).

Other potential material factors or assumptions that were applied in formulating the forward-looking statements contained herein include or relate to the following: that the business and economic conditions affecting the Corporation's operations will continue substantially in their current state, including, with respect to industry conditions, general levels of economic activity, regulations, weather, taxes and interest rates; that the preferred shares will remain outstanding and that dividends will continue to be paid on the preferred shares; that there will be no material delays in the Corporation's wind development projects achieving commercial operation; that the Corporation's power facilities will experience normal wind, hydrological and solar irradiation conditions, and ambient temperature and humidity levels; that there will be no further material changes to the Corporation's facilities, equipment or contractual arrangements; that there will be no material changes in the legislative, regulatory and operating framework for the Corporation's businesses; that there will be no material delays in obtaining required approvals for the Corporation's power facilities; that there will be no material changes in environmental regulations for the power facilities; that there will be no significant event occurring outside the ordinary course of the Corporation's businesses; the refinancing on similar terms of the Corporation's and its subsidiaries' various outstanding credit facilities and debt instruments which mature during the period in which the forward-looking statements relate; that the conversion rights pursuant to the convertible debenture issued in connection with the Ganaraska, Grey Highlands ZEP, Snowy Ridge and Settlers Landing wind facilities are exercised; market prices for electricity in Ontario and the amount of hours that the Cardinal Facility is dispatched; and the price that the Whitecourt Biomass Facility will receive for its electricity production considering the market price for electricity in Alberta, and the Whitecourt Biomass Facility's agreement with Millar Western, which includes sharing mechanisms regarding the price received for electricity sold by the facility.

Although the Corporation believes that it has a reasonable basis for the expectations reflected in these forward-looking statements, actual results may differ from those suggested by the forward-looking statements for various reasons, including: risks related to the Corporation's securities (controlling shareholder; dividends on common shares and preferred shares are not guaranteed; and volatile market price for the Corporation's securities); risks related to the Corporation and its businesses (availability of debt and equity financing; default under credit agreements and debt instruments; geographic concentration; acquisitions, development and integration; environmental, health and safety; changes in legislation and administrative policy; and reliance on key personnel); and risks related to the Corporation's power facilities (power purchase agreements; operational performance; market price for electricity; contract performance and reliance on suppliers; completion of the Corporation's wind development projects; land tenure and related rights; environmental; and regulatory environment).

For a comprehensive description of these risk factors, please refer to the "Risk Factors" section of the Corporation's Annual Information Form dated March 21, 2018, as supplemented by disclosure of risk factors contained in any subsequent annual information form, material change reports (except confidential material change reports), business acquisition reports, interim financial statements, interim management's discussion and analysis and information circulars filed by the Corporation with the securities commissions or similar authorities in Canada (which are available under the Corporation's SEDAR profile at www.sedar.com).

The assumptions, risks and uncertainties described above are not exhaustive and other events and risk factors could cause actual results to differ materially from the results and events discussed in the forward-looking statements. The forward-looking statements within this document reflect current expectations of the Corporation as at the date of this document and speak only as at the date of this document. Except as may be required by applicable law, the Corporation does not undertake any obligation to publicly update or revise any forward-looking statements.

INTRODUCTION

Management's discussion and analysis ("MD&A") summarizes Capstone Infrastructure Corporation's (the "Corporation" or "Capstone") consolidated financial position, operating results and cash flows as at and for the years ended December 31, 2018 and 2017.

This MD&A should be read in conjunction with the accompanying audited consolidated financial statements of the Corporation and notes thereto as at and for the years ended December 31, 2018 and 2017. Additional information about the Corporation, including its Annual Information Form ("AIF") for the year ended December 31, 2017, quarterly financial reports and other public filings of the Corporation are available under the Corporation's profile on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com.

This MD&A is dated March 7, 2019, the date on which this MD&A was approved by the Corporation's Board of Directors.

BASIS OF PRESENTATION

Financial information in this MD&A is prepared in accordance with International Financial Reporting Standards ("IFRS") and amounts are in Canadian thousands of dollars or thousands of share amounts unless otherwise indicated.

Discontinued Operations

On March 3, 2017, Capstone sold its interest in Värmevärden, resulting in the *utilities - district heating* segment being presented as a discontinued operation in the statements of income and cash flows for the year ended December 31, 2017.

Business Acquisition

On December 31, 2017, Capstone acquired the remaining interests in the Glen Dhu and Fitzpatrick wind facilities, resulting in the consolidation of these entities' balances and results with Capstone's other subsidiaries subsequent to December 31, 2017.

Foreign Currency Translation and Presentation

Amounts included in the consolidated financial statements of each entity in the Corporation are measured using the currency of the primary economic environment in which the entity operates ("functional currency"). The consolidated financial statements are presented in Canadian dollars ("presentation currency"), which is Capstone's functional currency. Capstone used a rate of 0.1484 to translate amounts in Swedish Krona relating to the disposal of its interest in Värmevärden. Since the disposal Capstone holds limited amounts of foreign currency.

ADDITIONAL GAAP PERFORMANCE MEASURES DEFINITIONS

While the accompanying consolidated financial statements have been prepared in accordance with IFRS, this MD&A also contains EBITDA, a performance measure not defined by IFRS. EBITDA is an additional GAAP performance measure and does not have a standardized meaning prescribed by IFRS and is, therefore, unlikely to be comparable to similar measures presented by other issuers. The Corporation believes that this indicator is useful since it provides additional information about the Corporation's earnings performance and facilitates comparison of results over different periods. EBITDA is defined as earnings (loss) before financing costs, income tax expense, depreciation and amortization. EBITDA includes earnings (loss) related to the non-controlling interest ("NCI"), interest income, and other gains and losses (net). EBITDA represents Capstone's capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible capital assets and intangible assets, which vary according to their age, technology, and management's estimate of their useful life. EBITDA is presented on the consolidated statement of income.

CHANGES IN THE BUSINESS

In 2018, Capstone was successful in executing a new long-term Electricity Purchase Agreement ("EPA") for the Sechelt Creek facility, in its application to Alberta's extended Bioenergy Producer Program ("BPP") at Whitecourt and in securing Renewable Electricity Support Agreements ("RESA") for the Buffalo Atlee wind development projects.

Sechelt Creek Facility EPA

On February 1, 2018, the Sechelt Creek facility executed a new long-term EPA with BC Hydro, subject to regulatory approval. The new EPA extends to March 1, 2058 at a price lower than the original EPA, which expired on February 28, 2017.

Whitecourt Bioenergy Producer Program

On June 7, 2018, the Government of Alberta approved Whitecourt's application to the BPP. Whitecourt expects to receive grant funding of up to \$9,172 for contributing to Alberta's bioenergy production capacity over the two and a half year program, which ends in March 2020. As at December 31, 2018, Capstone produced enough power to be eligible for \$3,553 of BPP grant funding for the year, of which \$2,821 was received and the remainder is accrued for in revenue.

Project Development

Capstone continues to pursue projects at all stages of development and is actively progressing a number of projects.

On December 17, 2018, Capstone and its partner Sawridge First Nation ("Sawridge") announced that their Buffalo Atlee wind development projects located near Jenner, Alberta (combined 48 MW gross) were selected by the Alberta Electricity System

Operator in a competitive bidding process for the second round of the Renewable Electricity Program. Capstone and Sawridge were awarded and executed three RESA for their Buffalo Atlee 1, 2 and 3 projects (collectively the "Buffalo Atlee" projects).

In addition, Capstone's contracted development pipeline also includes the Riverhurst wind project, a 10 MW facility located in Saskatchewan, which is expected to reach commercial operation ("COD") in 2020.

SUBSEQUENT EVENTS

Watford Wind Facility Acquisition

On February 1, 2019, Capstone acquired the assets of the Watford Wind Facility from Zephyr Farms Limited. The 10MW operating wind facility is located near the municipality of Brooke-Alvinston in Ontario and operates under a power purchase agreement ("PPA") that expires in 2032. Funding for the asset purchase came from existing cash.

RESULTS OF OPERATIONS

Overview

In 2018, Capstone's EBITDA and net income from continuing operations were higher than in 2017. Higher EBITDA from Capstone's continuing operations reflects:

- Higher power segment results, primarily due to Glen Dhu and Fitzpatrick, which were equity accounted investments prior to the acquisition of the remaining ownership interests on December 31, 2017. In addition, higher revenue from Whitecourt, due to higher power rates and production, and Cardinal, due to higher market revenues; and
- Higher interest income from the settlement of a formerly impaired loan receivable; partially offset by
- Declines in the Whitecourt embedded derivative and government grants, which were earned for fewer months than in 2017.

	For the year ended		Change
	Dec 31, 2018	Dec 31, 2017	
Revenue	183,629	154,163	29,466
Expenses	(60,838)	(53,098)	(7,740)
Other income and expenses	(115)	8,990	(9,105)
EBITDA	122,676	110,055	12,621
Interest expense	(38,797)	(36,668)	(2,129)
Depreciation and amortization	(77,967)	(66,787)	(11,180)
Income tax recovery (expense)	(2,015)	(17,541)	15,526
Net income (loss) from continuing operations	3,897	(10,941)	14,838
Net income from discontinued operations	—	129,317	(129,317)
Net income	3,897	118,376	(114,479)

The remaining material changes in net income from Capstone's continuing operations were:

- Higher interest expense, depreciation and amortization, primarily due to Glen Dhu and Fitzpatrick;
- Lower income tax expense, primarily attributable to the sale of Värmevärden in 2017; and
- Lower net income from discontinued operations, primarily reflecting the 2017 gain on sale of Värmevärden.

Results by Segment

Capstone's MD&A discusses the results of the Canadian power segment, as well as the corporate activities. The power segment consists of operating and development activities. The operating facilities produce electricity from natural gas, wind, biomass, hydro and solar resources, and are located in Ontario, Nova Scotia, Alberta, British Columbia and Québec.

Corporate activities primarily comprise growth initiatives, capital structure expenses not specifically attributed to the facilities and costs to manage, oversee and report on the facilities.

The *utilities - district heating* segment is presented as a discontinued operation resulting from Capstone's sale of the investment in 2017.

Revenue

Capstone's revenue is mainly driven by the generation and sale of electricity through long-term power contracts.

Revenue	For the year ended		
	Dec 31, 2018	Dec 31, 2017	Change
Wind ⁽¹⁾	113,566	93,512	20,054
Gas	25,269	21,160	4,109
Hydro	14,333	15,104	(771)
Solar	15,059	15,747	(688)
Biomass	15,402	8,640	6,762
Total Revenue	183,629	154,163	29,466

(1) Wind revenue for 2017 excludes the results of the Glen Dhu and Fitzpatrick wind facilities, which were equity accounted.

Power generated (GWh)	For the year ended		
	Dec 31, 2018	Dec 31, 2017	Change
Wind ⁽¹⁾	1,012.5	827.4	185.1
Gas	78.9	37.4	41.5
Hydro	164.5	176.4	(11.9)
Solar	35.8	36.7	(0.9)
Biomass	191.8	142.5	49.3
Total Power	1,483.5	1,220.4	263.1

(1) Wind production for 2017 excludes the Glen Dhu and Fitzpatrick wind facilities.

Capstone's power segment earns revenue from:

- The wind facilities, which are located in Ontario, Nova Scotia and Québec, by producing and selling electricity in accordance with their PPAs with government agencies or regulated credit-worthy counterparties. On a megawatt ("MW") weighted-average-basis, the wind facilities have 14 years remaining on the current PPAs, with the earliest expiry in 2020.
- Cardinal, a natural gas peaking facility located in Ontario, from fixed payments for providing capacity and availability to the IESO with a 2034 power contract expiry and by supplying electricity to the Ontario grid when it is profitable to do so. In addition, Cardinal receives a fixed amount (subject to escalation) to provide operational and maintenance services to Ingredion's 15MW facility.
- Amherstburg Solar Park, a solar facility located in Ontario, and the four hydro facilities located in Ontario and British Columbia, by generating and selling electricity under long-term PPAs. On a MW weighted-average-basis, the hydro facilities have 28 years remaining on the current PPAs. The Amherstburg Solar Park PPA expires in 2031.
- Whitecourt, a biomass facility located in Alberta, by selling electricity at market rates to the Alberta Power Pool. Whitecourt also earns a portion of its revenue from government grants and the sale of renewable energy credits. These are supplemented or offset by a revenue sharing agreement with Whitecourt's fuel supplier, Millar Western, where contractual settlements are included in other gains and losses in the consolidated statement of income.

The following table shows the significant changes in revenue from 2017:

Change	Explanations
21,485	Higher revenue from Glen Dhu and Fitzpatrick, which were equity accounted investments until December 31, 2017.
6,581	Higher revenue from Whitecourt due to higher Alberta Power Pool prices as well as higher production because of the plant refurbishment in 2017.
3,908	Higher revenue from Cardinal due to more runs as well as higher revenue to operate Ingredion's 15 MW facility, which commenced operations on November 24, 2017.
1,155	Higher revenue from Settlers Landing, which reached COD on April 5, 2017.
(2,574)	Lower revenue from the operating wind facilities (excluding Glen Dhu and Fitzpatrick) due to lower production, reflecting lower wind resources in 2018.
(1,247)	Lower revenue from Whitecourt due to fewer months of BPP funding earned in 2018.
158	Various other changes.
29,466	Change in revenue.

Seasonality

Overall, the results for Capstone's power segment fluctuate during the year because of seasonal factors that affect quarterly production of each facility. These factors include scheduled maintenance and environmental factors such as water flows, solar irradiation, wind speeds and air density, ambient temperature and humidity, which affect the amount of electricity generated. In aggregate, these factors have historically resulted in higher electricity production during the first and fourth quarters.

Expenses

Expenses consist of expenditures within the power segment relating to operating expenses and costs to develop new projects, as well as corporate business development and administrative expenses.

Expenses	For the year ended		
	Dec 31, 2018	Dec 31, 2017	Change
Wind ⁽¹⁾	(22,185)	(16,277)	(5,908)
Gas	(13,666)	(11,487)	(2,179)
Hydro	(4,151)	(4,258)	107
Solar	(1,043)	(961)	(82)
Biomass	(9,343)	(9,307)	(36)
Power operating expenses	(50,388)	(42,290)	(8,098)
Power	(1,602)	(1,557)	(45)
Corporate	(1,319)	(533)	(786)
Project development costs	(2,921)	(2,090)	(831)
Administrative expenses	(7,529)	(8,718)	1,189
Total Expenses	(60,838)	(53,098)	(7,740)

(1) Wind expenses for 2017 excludes the results of the Glen Dhu and Fitzpatrick wind facilities, which were equity accounted.

Expenses for the operation and maintenance ("O&M") of the power facilities mainly consist of wages and benefits and payments to third party providers. The hydro facilities are operated and maintained under an O&M agreement. Capstone's wind facilities are operated by Capstone's staff and maintained under service agreements, typically with the original equipment manufacturers, except for the Erie Shores wind facility, which has an internalized service function. In addition, Cardinal, Whitecourt and Amherstburg rely on the internal capabilities and experience of Capstone's staff. The remaining significant costs include fuel, transportation, insurance, utilities, land leases, raw materials, chemicals, supplies and property taxes.

Project development costs consist of professional fees and other costs to pursue greenfield opportunities, as well as costs to explore and execute transactions. Administrative expenses comprise of staff costs, professional fees for legal, audit and tax, as well as certain office administration and premises costs.

The following table shows the significant changes in expenses from 2017:

Change	Explanations
(4,561)	Higher operating expenses from Glen Dhu, which was an equity accounted investment until December 31, 2017.
(2,808)	Higher operating expenses at Cardinal due to more runs as well as costs to operate Ingridion's 15 MW facility, which commenced operations on November 24, 2017.
(1,125)	Higher operating expenses at SkyGen due to insurance recoveries in 2017.
1,228	Lower staff costs within administrative expenses related to employee separation costs in 2017.
(474)	Various other changes.
<u>(7,740)</u>	<u>Change in expenses.</u>

FINANCIAL POSITION REVIEW

Overview

As at December 31, 2018, Capstone's working capital was \$60,870, compared with \$10,372 as at December 31, 2017. During the year, the SkyGen and Skyway 8 project debt was refinanced, reducing the current portion of long-term debt by \$36,253. In addition, Capstone repaid \$20,915 on the CPC credit facilities and reduced the letters of credit by \$9,047, increasing the available capacity on the CPC credit facilities to \$58,141.

Capstone and its subsidiaries continue to comply with all debt covenants.

Liquidity

Working capital

As at	Dec 31, 2018	Dec 31, 2017
Power	57,306	2,409
Corporate	3,564	7,963
Working capital (equals current assets, less current liabilities)	60,870	10,372

Capstone's working capital was \$50,498 higher than December 31, 2017 due to an increase of \$54,897 for the power segment, partially offset by a \$4,399 decrease at corporate. The power segment increase primarily reflects a decrease in the current portion of long term debt due to a \$36,253 refinancing at SkyGen and Skyway 8. In addition, there was higher cash of \$16,748, higher restricted cash \$694, and lower accruals of \$3,226 due to payments made upon completing the Whitecourt refurbishment.

The remaining difference mainly reflects the use of other assets. The corporate decrease primarily reflects lower cash due to contributions for the Whitecourt refurbishment and, to a lesser extent, the timing of receipts and payments.

Cash and cash equivalents

As at	Dec 31, 2018	Dec 31, 2017
Power	70,574	53,826
Corporate	5,767	10,257
Unrestricted cash and cash equivalents	76,341	64,083

These funds are available for operating activities, capital expenditures and future acquisitions. The \$12,258 increase consists of a \$16,748 increase from the power segment, partially offset by a \$4,490 decrease at corporate. Higher cash at the power segment reflects accumulation of asset distributions, partially offset by the repayment of \$20,915 on the CPC credit facilities. The decrease at corporate reflects contributions to Whitecourt to pay for the refurbishment and settling year-end liabilities. In addition to these funds, the CPC revolving credit facility has an available capacity of \$58,141, as at December 31, 2018.

Cash at the power segment of \$70,574 is only periodically accessible by corporate through distributions. The power segment's cash and cash equivalents are accessible through distributions under the terms of the CPC credit facilities, which allows for distributions, subject to certain conditions. In turn, CPC receives distributions from its subsidiary power assets, which are subject to the terms of their project-specific credit agreements.

Cash flow

Capstone's consolidated cash and cash equivalents increased by \$12,258 in 2018 compared with an increase of \$1,837 in 2017. The components of the change in cash, as presented in the consolidated statement of cash flows, from both continuing and discontinued operations, are summarized as follows:

For the year ended	Dec 31, 2018	Dec 31, 2017
Operating activities	93,098	73,125
Investing activities	(5,508)	(23,040)
Financing activities (excluding dividends to shareholders)	(72,880)	(45,796)
Dividends paid to shareholders	(2,452)	(2,452)
Change in cash and cash equivalents	12,258	1,837

Cash flow from operating activities was \$19,973 higher in 2018, and \$21,345 higher excluding discontinued operations. The increase from continuing operations consists of \$24,458 of higher power segment cash flows, partially offset by \$3,113 of lower corporate cash flows. The increase in power segment cash flows reflects higher revenue from Glen Dhu and Fitzpatrick, which were equity accounted investments in 2017, higher market revenues in response to higher demand at Cardinal, and higher revenue at Whitecourt due to higher prices and production. In addition, there was higher interest income from the settlement of a formerly impaired loan receivable. The decrease in corporate cash flows is primarily attributable to changes in current liabilities. Cash flows from discontinued operations consisted of the Värmevärden results prior to its sale in March 2017.

Cash flow used in investing activities was \$17,532 lower in 2018 primarily due to \$17,443 of lower cash as there was no construction at Settlers Landing in 2018, as well as \$12,004 of lower capital asset additions related to payments for the Whitecourt refurbishment. This was partially offset by a lower release of restricted cash of \$5,989, which resulted from a change to cash funding certain hydro facilities reserves and the release of construction reserves at GHG, Grey Highlands Clean, Snowy Ridge and Settlers Landing in 2017. In addition, the acquisition of the remaining 51% ownership interest in Glen Dhu and Fitzpatrick contributed lower cash of \$3,574 as well as lower dividends from equity accounted investments of \$2,352 in 2018.

Cash flow used in financing activities was \$27,084 higher in 2018, and \$115,114 lower excluding discontinued operations. Cash used in the continuing operations were lower primarily due to a \$131,968 return of capital to Irving Infrastructure Corp. ("Irving") and a \$10,370 cash repayment of the Irving promissory note in 2017, as well as lower debt payments of \$17,855 as a result of the corporate debt refinancing completed in December 2017. These were partially offset by lower proceeds from debt draws of \$46,471 due to the refinancing at SkyGen and Skyway 8 in 2018, compared to the corporate debt refinancing in 2017. Cash flows from discontinued operations in 2017 consisted of \$142,198 of proceeds received on the sale of Värmevärden.

Long-term Debt

Continuity of Capstone's long-term debt for the year ended was:

	Dec 31, 2017	Additions	Repayments	Other	Dec 31, 2018
Long-term debt ^{(1), (2)}	833,690	37,246	(103,277)	906	768,565
Deferred financing fees	(15,148)	(93)	—	1,370	(13,871)
	818,542	37,153	(103,277)	2,276	754,694
Less: current portion of long-term debt ^{(3), (4)}	(86,208)	—	5,000	31,853	(49,355)
	732,334	37,153	(98,277)	34,129	705,339

(1) Repayments of \$103,277 include a \$15,915 repayment for the CPC revolving credit facility, as well as scheduled repayments.

(2) The power segment has a cumulative \$51,168 utilized on its letter of credit facilities.

(3) Repayments are for the CPC term credit facility.

(4) Other reflects a \$36,253 decrease in the current portion due to debt refinancing at SkyGen and Skyway 8.

As at December 31, 2018, Capstone's long-term debt consisted of \$45,000 for the CPC credit facilities and \$723,565 of project debt. The current portion of long-term debt was \$49,355, consisting of scheduled debt amortization. Capstone expects to repay the scheduled amortization from income generated by the power assets. On July 17, 2018, the SkyGen and Skyway 8 project debts were refinanced. The new debt matures in 2021 and amortizes over the same period as the prior debt, carrying a fixed interest rate of 4.90%.

CPC is subject to customary covenants, including specific limitations on leverage and interest coverage ratios. All of the power segment's project debt is non-recourse to Capstone, except for certain limited recourse guarantees provided to the lenders of the various facilities.

Equity

Shareholders' equity comprised:

As at	Dec 31, 2018	Dec 31, 2017
Common shares	62,270	62,270
Preferred shares ⁽¹⁾	72,020	72,020
Share capital	134,290	134,290
Retained earnings	71,842	72,024
Equity attributable to Capstone shareholders	206,132	206,314
Non-controlling interests	50,086	55,249
Total shareholders' equity	256,218	261,563

(1) Capstone has 3,000 publicly listed Series A preferred shares on the Toronto Stock Exchange.

Contractual Obligations

As at December 31, 2018, Capstone had outstanding contractual obligations with amounts due as follows:

	Within one year	One year to five years	Beyond five years	Total
Long-term debt ⁽¹⁾	80,777	353,489	602,333	1,036,599
Operating leases	4,503	18,271	37,013	59,787
Asset retirement obligations	—	—	15,318	15,318
Purchase obligations	14,164	29,104	5,590	48,858
Total contractual obligations	99,444	400,864	660,254	1,160,562

(1) Long-term debt includes principal and interest payments.

Long-term debt

- Long-term debt is discussed on page 8 "Long-term Debt" in this MD&A.

Operating leases

The following leases have been included in the table based on known minimum operating lease commitments:

- Capstone's operating wind facilities and wind development projects have entered into agreements for the use, or option to use, land in connection with the operation of existing and future wind facilities. Payment under these agreements is typically a minimum amount with additional payments dependent on the amount of power generated by the wind facility. The agreements can be renewed and extend as far as 2061.
- Cardinal leases the site on which it is located from Ingredion. Under the lease, Cardinal pays monthly rent. The lease extends through 2034 and expires concurrently with the Energy Savings Agreement between Ingredion and Cardinal.
- Amherstburg leases the land on which its operating facilities are located. The terms of the lease agreements extend to 2036.

- The Corporation has an operating lease for the corporate office ending in 2023.

Capstone's operating lease commitments with no minimum operating lease commitments required are:

- Capstone has agreements with the Provinces of Ontario and British Columbia for the lease of certain lands and water rights necessary for the operation of its hydro power facilities. The payments under these agreements vary based on actual power production. The terms of the lease agreements extend to 2033 and 2042.

Asset retirement obligations

Commitments associated with our asset retirement obligations for Capstone's power facilities are projected to occur principally over the next 25 years.

Purchase obligations

Capstone enters into contractual commitments in the normal course of business, either directly or through its subsidiaries. These contracts include capital commitments and operations and maintenance ("O&M") agreements:

O&M agreements

- Cardinal has a maintenance contract with Siemens Canada Limited covering the gas turbine at Ingredion's 15 MW facility. The contract expires on November 24, 2023.
- Capstone has several service and maintenance agreements covering the turbines in operation on various wind facilities. The agreements provide for scheduled and unscheduled maintenance and require annual minimum payments, subject to inflationary increases, as applicable.
- Capstone has an O&M agreement with Regional Power OPCO Inc. ("Regional") to operate and maintain the hydro power facilities. Regional is paid a monthly management fee and is eligible for an annual incentive fee. The agreement expires on November 30, 2021.

Other commitments

In addition to the commitments included in the table on page 8, Capstone has the following other commitments with no fixed minimum payments:

Power Purchase Agreements

A significant portion of the Corporation's electricity revenue is earned through long-term PPAs. The majority of these contracts include terms and conditions customary to the industry. For Cardinal's contract, the nature of commitments includes: electricity capacity; availability; and production targets. For the remaining power facilities, Capstone is not obligated to deliver electricity; however, in certain circumstances, if a facility fails to meet the performance requirements, the operating facilities' PPA may be terminated after a specified period of time.

Management services agreements

Capstone has agreements with all the partially owned wind facilities and development projects, including Amherst, Saint-Philémon, Goulais, GHG, Snowy Ridge and Settlers Landing. For the operating projects, these agreements are primarily for the provision of management and administration services and are based on an agreed percentage of revenue. The development projects additionally include a development fee for the successful completion of the projects, which pays an agreed fee per MW on completion of development.

Wood waste supply agreement

The Whitecourt and Millar Western fuel supply agreement for wood waste includes sharing mechanisms regarding the price received for electricity sold by Whitecourt.

Energy savings agreement ("ESA")

Cardinal has an ESA with Ingredion which matures on December 31, 2034. Under the terms of the ESA, Cardinal is required to provide O&M services in respect of Ingredion's 15 MW facility, and supply steam and compressed air to Ingredion for the use of its manufacturing facility. Cardinal entered into a maintenance contract with Siemens Canada Limited in connection with the operation and maintenance of the 15 MW plant in order to support Cardinal's satisfaction of the O&M terms of the ESA.

Guarantees

Capstone has provided limited recourse guarantees on the project debt of certain wind projects totalling \$6,000 as at December 31, 2018. Capstone has also provided a guarantee to the former 25% owner of the Grey Highlands Clean wind facility which provides future contractual payments based on operational performance up to a maximum amount of \$4,614. The guarantee terminates when the final payment is made, on or prior to March 21, 2021.

There have been no other significant changes to the specified contractual obligations that are outside the ordinary course of business. Capstone is not engaged in any off-balance sheet financing transactions. Due to the nature of their operations, the Facilities are not expected to incur material contingent liabilities upon the retirement of assets.

Capital Asset Expenditure Program

Capstone incurred \$4,400 of capital asset expenditures during 2018, which included \$3,535 of additions to capital assets and \$865 of additions to projects under development. Capstone's capital expenditures were:

	For the year ended	
	Dec 31, 2018	Dec 31, 2017
Power	4,400	32,305
Corporate	—	45
	<u>4,400</u>	<u>32,350</u>

Income Taxes

In 2018, the current income tax expense was \$270 (2017 - \$371), which primarily relates to current tax on interest income from the settlement of loans receivable.

Capstone's total deferred income tax asset of \$125 primarily relates to unused tax losses carried forward (2017 - nil). Deferred income tax liabilities of \$89,962 (2017 - \$89,243) primarily relate to the differences between the amortization of intangible and capital assets for tax and accounting purposes.

In 2018, Capstone's net deferred income tax liability increased by \$594 primarily due to the utilization of tax losses, partially offset by the differences between accounting and tax amortization claimed during the year.

DERIVATIVE FINANCIAL INSTRUMENTS

Capstone has exposure to market, credit and liquidity risks from its use of financial instruments as described in note 7 financial instruments and note 8 financial risk management in the consolidated financial statements as at and for the year ended December 31, 2018. These notes contain further details on the implicit risks and valuation methodology employed for Capstone's financial instruments.

To manage the certain financial risks inherent in the business, Capstone enters into derivative contracts primarily to mitigate the economic impact of the fluctuations in interest rates. The fair values of these contracts, as well as the Whitecourt embedded derivative included in the consolidated statement of financial position, were:

As at	Dec 31, 2018	Dec 31, 2017
Derivative contract assets	13,851	21,364
Derivative contract liabilities	(2,144)	(2,144)
Net derivative contract assets (liabilities)	<u>11,707</u>	<u>19,220</u>

Net derivative contracts assets decreased by \$7,513 from December 31, 2017, due to losses of \$5,074, and contractual settlement payments of \$2,439 received from Millar Western.

Fair value changes of derivatives in the consolidated statements of income and comprehensive income comprised:

For the year ended	Dec 31, 2018	Dec 31, 2017
Whitecourt embedded derivative	(3,489)	5,396
Interest rate swap contracts	(1,585)	4,534
Gains (losses) on derivatives	<u>(5,074)</u>	<u>9,930</u>

The loss on derivatives were primarily attributable to a lower embedded derivative asset at Whitecourt due to the introduction of Emission Performance Credits ("EPCs"). In addition, losses from the interest rate swap contracts were primarily attributable to lower long-term interest rates since December 31, 2017.

RISKS AND UNCERTAINTIES

Introduction

Risk is an inevitable aspect of operating any business. Decisions that balance risk exposure with intended financial rewards within risk tolerances are the responsibility of the Corporation's management under the supervision of the Board of Directors. When a risk exposure exceeds the Corporation's risk tolerance, the Corporation will, to the extent possible, take steps to eliminate, avoid, reduce or transfer such risk.

The Corporation recognizes the importance and benefits of timely identification, assessment and management of risks that may impact the Corporation's ability to achieve its strategic and financial objectives. In this respect, the Corporation is committed to prudent risk management practices within the context of an enterprise risk management ("ERM") framework. The Corporation maintains a registry of risks that is reviewed by management and the Board of Directors at least quarterly. The Corporation also undertakes an annual comprehensive review of its ERM framework and practices to continuously improve its risk management practices.

What follows is a description of the Corporation's key risk governance and risk processes to support achievement of strategic and financial performance objectives.

Risk Management Principles and Governance

The Corporation's ERM framework is based on five core principles which establish the culture and tone that guide risk management decisions. Risk management is everyone's responsibility, about decision-making, embedded within existing management routines, about people and culture, and specific to each business unit. The Corporation's interpretation of the ERM framework includes the following hierarchy of responsibilities:

- **Board of Directors and Audit Committee** have overall governance responsibility for setting and overseeing management's implementation of the risk management policy.
- **Internal Audit** reports to the Audit Committee and is responsible for reviewing management's practices to manage risks in specific areas agreed from time to time between management and the Audit Committee.
- **Senior Management** is responsible for ensuring the implementation of the ERM framework to all applicable activities and reporting to the Audit Committee.
- **Business Units** are responsible for ensuring the application of a risk management framework to identify, monitor and report risk.
- **Risk Owners** are responsible for the identification and day-to-day management and oversight of risks in their assigned area.



Risk Management Processes

The Corporation's framework relies on the following six key ERM processes to integrate risk management activities with strategic and operational planning, decision-making and day-to-day oversight of business activities.

- **Risk identification** is the process of identifying and categorizing risks that could impact the Corporation's objectives.
- **Risk assessment** is the process of determining the likelihood and impact of the risk. The Corporation uses a five-point rating scale for likelihood and impact.
- **Risk prioritization** is the process of ranking risks as high, medium or low based on the net risk rating as described in the diagram below.
- **Risk management** responses are measures taken to optimize the Corporation's net risk exposure within overall tolerance to achieve the desired balance between risk and reward.
- **Monitoring and reporting** are the processes of assessing the effectiveness of risk management responses.
- **Training and support** ensure that personnel tasked with risk management responsibilities have sufficient knowledge and experience to complete their risk management obligations.

The Corporation's risk management approach is comprehensive. It combines the experience and specialized knowledge of individual business segments and corporate oversight functions as well as various analytic tools and methodologies, including a risk matrix (see chart to the right), to assist the Corporation in regularly assessing and updating the net exposure (including mitigants) of each known material risk facing the Corporation in the following four risk categories: operational; strategic; financial; and legal and regulatory. The Corporation's assessment process prioritizes risks.

		Likelihood of Risk Occurrence				
		Rare	Unlikely	Somewhat Likely	Likely	Almost Certain
		1	2	3	4	5
Impact of Risk	Insignificant					
	Minor					
	Moderate					
	Major					
	Catastrophic					

Managing Risk

The Corporation requires that risk assessments (which encompass operational, strategic, financial and legal and regulatory risks) be performed for the power facilities and at the corporate level.

In addition to these risks, there are numerous other risk factors, many of which are beyond the Corporation's control and the effects of which can be difficult to predict, that could be material to investors or cause the Corporation's results to differ significantly from its plans, objectives and estimates. For a more comprehensive list and description of the risks affecting the Corporation refer to the "Risk Factor" section of the Corporation's most recently filed Annual Information Form, as supplemented by risk factors contained in any of the following documents filed by the Corporation with securities commissions or similar authorities in Canada after the date of this annual MD&A, which are available on SEDAR at www.sedar.com: material change reports; business acquisition reports; interim financial statements; and interim management's discussion and analysis.

Risks Related to the Corporation and its Businesses

Risks that have materially affected the Corporation's financial statements, or that have a reasonable likelihood of affecting them materially in the future, are presented in the table below. Risks specific to Capstone's power segment, as well as at the corporate-level, are included.

Risk and Description	Impact	Monitoring and Mitigation
Operational Risks		
PPA renewal risk concerns the ability to recontract expiring PPAs on economically feasible terms and failing to align with the useful lives of the power facilities.	If Capstone is unsuccessful or delayed in recontracting its expiring PPAs, it would cause Capstone to fall short of its financial forecasts, as revenue short-falls could result from operating in merchant or other markets.	Capstone mitigates by starting negotiations with counter-party(ies) well before contract expiry, considering impacts of other stakeholders and working to ensure the broader benefits of the facility are considered in the process. In addition, company-wide mitigation is provided by maintaining a diversified portfolio to reduce the impact of any one facility to the overall consolidated financial results.
Production risk concerns the dependence of power production on adequate resources such as wind, sunlight and water flow as well as fuel supply and the availability of each of the sites.	Low availability, inadequate wind, sunlight, water flow, wood waste or gas leads to lower power production which results in lower revenues.	Capstone maintains facilities in quality condition to maximize availability for power generation when renewable resources are available and strongest. Capstone also seeks to diversify its portfolio of businesses to mitigate the dependency on a single resource or geography.
Development and capital expenditure risks concern the construction of new power generation facilities in line with the requirements of awarded PPAs and planned maintenance capital expenditures required on existing facilities to maintain operations.	Delays and cost overruns in the construction of new facilities or in performing planned maintenance or refurbishments could lead to lower cash flows, and where PPA requirements are not met, cancellation of the PPA resulting in lost revenue and impairment of any capitalized costs for the facility.	Capstone has professional project management processes and uses experienced contractors and advisors. Capstone contracts include a combination of incentives, liquidated damages, or fixed-pricing to align suppliers interests to project results.
Information technology and data security risk concerns the ability to develop, maintain and manage complex information technology systems which are used to operate and monitor its facilities and other business systems.	Cyber attacks or unauthorized access to information technology systems may lead to production disruptions and system failures that, amongst other things, may result in lower production and revenues.	Capstone follows a recognized IT framework which includes security and recovery plans. In addition, certain sites are compliant with North American Electric Reliability Corporation standards.
Succession and human resources retention risks concern the ability to replace senior management and attract, retain and motivate key staff.	Inability to retain or replace key staff or senior management could prevent or delay Capstone from executing its business strategy, thereby causing Capstone to fall short of its financial forecasts.	Capstone mitigates this risk by having a detailed succession plan and providing related career and development opportunities to its employees.
Strategic Risks		
Competition risk concerns the ability to source and complete attractive investment opportunities that support Capstone's growth initiatives within the power segment.	Inability to source and execute attractive growth opportunities may lead to lower long-term cash flow as businesses operating under finite term contracts experience uncertainty about their longer term cash flow potential.	Management periodically reviews and updates strategy according to market conditions and developments.
Financial Risks		
Expense management risk concerns unexpected non-recoverable increases in operating and administrative costs.	Unanticipated increases in costs could result in lower earnings and cash flow.	Capstone attempts to mitigate this risk by monitoring costs versus budgets and controlling discretionary spending.
Forecasting risk concerns the accuracy of projections for results from operations due to error or unpredictable economic, market and specific business factors.	Volatility of financial forecasts increases liquidity reserve requirements to pay expenses, reducing cash flows.	Capstone targets businesses which have inherently predictable financial results from operations. Capstone maintains adequate levels of liquidity to manage during periods of uncertainty.
Taxation risk concerns higher income and other taxes attributable to adverse legislation changes, including tax rate increases, or interpretations by tax authorities on audit.	Higher taxation results in both lower income and cash flow available.	Capstone minimizes exposures to adverse tax rulings by choosing structures that adhere to taxation regulations, are commonly used in practice and wherever practical supported by opinions of external advisers. In addition, Capstone monitors the trends and policies of taxation authorities in the jurisdictions where its businesses operate.

Risk and Description	Impact	Monitoring and Mitigation
Financing risk concerns the ability to access timely and cost effective debt or equity to support the development and construction of power facilities, business acquisitions and replace maturing debt.	Inability to access cost-effective debt or equity could result in higher interest costs, lower cash flow or liquidity difficulties. For an acquisition, this could also prevent Capstone from realizing a growth opportunity.	Capstone maintains relationships with multiple financial institutions that have the resources to provide some or all financing requirements. In addition, most existing project debt amortizes over the term of the PPAs to minimize refinancing requirements and debt maturities are staggered.
Legal and Regulatory Risks		
Contract and permit compliance risk concerns the ability to operate Capstone's power businesses within the allowances of an increasing number of requirements.	Failure to comply with contracts and permits can impact Capstone's power contracts, debt facilities, and other agreements, which can lead to lower cash flow from the existing businesses by reducing revenue or increasing costs to restore the ability to operate at capacity.	Capstone maintains its contracts, permits and licenses, works with knowledgeable contractors and responds to adverse findings promptly to minimize the impact.

ENVIRONMENTAL, HEALTH AND SAFETY REGULATION

Capstone's power facilities (collectively the "Facilities") hold all material permits and approvals required for their operation and maintenance. All assets are managed to comply with health, safety and environmental ("HSE") laws in addition to Capstone's corporate and facility-specific HSE policies.

The Facilities are subject to robust and stringent environmental, health and safety regulatory regimes, which focus on:

- Commitment to identify, eliminate, mitigate and manage health and safety issues for all workers, visitors, nearby landowners and other personnel at each of the Facilities;
- Regulatory compliance of emissions and discharges related to air, noise, water, and sewage;
- Proper storage, handling, use, transportation and distribution of dangerous goods and hazardous and residual materials including the prevention of releases of these materials to the environment;
- Management of construction and operation related permits to ensure compliance with all HSE regulations; and
- Protection of the natural and built environment.

Climate Change, Greenhouse Gases and Policy Changes

Due to the emission of greenhouse gases, such as carbon dioxide ("CO₂") and nitrous oxides ("NO_x"), some of the Facilities, specifically the Cardinal and Whitecourt facilities, have an ongoing operational impact on the environment. All Facilities comply in all material respects with the applicable Canadian and provincial legislation and guidelines regarding greenhouse gases and other emissions. Capstone monitors the potential impact of future changes to environmental legislation and guidelines by remaining diligent in the operation of the Facilities, including implementing stringent policies and procedures to prevent the contravention of permits and approvals. The Canadian federal government ratified the Paris Accord, negotiated under the United Nations Framework Convention on Climate Change, in the fall of 2016. Pursuant to the Paris Accord, the parties committed, in a non-binding manner, to accelerate actions and investments needed to limit global average temperatures to below 2°C above pre-industrial levels and to pursue efforts to limit the increase to 1.5°C.

In late 2016, Canada and its provinces, other than Saskatchewan and Manitoba, agreed to the Pan-Canadian Framework on Clean Growth and Climate Change ("Framework"). Manitoba subsequently signed onto the Framework, whereas Ontario and Alberta have since pulled out of it. The Framework is the blueprint by which the federal government and the provinces will attempt to meet Canada's commitment under the Paris Accord. Elements of the Framework include all provincial jurisdictions being required to price carbon by 2018. However, provincial jurisdictions have the flexibility to implement a variety of carbon regimes ranging from price-based regimes such as a carbon tax, to performance-based emissions regimes such as cap and trade. For jurisdictions with a price-based regime, the price should at least start at \$10/tonne in 2018 and rise by \$10/tonne each year to \$50/tonne by 2022. As a regulatory backstop, the federal government has also enacted the Greenhouse Gas Pollution Pricing Act ("GGPPA"), which introduces a carbon pricing regime to those provinces that fail to implement adequate provincial measures.

In Alberta, under the Carbon Competitiveness and Incentive Regulation ("CCIR"), regulated facilities that emit 100,000 tonnes of greenhouse gases per annum or more must meet greenhouse gas emissions thresholds. If they cannot do so through operational improvements, they can purchase emissions offsets from qualified offset facilities. Once operating, Capstone's Alberta-based wind development projects are all eligible to produce valid offsets under the CCIR. The Alberta Climate Leadership Act was proclaimed in force as of January 1, 2017. It imposes a carbon levy on certain fuels, such as natural gas and oil, imported into the Province or sold in the Province. This legislation will not have a direct effect on renewable generation including the Whitecourt facility.

On July 3, 2018, Ontario announced the revocation of its previously enacted cap and trade program. Ontario has not yet implemented a replacement greenhouse gas regime. Therefore, the provisions of the GGPPA may apply to Ontario. As indicated

above, Ontario has initiated judicial proceedings to challenge the constitutionality of the GGPPA and is in the process of developing and implementing an alternative provincial regime.

Saskatchewan and Ontario have subsequently launched constitutional challenges to the GGPPA, the results of which could significantly impact how greenhouse gas emissions are regulated in Canada. Capstone continues to monitor potential implications of this issue on its business.

Cardinal

There is currently no restriction on the amount of CO₂ that the Cardinal facility may emit, although the facility is required to report its CO₂ emissions under various federal and provincial regulations. Environmental regulations in Ontario also provide for, among other things, the reporting, allocation and retirement of NO_x emissions. NO_x emissions from Cardinal's generating equipment are lower than the levels mandated by legislation.

Whitecourt

The Whitecourt facility uses biomass combustion technology to convert the energy content in wood waste into electricity. Biomass is generally considered to be carbon-neutral as the amount of CO₂ arising from combustion is equal to what would be emitted if the biomass were to decompose naturally. As a result, electricity generated from biomass is regarded as an environmentally friendly form of power generation. The Whitecourt facility is subject to limits governing the emissions of carbon monoxide, NO_x and particulates in accordance with the facility's Environmental Approval. Average annual emission levels at the Whitecourt facility are below the levels of permitted emissions for it. The Whitecourt facility is also subject to certain federal and provincial greenhouse gas reporting requirements and is in compliance with these requirements.

Hydro Facilities

Capstone's hydro facilities do not produce greenhouse gases. However, their operations are governed by water management plans and/or water licenses, which specify the hydrological conditions during which production may occur.

Wind Facilities

Capstone's wind facilities do not produce greenhouse gases, but are subject to regulations and/or approvals relating to the natural and built environment.

Amherstburg Solar Park

The operation of Amherstburg does not generate greenhouse gases.

Further information regarding Environmental, Safety and Health Regulations matters is contained in the Corporation's Annual Information Form (which is available under the Corporation's profile on www.sedar.com).

RELATED PARTY TRANSACTIONS

Capstone's 2018 related party transactions and balances are primarily comprised of transactions with iCON Infrastructure LLP and subsidiaries ("iCON") and compensation to key management.

Shared Service Arrangement with iCON

Fees earned from iCON Infrastructure Canada Inc. ("iCON Canada"), a subsidiary of iCON, under a shared service arrangement, are reported in the consolidated statements of income as an administrative expense recovery. During 2018, Capstone earned fees of \$232 from iCON Canada (2017 - \$174).

Compensation of Key Management

Key management includes the Corporation's directors, Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") during the year. Compensation awarded to key management consisted of salaries, directors' fees, short-term employee benefits, long-term incentive plans, and termination benefits. Key management compensation is described in note 24 related party transactions in the consolidated financial statements for the year ended December 31, 2018.

Linking Management Compensation to Performance

Compensation plays an important role in achieving short- and long-term business objectives that ultimately drive the Corporation's business success in alignment with long-term shareholder goals. The objectives of the Corporation's compensation program are to:

- Attract and retain highly qualified employees with a history of proven success;
- Align the interests of employees with shareholders' interests and with the execution of the Corporation's business strategy;
- Establish performance goals that, if met, are expected to improve long-term shareholder value; and
- Tie compensation to those goals and provide meaningful rewards for achieving them.

Corporate performance targets are set each year to provide management with an incentive to exceed annual budgeted financial results and other business performance measures and are therefore aligned with shareholder interests.

The following table summarizes the link between the Corporation's executive and senior officer forms of compensation and performance:

	Salary	Short-term incentive plan ("STIP")	Long-term incentive plan ("LTIP")
Description	Salary is a fixed component of compensation that provides income certainty by establishing a base level of compensation for executives fulfilling their roles and responsibilities.	The STIP provides the possibility of an additional annual cash award based on the achievement of corporate and individual goals.	Capstone has a discretionary LTIP and share appreciation rights ("SAR") plan tied to long-term growth to motivate and retain executives on a long-term basis. The awards are paid in cash after meeting certain vesting conditions.
Purpose	To attract and retain qualified executives.	To motivate, attract and retain qualified executives.	To reward long-term performance and align interests of executives with security holders.
Link to performance	No direct link.	A significant portion of this award is based on actual business performance against Capstone's internal performance measures.	The discretionary LTIP is not directly linked to performance. The SAR is directly linked to the long-term increase in the Corporation's value upon a sale transaction.

For a comprehensive understanding of Capstone's compensation program refer to the "Compensation Discussion and Analysis" section of the Corporation's most recently filed AIF.

SUMMARY OF QUARTERLY RESULTS

The following table provides a summary of the previous eight quarters of Capstone's financial performance.

	2018				2017			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenue	49,991	39,951	44,817	48,870	41,561	29,089	40,380	43,133
EBITDA	29,018	31,262	31,061	31,335	28,529	22,221	30,176	29,129
Net income (loss) ^{(1), (2)}	(668)	272	1,386	1,314	1,287	(2,125)	3,285	114,936
Preferred dividends	613	613	613	613	613	613	613	613

(1) Net income (loss) attributable to the common shareholders includes discontinued operations for applicable periods, but excludes non-controlling interests.

(2) Net income includes a gain on the sale of Värmevärdan of \$128,087 in Q1 2017.

FOURTH QUARTER 2018 HIGHLIGHTS

	Three months ended	
	Dec 31, 2018	Dec 31, 2017
Revenue	49,991	41,561
Operating expenses	(12,122)	(10,486)
Administrative expenses	(2,239)	(2,074)
Project development costs	(1,019)	(383)
Equity accounted income	—	825
Interest income	408	1,182
Other gains and (losses), net	(6,015)	(2,095)
Foreign exchange gain (loss)	14	(1)
Earnings before interest, taxes, depreciation and amortization	29,018	28,529
Interest expense	(9,990)	(9,900)
Depreciation of capital assets	(16,627)	(15,888)
Amortization of intangible assets	(2,684)	(2,488)
Earnings (loss) before income taxes	(283)	253
Income tax recovery (expense)		
Current	208	1,263
Deferred	(418)	570
Total income tax recovery (expense)	(210)	1,833
Net income (loss)	(493)	2,086
Net income (loss) attributable to:		
Shareholders of Capstone	(668)	1,287
Non-controlling interest	175	799
	(493)	2,086

In the fourth quarter of 2018, Capstone's EBITDA was higher and net income was lower than in 2017. Higher quarterly EBITDA reflects:

- Higher revenue, primarily due to Glen Dhu and Fitzpatrick, which were equity accounted investments prior to the acquisition of the remaining ownership interests on December 31, 2017. In addition, higher revenue from Whitecourt, due to higher power rates, and Cardinal, due to higher market revenues in response to higher demand; partially offset by
- Decrease in the fair value of the Whitecourt embedded derivative relates to the introduction of EPCs.

In addition to the EBITDA factors and the impacts on interest expense, depreciation and amortization from the acquisition of Glen Dhu and Fitzpatrick, the remaining material change in net income was:

- Lower income tax recovery, primarily attributable to the sale of Värmevärden in 2017.

ACCOUNTING POLICIES AND INTERNAL CONTROLS

Significant Changes in Accounting Standards

The consolidated financial statements have been prepared in accordance with IFRS and are consistent with policies for the year ended December 31, 2017.

Capstone has adopted the new and revised standards, along with consequential amendments, effective January 1, 2018, none of which had an impact on measurement in 2018. These changes include:

- **IFRS 9, *Financial Instruments***
- **IFRS 15, *Revenue from Contracts with Customers***

Refer to note 2 to the December 31, 2018 consolidated financial statements for a summary of significant accounting policies, and detail of the nature of these changes to disclosure in the consolidated financial statements.

Future Accounting Changes

The International Accounting Standards Board ("IASB") has announced new standards and amendments that will be effective for future reporting periods that have not yet been adopted by the Corporation. Capstone's assessment of the impact of the material standards and amendments are ongoing. Capstone continues to monitor changes to IFRS and has implemented applicable IASB changes to standards, new interpretations and annual improvements. The significant upcoming changes to IFRS are:

Title of the New IFRS ⁽¹⁾

- **IFRS 16, Leases** [Effective: Jan 1, 2019]

(1) Refer to note 2 to the consolidated financial statements for the year ended December 31, 2018 for further detail about the nature of this future accounting change.

Accounting Estimates

The consolidated financial statements require the use of estimates and judgment in reporting assets, liabilities, revenues, expenses and contingencies.

The following accounting estimates included in the preparation of the consolidated financial statements are based on significant estimates and judgments, which are summarized as follows:

Area of Significance	Critical Estimates and Judgments
Capital assets, projects under development and intangible assets:	
<ul style="list-style-type: none"> • Purchase price allocations • Depreciation on capital assets • Amortization on intangible assets • Asset retirement obligations • Impairment assessments of capital assets, projects under development and intangibles assets 	<ul style="list-style-type: none"> • Initial fair value of net assets. • Estimated useful lives and residual value. • Estimated useful lives. • Expected settlement date, amount and discount rate. • Future cash flows and discount rate.
Deferred income taxes	<ul style="list-style-type: none"> • Timing of reversal of temporary differences, tax rates and current and future taxable income.
Financial instruments and fair value measurements	<ul style="list-style-type: none"> • Forward Alberta power pool prices, volatility, credit spreads, cost and inflation escalators and fuel supply volumes, electricity sales, and EPC generation.
Accounting for investments in non-wholly owned subsidiaries	<ul style="list-style-type: none"> • Determine how relevant activities are directed (either through voting rights or contracts); • Determine if Capstone has substantive or protective rights; and • Determine Capstone's ability to influence returns.

Management's estimates and judgments were based on historical experience, trends and various other assumptions that are believed to be reasonable under the circumstances. Actual results could materially differ from those estimates.

Internal Controls over Financial Reporting and Disclosure Controls and Procedures

Capstone's CEO and CFO are required by the various provincial securities regulators to certify annually that they have designed, or caused to be designed, Capstone's disclosure controls and procedures, as defined in the Canadian Securities Administrators' National Instrument 52-109 ("NI 52-109"), and that they have evaluated the effectiveness of the presence and function of these controls and procedures in the applicable period. Disclosure controls are those controls and other procedures that are designed to provide reasonable assurance that the relevant information that Capstone is required to disclose is recorded, processed and reported within the time frame specified by such securities regulators.

Capstone's management, under the supervision of and with the participation of the CEO and CFO, has designed internal controls over financial reporting, as defined in NI 52-109. The purpose of internal controls over financial reporting is to provide reasonable assurance regarding the reliability of Capstone's financial reporting, in accordance with IFRS, focusing in particular on controls over information contained in the audited annual and unaudited interim consolidated financial statements. The internal controls are not expected to prevent and detect all misstatements due to error or fraud. Consistent with the prior year, Capstone uses the 2013 version of Committee of Sponsoring Organizations (COSO) internal control framework.

The CEO and CFO have concluded that Capstone's disclosure controls and procedures were effective as at December 31, 2018 to ensure that information required to be disclosed in reports that Capstone files or submits under Canadian securities legislation is recorded, processed, summarized and reported within applicable time periods.

As at December 31, 2018, Capstone's management had assessed the effectiveness of Capstone's internal control over financial reporting using the criteria set forth by COSO of the Treadway Commission in Internal Control – Integrated Framework (2013). Based on this assessment, management has determined that Capstone's internal control over financial reporting was effective as at December 31, 2018.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements and other financial information contained in this annual report have been prepared by management. It is management's responsibility to ensure that sound judgment, appropriate accounting policies and reasonable estimates have been used to prepare this information and that the consolidated financial statements are in accordance with International Financial Reporting Standards.

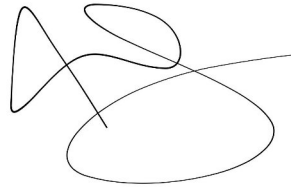
Management is also responsible for designing, maintaining and testing a system of internal controls over the financial reporting processes. Internal controls have been designed to provide reasonable assurance that the financial records are reliable, accurate and form a proper basis for the preparation of the consolidated financial statements. As of December 31, 2018, management reviewed and tested the internal controls over financial reporting and concluded that they were effective to provide reasonable assurance over the consolidated financial statements.

The Audit Committee of the Board of Directors, consisting entirely of independent directors, is responsible for reviewing the consolidated financial statements with management and the external auditors and reporting to the Board of Directors. The Audit Committee is responsible for retaining the services of the independent auditor and for renewing the auditor's mandate, which is subject to Board of Directors' review and shareholders' approval.

The independent auditor, PricewaterhouseCoopers LLP, is responsible for conducting an examination in accordance with Canadian generally accepted auditing standards to express an opinion on whether the consolidated financial statements have been prepared in accordance with International Financial Reporting Standards. The report of PricewaterhouseCoopers LLP, which outlines the scope of its examination and its opinion on the consolidated financial statements, appears on the following page.



David Eva
Chief Executive Officer



Andrew Kennedy
Chief Financial Officer

Toronto, Canada
March 7, 2019



Independent auditor's report

To the Shareholders of Capstone Infrastructure Corporation

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Capstone Infrastructure Corporation and its subsidiaries (together, the Company) as at December 31, 2018 and 2017, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS).

What we have audited

The Company's consolidated financial statements comprise:

- the consolidated statements of financial position as at December 31, 2018 and 2017;
- the consolidated statements of changes in shareholders' equity for the years then ended;
- the consolidated statements of income and comprehensive income for the years then ended;
- the consolidated statements of cash flows for the years then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

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

Independence

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto, Ontario, Canada M5J 0B2
T: +1 416 863 1133, F: +1 416 365 8215



In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.



- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Ross Sinclair.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Ontario
March 7, 2019

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at	Notes	Dec 31, 2018	Dec 31, 2017
Current assets			
Cash and cash equivalents	4	76,341	64,083
Restricted cash	4	23,132	22,438
Accounts receivable	5	25,477	24,408
Other assets	6	2,747	4,778
Current portion of derivative contract assets	7	1,996	1,130
		<u>129,693</u>	<u>116,837</u>
Non-current assets			
Derivative contract assets	7	11,855	20,234
Capital assets	10	833,799	896,377
Projects under development	11	1,595	730
Intangible assets	12	154,861	167,732
Deferred income tax assets	13	125	—
Total assets		<u>1,131,928</u>	<u>1,201,910</u>
Current liabilities			
Accounts payable and other liabilities	14	19,468	20,257
Current portion of long-term debt	15	49,355	86,208
		<u>68,823</u>	<u>106,465</u>
Long-term liabilities			
Derivative contract liabilities	7	2,144	2,144
Deferred income tax liabilities	13	89,962	89,243
Long-term debt	15	705,339	732,334
Liability for asset retirement obligation	16	9,442	10,161
Total liabilities		<u>875,710</u>	<u>940,347</u>
Equity attributable to shareholders' of Capstone		206,132	206,314
Non-controlling interest	18	50,086	55,249
Total liabilities and shareholders' equity		<u>1,131,928</u>	<u>1,201,910</u>
Commitments and contingencies	23		
Subsequent events	26		

See accompanying notes to these consolidated financial statements

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Notes	Equity attributable to shareholders of Capstone			Total Equity
		Share Capital	Retained Earnings (Deficit)	NCI ⁽¹⁾	
Balance, December 31, 2016		112,453	2,800	61,417	176,670
Net income for the period		—	117,383	993	118,376
Conversion of promissory note ⁽²⁾	17	86,332	—	—	86,332
Return of capital ⁽²⁾	17	(86,332)	(45,636)	—	(131,968)
Business acquisition ⁽³⁾	3	21,837	—	—	21,837
Dividends declared to preferred shareholders of Capstone ⁽⁴⁾	17	—	(2,523)	—	(2,523)
Dividends declared to NCI	18	—	—	(3,240)	(3,240)
Convertible debenture repayments ⁽⁵⁾	18	—	—	(3,921)	(3,921)
Balance, December 31, 2017		134,290	72,024	55,249	261,563
Net income for the period		—	2,304	1,593	3,897
Dividends declared to preferred shareholders of Capstone ⁽⁴⁾	17	—	(2,486)	—	(2,486)
Dividends declared to NCI	18	—	—	(3,793)	(3,793)
Convertible debenture repayments ⁽⁵⁾	18	—	—	(2,963)	(2,963)
Balance, December 31, 2018		134,290	71,842	50,086	256,218

(1) Non-controlling interest ("NCI").

(2) Refer to note 3 for changes related to the sale of Värmevärden.

(3) Refer to note 3 for changes related to the acquisition of remaining interests of the Glen Dhu and Fitzpatrick wind facilities.

(4) Dividends declared to preferred shareholders of Capstone include current and deferred income taxes of \$34 (2017 - \$71).

(5) Repayments are to the holder of the convertible debenture related to the GHG Wind Development LP, SR Wind Development LP and SLS Wind Development LP wind facilities. The convertible debenture provides the holder the option to convert its debt into a 50% equity interest in these projects.

See accompanying notes to these consolidated financial statements

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

	Notes	For the year ended	
		Dec 31, 2018	Dec 31, 2017
Revenue	20	183,629	154,163
Operating expenses	21	(50,388)	(42,290)
Administrative expenses	21	(7,529)	(8,718)
Project development costs	21	(2,921)	(2,090)
Equity accounted income	9	—	935
Interest income	7	5,139	1,600
Other gains and (losses), net	22	(5,258)	6,437
Foreign exchange gain		4	18
Earnings before interest expense, taxes, depreciation and amortization		122,676	110,055
Interest expense	7	(38,797)	(36,668)
Depreciation of capital assets	10	(66,785)	(56,962)
Amortization of intangible assets	12	(11,182)	(9,825)
Earnings before income taxes		5,912	6,600
Income tax expense			
Current		(270)	(371)
Deferred		(1,745)	(17,170)
Total income tax expense	13	(2,015)	(17,541)
Net income (loss) and total comprehensive income (loss) from continuing operations		3,897	(10,941)
Net income and total comprehensive income from discontinued operations, net of tax	3	—	129,317
Net income and total comprehensive income		3,897	118,376
Attributable to:			
Shareholders of Capstone		2,304	117,383
Non-controlling interest	18	1,593	993
		3,897	118,376

See accompanying notes to these consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Notes	For the year ended	
		Dec 31, 2018	Dec 31, 2017
Operating activities:			
Net income (loss) from continuing operations		3,897	(10,941)
Deferred income tax expense		1,745	17,170
Depreciation and amortization		77,967	66,787
Non-cash other gains and losses (net)		7,697	(773)
Amortization of deferred financing costs and non-cash financing costs		2,712	2,581
Equity accounted income	9	—	(935)
Foreign exchange gain		(4)	(18)
Change in non-cash working capital		(916)	(2,118)
Cash flows from continuing operations		93,098	71,753
Cash flows from discontinued operations	3	—	1,372
Total cash flows from operating activities		93,098	73,125
Investing activities:			
Investment in capital assets	10	(4,021)	(16,025)
Investment in projects under development	11	(793)	(18,236)
Decrease (increase) in restricted cash		(694)	5,295
Cash acquired from acquisition of equity accounted investment	3	—	3,574
Distributions from equity accounted investments	9	—	2,352
Total cash flows used in investing activities		(5,508)	(23,040)
Financing activities:			
Repayment of long-term debt		(103,277)	(121,132)
Dividends paid to non-controlling interests	18	(3,793)	(3,240)
Convertible debenture repayments	18	(2,963)	(3,921)
Dividends paid to preferred shareholders		(2,452)	(2,452)
Transaction costs on debt issuance		(93)	(1,080)
Proceeds from issuance of long-term debt		37,246	83,717
Return of capital to Irving	3	—	(131,968)
Repayment of promissory note	3	—	(10,370)
Cash flows used in continuing operations		(75,332)	(190,446)
Cash flows from discontinued operations	3	—	142,198
Total cash flows used in financing activities		(75,332)	(48,248)
Increase in cash and cash equivalents		12,258	1,837
Cash and cash equivalents, beginning of year		64,083	62,246
Cash and cash equivalents, end of year		76,341	64,083
Supplemental information:			
Interest paid		36,293	34,077
Taxes paid		973	1,882

See accompanying notes to these consolidated financial statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 1. CORPORATE INFORMATION

Capstone is incorporated and domiciled in Canada and located at 155 Wellington Street West, Suite 2930, Toronto, Ontario, M5V 3H1. All of Capstone's Class A common shares are owned by Irving Infrastructure Corp. ("Irving"), a subsidiary of iCON Infrastructure Partners III, LP ("iCON III"), a fund managed by London, UK-based iCON Infrastructure LLP ("iCON"), who is the ultimate parent. Capstone Infrastructure Corporation and its subsidiaries (together the "Corporation" or "Capstone") mission is to provide investors with an attractive total return from responsibly managed long-term investments in power generation in North America. Capstone's strategy is to develop, acquire and manage a portfolio of high quality power assets. As at December 31, 2018, Capstone owns and operates an approximate net installed capacity of 531 megawatts across 23 facilities in Canada, including wind, hydro, solar, biomass, and natural gas power plants.

All amounts are in Canadian thousands of dollars or thousands of share amounts unless otherwise indicated.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following significant accounting policies are used in the preparation of these consolidated financial statements.

Basis of Preparation

Statement of compliance

The consolidated financial statements of Capstone have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The consolidated financial statements were authorized for issue by the Board of Directors on March 7, 2019.

Discontinued Operations and Assets Held for Sale

As further discussed in note 3, on March 3, 2017, Capstone sold its interest in Värmevärden, resulting in the *utilities - district heating* segment being presented as a discontinued operation in the statements of income and cash flows for the year ended December 31, 2017.

Basis of measurement

The consolidated financial statements have been prepared under the historical cost basis, except for the revaluation of certain financial instruments, which are measured at fair value as explained in the accounting policies set out below and on a going concern basis of accounting (see note 8). Historical cost is generally based on the fair value of the consideration given in exchange for assets.

Consolidation

These consolidated financial statements are primarily made up of the assets, liabilities and results of operations of the Corporation's subsidiaries. Subsidiaries are all entities over which Capstone has control. Capstone controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

The following table lists the significant subsidiaries of the Corporation which are accounted for on a consolidated basis:

Name of entity	Principal place of business and country of incorporation	Ownership at December 31,		Principal activity
		2018	2017	
Capstone Power Corp. ("CPC")	Canada	100%	100%	Power holding company
Cardinal Power of Canada, L.P. ("Cardinal")	Canada	100%	100%	Power generation
Erie Shores Wind Farm Limited Partnership ("Erie Shores")	Canada	100%	100%	Power generation
MPT Hydro LP ("Hydro")	Canada	100%	100%	Power generation
Whitecourt Power Limited Partnership ("Whitecourt")	Canada	100%	100%	Power generation
Helios Solar Star A-1 Partnership ("Amherstburg")	Canada	100%	100%	Power generation
Glance Bay Langan Wind Power Ltd. ("Glance Bay")	Canada	100%	100%	Power generation
Sky Generation L.P. ("SkyGen"), formerly Sky Generation Inc. ⁽¹⁾	Canada	100%	100%	Power generation
SP Amherst Wind Power LP ("Amherst")	Canada	51%	51%	Power generation
Parc Éolien Saint-Philémon S.E.C. ("Saint-Philémon")	Canada	51%	51%	Power generation
Chi-Wiikwedong LP ("Goulais")	Canada	51%	51%	Power generation
Chi-Wiikwedong Holdings LP	Canada	100%	100%	Power holding company
Grey Highlands Clean Energy Development LP ("Grey Highlands Clean")	Canada	100%	100%	Power generation
GHG Wind Development LP ("GHG") ⁽²⁾	Canada	100%	100%	Power generation
SR Wind Development LP ("Snowy Ridge") ⁽²⁾	Canada	100%	100%	Power generation
SLS Wind Development LP ("Settlers Landing") ⁽²⁾	Canada	100%	100%	Power generation
Glen Dhu Wind Energy LP ("Glen Dhu")	Canada	100%	100% ⁽³⁾	Power generation
Fitzpatrick Mountain Wind Energy Inc. ("Fitzpatrick")	Canada	100%	100% ⁽³⁾	Power generation

(1) The SkyGen entity holds the Ferndale, Ravenswood, Proof Line and Skyway 8 operating wind facilities.

(2) GHG, Snowy Ridge and Settlers Landing have convertible debentures outstanding which provide the holder the option to convert its debt into a 50% equity interest in these projects.

(3) On December 31, 2017, Capstone acquired the remaining 51% interest in Glen Dhu and the remaining 50% interest in Fitzpatrick, increasing Capstone's interests in both wind facilities to 100%. Results for the periods up to the acquisition are included in equity accounted income in the statement of income. Refer to note 3.

The Corporation accounts for its controlled investments using the consolidation method of accounting from the date control is obtained and deconsolidates from the date that control ceases. All intercompany balances and transactions have been eliminated on consolidation.

Non-controlling interests represent equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Their share of net income and comprehensive income is recognized directly in equity. Changes in the Corporation's interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

Equity Accounted Investments

Companies in which the Corporation has the ability to exercise significant influence, but not control, or has the ability to exercise joint control over financial and operating policy decisions are accounted for using the equity method. Significant influence is presumed to exist when the Corporation holds between 20% and 50% of the voting power of another entity. Capstone's investments in Värmevärden AB ("Värmevärden") and the Glen Dhu and Fitzpatrick wind facilities were accounted for on an equity accounting basis for portions of 2017, prior to the respective sale transaction of Värmevärden and consolidation of the wind facilities.

Business Combinations

The acquisitions of businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets transferred, liabilities incurred or assumed, and equity instruments issued by the Corporation in exchange for control of the acquired business. The acquired identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3R, Business Combinations ("IFRS 3R") are recognized at their fair value at the acquisition date.

The Corporation recognizes any non-controlling interest in the acquiree at the non-controlling interest's proportionate share of the recognized amounts of acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

Foreign Currency Translation

Functional and presentation currency

Amounts included in the financial statements of each entity that is a foreign operation are measured using the currency of the primary economic environment in which the entity operates ("functional currency"). The consolidated financial statements are presented in Canadian dollars ("presentation currency"), which is Capstone's functional currency. Capstone used a rate of 0.1484 to translate amounts in Swedish Krona relating to the disposal of its interest in Värmevärden. Since the disposal, Capstone holds a limited amount of foreign currency.

The financial statements of entities that have a functional currency different from that of the Corporation are translated into Canadian dollars as follows: assets and liabilities – at closing rate at the date of the statement of financial position, and income and expenses – at the average rate of the period (as this is considered a reasonable approximation of the actual rates prevailing at the transaction dates).

Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of transactions. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at exchange rates of monetary assets and liabilities denominated in currencies other than an entity's functional currency are recognized in the consolidated statement of income in "foreign exchange gain (loss)".

Cash and Cash Equivalents

Cash and cash equivalents are composed of highly liquid investments with original maturities of 90 days or less at the date of acquisition and are recorded at fair value.

Capitalized Interest

The Corporation capitalizes interest and borrowing costs when activities that are necessary to prepare the asset for its intended use are in progress, and expenditures for the asset have been used or borrowed to fund the construction or development. Capitalization of interest and borrowing costs ceases when the asset is ready for its intended use. Capitalized interest is included in the statement of financial position as part of capital assets and projects under development.

Grants and Contributions

Grants are recognized at their fair value when there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. Grants and contributions related to charges to net income are netted against such expenditures as received.

Capital Assets

Capital assets are stated at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. 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 associated with the item will flow to the Corporation and the cost can be measured reliably. The carrying value of an asset is derecognized when replaced.

Major maintenance costs are capitalized in the carrying value of the assets as incurred, and depreciated over their useful lives. Other repairs and maintenance costs are charged to the consolidated statement of income during the period incurred.

Gains or losses on disposals are determined by comparing the proceeds of sale with the carrying amount and are recognized within the consolidated statement of income.

The Corporation allocates the amount initially recognized in respect of an item of capital assets to its significant parts and depreciates separately each such part. Residual values, method of amortization and useful lives of the assets are reviewed annually and adjusted if appropriate. The major categories of capital assets are depreciated using the straight-line method as follows:

	Power
Equipment and vehicles:	
Computer hardware	3 to 5 years
Communications, meters and telemetry equipment	15 to 30 years
Vehicles	5 years
Property and plant:	
Operational structures	15 to 30 years
Operational properties	40 years

Leased Assets

Assets financed by leasing agreements that transfer substantially all the risks and rewards of ownership of an asset to the lessee are capitalized and depreciated over the shorter of their estimated useful lives and the lease term. The corresponding liability is recorded as borrowings. The capital element of the lease rental is deducted from the obligation to the lessor as paid. The interest element of lease rentals and the depreciation of the relevant assets are charged to the consolidated statement of income.

Operating lease rental payments are charged to the consolidated statement of income on a straight-line basis as incurred over the term of the lease.

Projects Under Development ("PUD")

Capitalized costs related to an asset under development include all eligible expenditures incurred in connection with the development and construction of the power generating asset until it is available for its intended use. The Corporation capitalizes all direct project costs related to the development of the Corporation's electricity generation projects. Capitalization commences when the project is:

- Clearly identified;
- The technical feasibility has been established;
- Management has indicated its intention to construct, operate and maintain the project;
- An offtake market is identified or a power purchase agreement ("PPA") awarded; and
- Adequate resources exist or are expected to be available to complete the project.

Upon a project becoming commercially operational, the capitalized costs, including capitalized borrowing costs, if any, are transferred to capital assets and are amortized on a straight-line basis over the estimated useful lives of the various components.

The recovery of project development costs is dependent upon successful commercialization of project sites for the profitable sale of electricity.

Intangible Assets

Identifiable intangible assets

The Corporation separately identifies acquired intangible assets, including computer software, electricity supply contracts, gas purchase contracts, water rights and licenses, and records each at their fair value at the date of acquisition. The initial fair value is amortized over their estimated useful lives using the straight-line method as follows:

	Power
Computer software	3 to 7 years
Electricity supply, gas purchase and other contracts ⁽¹⁾	15 to 25 years
Water rights	10 to 35 years

(1) Generally amortized over the contract term.

The expected useful lives of intangible assets are reviewed on an annual basis and adjusted prospectively.

Impairment of Non-financial Assets

The capital assets, projects under development and intangible assets with finite lives are tested for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash inflows. The recoverable amount is the higher of an asset's fair value less costs to sell the assets and the value in use (being the present value of the expected future cash flows of the relevant assets or Cash Generating Unit ("CGU")). An impairment loss is recognized for the amount by which the asset's carrying value exceeds its recoverable amount. The Corporation evaluates impairment losses, for potential reversals when events or circumstances warrant such consideration.

Provisions

Provisions are recognized when the Corporation has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured using management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. The Corporation performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

Retirement Benefit Plans

The Corporation operates defined contribution pension plans through its subsidiaries. Costs of defined contribution pension plans are charged to the consolidated statement of income in the period in which they fall due.

Asset Retirement Obligations

The Corporation recognizes a provision for the future retirement obligations associated with its operating plants. These obligations are initially measured at the present value, which is the discounted future cost of the liability. A reassessment of the expected costs associated with these liabilities is performed annually with changes in the estimates of timing or amount of cash flows added or deducted from the cost of the related asset. The liability grows until the date of expected settlement of the retirement obligations.

Share Capital

Common and Class A shares are classified as equity. Incremental costs directly attributable to the issuance of shares are recognized as a reduction in equity.

Preferred Shares

The Corporation classifies its series A preferred shares as equity for reporting purposes given that the preferred shares may be converted into a fixed number of the Corporation's own equity instruments and there is no settlement required at a future date. Incremental costs directly attributable to the issuance of shares are recognized as a reduction in equity.

Dividends

Dividends on series A preferred shares are recognized in the Corporation's consolidated financial statements in the period in which the dividends are declared by the Board of Directors of the Corporation.

Revenue Recognition

Revenue from Contracts with Customers

Revenue derived from the sale of electricity and steam is recognized upon delivery to the customer and priced in accordance with the provisions of the applicable electricity and steam sales agreements. In addition, capacity and availability payments to Cardinal are recognized in accordance with the non-utility generator contract. Certain power purchase arrangements provide for an electricity rate adjustment, which is updated periodically both for the current and prior periods. Capstone accounts for such adjustments when a reliable estimate of the adjustment can be determined. Revenue derived from Whitecourt electricity sales to the Alberta power pool are recorded at the hourly average weighted power pool rate.

The customer invoices and provides payments on a systematic basis based on fixed billing cycles. There are no significant financing components inherent in Capstone's contracts with customers. Capstone does not make significant judgments that affect the determination of the amount and timing of revenue from contracts with customers.

Other Revenue and Income Recognition

Capstone follows Accounting for Government Grants and disclosure of Government Assistance (IAS 20) with respect to certain power contracts with provincial jurisdictions.

Capstone recognizes management fees and development-related incentive fees received from its equity accounted investments in revenue as earned based on the terms of its respective agreements.

Interest income is earned with the passage of time and is recorded on an accrual basis.

Expense Recognition

Costs related to the purchases of fuel are recorded upon delivery. All other costs are recorded as incurred.

Project development costs are recorded as incurred. These costs include the activities to pursue and develop greenfield projects and acquisition-related business development expenses incurred at both the power segment and corporate.

Interest expense is incurred with the passage of time and is recorded on an accrual basis.

Long-term Incentive Plans

The Corporation accounts for grants under its share appreciation rights ("SAR") plan in accordance with IFRS 2 Share-Based Payments.

Income Taxes

Current and deferred income taxes are recognized in the consolidated statement of income except to the extent that they relate to items recognized directly in equity or in other comprehensive income, in which case the income tax is also recognized directly in equity or in other comprehensive income.

Current income tax is the amount recoverable or expensed based on the current year's taxable income using tax rates enacted, or substantively enacted, at the reporting period, and any adjustments to income tax payable or recoveries in respect of previous years.

The Corporation follows the liability method of accounting for deferred income tax whereby deferred income tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying values in the consolidated financial statements. Deferred income tax assets and liabilities are determined using income tax rates that are both expected to apply when the deferred income tax asset or liability will be settled and that have been enacted or substantively enacted as at the date of the consolidated statement of financial position. Deferred income tax assets are recognized to the

extent that it is probable that the asset can be recovered. Deferred income tax assets and liabilities are presented as non-current.

Financial Instruments

Financial assets and financial liabilities are recognized on the consolidated statement of financial position when the Corporation becomes a party to the contractual provisions of the financial instrument.

Classification and Measurement

Financial instruments are required to be measured at fair value on initial recognition plus transaction costs in the case of financial instruments measured at amortized cost. Transaction costs that are directly attributable to the acquisition or issue of financial instruments classified as fair value through profit and loss ("FVTPL") are expensed as incurred. Measurement in subsequent periods depends on the classification of the financial instrument.

The Corporation has designated each of its significant categories of financial instruments outstanding as follows:

IFRS 9 Classification	Significant Categories	Measurement
Amortized cost (asset)	<ul style="list-style-type: none"> • Cash and cash equivalents • Restricted cash • Accounts receivable 	<ul style="list-style-type: none"> • At amortized cost using the effective interest method
Financial assets and liabilities at fair value through profit and loss	<ul style="list-style-type: none"> • Derivative contract assets • Derivative contract liabilities 	<ul style="list-style-type: none"> • At fair value with changes in fair value recognized in the consolidated statement of income
Other liabilities	<ul style="list-style-type: none"> • Accounts payable and other liabilities • Long-term debt 	<ul style="list-style-type: none"> • At amortized cost using the effective interest method

The classification of financial assets depends on Capstone's business objectives for managing the assets and whether contractual terms of the cash flows are considered solely payments of principal and interest. For assets measured at FVTPL, gains and losses will be recorded in the statement of income as incurred.

The Corporation determines the fair value of its financial instruments based on the following hierarchy:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and

Level 3 – Inputs that are not based on observable market data.

Derivative Financial Instruments

The Corporation's derivatives are carried at fair value and are reported as assets when they have a positive fair value and as liabilities when they have a negative fair value. In 2018, the Corporation's derivatives include interest rate swaps and an embedded derivative in Whitecourt's fuel supply agreement.

Changes in the fair values of derivative financial instruments are reported in the consolidated statement of income.

Derivatives embedded in other financial instruments or contracts are separated from their host contracts and accounted for at fair value when their economic characteristics and risks are not closely related to those of the host contract.

Impairment of Financial Assets

For financial assets measured at amortized cost, Capstone applies the simplified expected credit loss ("ECL") approach as permitted by IFRS 9. ECLs are estimated based on historical information, third-party accreditations such as credit ratings, and forward looking information regarding historical customer default rates. Capstone does not expect this to affect any measurement of financial assets and liabilities as its customer base is predominantly government entities.

If impairment exists on the financial asset, the Corporation recognizes an impairment loss in the consolidated statement of income. The loss is measured as the difference between the carrying and the present value of the expected future cash flows. Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

Impairment of cash and cash equivalents and restricted cash are evaluated by reference to the credit quality of the underlying financial institution.

Segment Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker is responsible for allocating resources and assessing performance of the operating segments.

Discontinued Operations

Entities or components of entities that have been disposed of or classified as held for sale and represent separate CGUs are presented separately as discontinued operations. The results of discontinued operations for both the current and comparative periods are included in a separate line item in the statement of comprehensive income which includes post-tax profit or loss of the entities and the post-tax gain or loss recognized on the disposal or re-measurement of the entities.

Earnings Before Interest Expense, Taxes, Depreciation and Amortization ("EBITDA")

EBITDA is an additional GAAP financial measure defined as earnings (loss) before financing costs, income tax expense, depreciation and amortization. EBITDA includes earnings (loss) related to the non-controlling interest ("NCI"), interest income, and other gains and losses (net). EBITDA represents Capstone's capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible capital assets and intangible assets, which vary according to their age, technology, and management's estimate of their useful life. EBITDA is presented on the consolidated statement of income.

Changes to Accounting Policies

Capstone has adopted the following new IFRS standards effective January 1, 2018. These changes were required due to changes in IFRS and are summarized as follows:

IFRS 9, *Financial Instruments*, replaces IAS 39, *Financial Instruments: Recognition and Measurement* as the recognition, classification and measurement of financial assets and liabilities; derecognition of financial instruments; impairment of financial assets and if elected, hedge accounting. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7, *Financial Instruments: Disclosures*.

Derivative contract assets and liabilities remain measured at fair value through profit and loss. All other financial assets and liabilities are measured at amortized cost. The adoption of IFRS 9 did not require any changes to existing recognition, classification, measurement and disclosure of Capstone's financial assets and liabilities.

There were no changes to the classification of Capstone's financial liabilities. The new asset classifications, as well the concept of ECLs are within the financial instruments policy note.

IFRS 15, *Revenue from Contracts with Customers*, replaces IAS 11, *Construction Contracts* and IAS 18, *Revenue* and outlines a single comprehensive model to account for revenue arising from contracts with customers. In addition, IFRS 15 requires enhanced disclosure that will detail the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts with customers. The standard provides a principles-based five-step model to be applied to all contracts with customers. The adoption of IFRS 15 did not require any changes to Capstone's revenue recognition approach and did not result in any measurement adjustments. Additional disclosure requirements are included in note 20.

The adoption of both these accounting standards did not change any comparative figures presented in the interim consolidated financial statements.

Future Accounting Changes

The International Accounting Standards Board ("IASB") has announced new standards and amendments that will be effective for future reporting periods that have not yet been adopted by the Corporation. Capstone's assessment of the impact of the material standards and amendments are ongoing. Capstone continues to monitor changes to IFRS and has implemented applicable IASB changes to standards, new interpretations and annual improvements.

The significant upcoming changes to IFRS are:

Title of the New IFRS	Nature of the Impending Change to Capstone	Status of Adoption
IFRS 16, Leases Effective: Jan 1, 2019	<p>IFRS 16 specifies how to recognize, measure, present and disclose leases. This standard may be applied retrospectively or using a cumulative catch-up approach. The cumulative catch-up approach does not require restatement of prior period financial information and instead requires the recognition of liabilities and an equal Right-of-use ("ROU") assets on transition, and applies the standard prospectively. The Corporation uses the cumulative catch-up approach.</p> <p>On adoption, the Corporation will recognize lease liabilities at the present value of the remaining lease payments, discounted at the incremental borrowing rate of the Corporation. This will equal the ROU assets with no impact to retained earnings. The following practical expedients were permitted under IFRS 16, which the Corporation has elected:</p> <ul style="list-style-type: none">• use of a single discount rate for leases with similar characteristics;• accounting for leases with remaining terms of less than twelve months as short-term leases;• accounting for payments as expenses for low dollar value assets; and• use of hindsight in determining term where options to extend or terminate exist.	Capstone expects the adoption of IFRS 16 to expand lease disclosure, create new ROU assets and corresponding lease liabilities on the statement of financial position, as well as increase EBITDA. On adoption, the long-term assets and liabilities and EBITDA are expected to increase by approximately \$30,000 and \$2,600, respectively.

Critical Accounting Estimates and Judgments

The Corporation makes estimates and assumptions concerning the future that will, by definition, seldom equal actual results. The following are the estimates and judgments applied by management that most significantly affect the Corporation's financial statements. These estimates and judgments have a risk of causing a material adjustment to the carrying values of financial assets and financial liabilities within the next financial year.

Area of Significance	Critical Estimate	Critical Judgment
Capital assets, projects under development and intangible assets – carrying values Fair value estimates are required in the determination of the net assets acquired in a business combination and in the impairment assessment for our capital assets and the assignment of amounts to the asset retirement obligations, as well as assessing capitalization criteria for project development costs.	<ul style="list-style-type: none"> Estimates are based on assumptions that are sensitive to change, which may have a significant impact on the valuations performed. Impairment reviews of the carrying value of capital and other long-lived assets along with the asset retirement obligations require management to estimate fair value based on future cash flows, discount rates and business performance. 	<ul style="list-style-type: none"> Initial fair value of net assets Estimated useful lives and residual value Expected settlement date, amount and discount rate Future cash flows and discount rate
Deferred income taxes Estimates in the determination of deferred income taxes affect asset and liability balances.	<ul style="list-style-type: none"> The determination of the deferred income tax balances of the Corporation requires management to make estimates of the reversal of existing temporary differences between the accounting and tax bases of assets and liabilities in future periods. 	<ul style="list-style-type: none"> Timing of reversal of temporary differences Tax rates Current and future taxable income
Financial instrument fair value measurements When observable prices are not available, fair values are determined by using valuation techniques that refer to observable market data. This is specifically related to Capstone's financial instruments.	<ul style="list-style-type: none"> Management's valuation techniques include comparisons with similar instruments where market observable prices exist, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. For embedded derivatives, fair values are determined from valuation techniques using non-observable market data or transaction processes. <p>A number of factors such as bid-offer spread, credit profile and model uncertainty are taken into account, as appropriate.</p>	<ul style="list-style-type: none"> Forward Alberta power pool prices, volatility, credit spreads, cost and inflation escalators and fuel supply volumes and electricity sales, and Emissions Performance Credits ("EPC") generation.
Accounting for investments in non-wholly owned subsidiaries When Capstone owns a partial interest in an entity, significant judgment is required to determine the proper accounting treatment. Capstone consolidates upon evaluating its ability to control a subsidiary.	<ul style="list-style-type: none"> No critical estimates are involved in determining control. 	<ul style="list-style-type: none"> Determine how relevant activities are directed (either through voting rights or contracts) Determine if Capstone has substantive or protective rights Determine Capstone's ability to influence returns

NOTE 3. ACQUISITIONS, DISPOSALS AND DISCONTINUED OPERATIONS

(A) Discontinued Operations - Sale of Värmevärden

On March 3, 2017, Capstone and its co-shareholder Macquarie European Infrastructure Fund 2 ("MEIF 2") sold 100% of Värmevärden. Capstone received proceeds of \$142,198, net of transaction costs, for its 33.3% indirect interest in Värmevärden and the related outstanding loans receivable.

On March 31, 2017, Irving Infrastructure Corp. ("Irving") converted its 552,700 SEK tranche of the promissory note into 76,876 Class A shares of the Corporation, with a carrying value of \$86,332, and the \$10,370 Canadian denominated tranche of the promissory note was repaid. As a result, no promissory note payable to Irving remains. Capstone then distributed \$131,968 to Irving as a return of capital, which included a \$45,636 reduction to retained earnings and \$86,332 to the Class A shares. The impact of these transactions did not change the carrying value of the Class A shares.

For the year ended December 31, 2017, Capstone's consolidated statements of income and cash flows for the year ended December 31, 2017 include results for the discontinued operations of Värmevärden. Net income from discontinued operations, net of tax was \$129,317. Operating cash flows provided by discontinued operations were \$1,372, and financing cash flows provided by discontinued operations were \$142,198, consisting of net proceeds on sale.

As at March 3, 2017	\$
Net proceeds on sale ⁽¹⁾	142,198
Carrying value of assets held for sale ⁽²⁾	(14,111)
Gain on sale of Värmevärden	128,087

(1) Proceeds are net of transaction costs of \$2,378.

(2) Värmevärden had \$3,025 working capital and \$11,086 loans receivable on March 3, 2017.

The results of the *utilities - district heating* segment, including the gain on sale, are presented as a discontinued operation.

Net income from discontinued operations

The net income from Värmevärden's discontinued operations for the year ended December 31, 2017 was:

For the year ended	Dec 31, 2017
Administrative expenses	(238)
Gain on sale ⁽¹⁾	128,087
Other income (loss)	1,468
Net income (loss) from discontinued operations, net of tax	129,317

(1) Gain on sale is net of foreign exchange impact of \$119.

(B) Business Acquisition - Glen Dhu and Fitzpatrick Wind Facilities

In December 2017, through a series of transactions, Capstone acquired the remaining (approximately 50%) ownership interests in the Glen Dhu and Fitzpatrick wind facilities for \$21,837, bringing Capstone's ownership interest to 100%. The acquisition of the remaining interest was initially completed by a subsidiary of iCON III, who then contributed the acquired assets to Capstone on December 31, 2017 in return for an additional capital contribution, recorded as an increase in shareholders' equity.

Beginning December 31, 2017, the balances in Capstone's consolidated statement of financial position include amounts from Glen Dhu and Fitzpatrick; prior to this transaction these investments were equity accounted. Refer to note 9.

The transaction was accounted for as a step acquisition using the acquisition method of accounting. Under this method, total assets and liabilities are initially recognized at their fair values on the date of acquisition and the equity accounted investment is derecognized. Transaction costs on acquisition of \$225 were expensed in the consolidated statement of income as part of project development costs.

The preliminary and final allocation of the purchase price were allocated to net assets acquired as follows:

Recognized amounts of identifiable assets acquired and liabilities assumed	Notes	Original Fair Value	Adjustment	Revised Fair Value
		Dec 31, 2017		Dec 31, 2018
Working capital ⁽¹⁾		3,448	—	3,448
Other assets		1,763	—	1,763
Capital assets		118,235	(570)	117,665
Intangible assets – electricity supply and other contracts		21,496	—	21,496
Less: net financial liabilities (net of \$3,941 cash acquired, after adjustment)		(85,311)	367	(84,944)
Other liabilities		(1,687)	—	(1,687)
Deferred income tax liability		(15,060)	203	(14,857)
Total identifiable net assets acquired		42,884	—	42,884
Consideration in the form of equity contribution	17	21,837	—	21,837
Previously held equity accounted investments ⁽²⁾	9	21,047	—	21,047
		42,884	—	42,884

(1) Working capital includes \$2,948 of accounts receivable, no allowance for doubtful debts are recorded.

(2) As at the date of acquisition, the book value of the equity accounted investment approximated the fair value of Capstone's interest in the acquiree. No gain or loss was recognized on the transaction.

NOTE 4. CASH AND CASH EQUIVALENTS AND RESTRICTED CASH

	Dec 31, 2018	Dec 31, 2017
Debt service and maintenance reserves	12,889	12,452
Construction escrow	10,168	9,911
Cash on deposit	75	75
Restricted cash	23,132	22,438
Unrestricted cash and cash equivalents	76,341	64,083
	99,473	86,521

Restricted cash is primarily cash that is held by the Corporation's subsidiaries in support of segregated bank accounts to support debt service reserves, operating and maintenance reserves in support of specific long-term debt and/or proceeds from construction facilities used for specific project costs. Capstone has also provided letters of credit to back other reserve requirements (refer to note 15).

NOTE 5. ACCOUNTS RECEIVABLE

	Dec 31, 2018	Dec 31, 2017
Power	25,357	24,360
Corporate	120	48
	25,477	24,408

For both periods presented, Capstone's power segment and corporate trade and other receivables did not require a provision for impairment. Substantially all of the accounts receivable are with government authorities and none are past due. Refer to note 8b and 8c for further detail of credit risk and economic dependence.

NOTE 6. OTHER ASSETS

	Dec 31, 2018	Dec 31, 2017
Prepaid expenses	906	2,697
Inventory of spare parts and consumable supplies, net ⁽¹⁾	1,841	2,081
	2,747	4,778

(1) No inventory obsolescence provision is required as at December 31, 2018.

The cost of inventories recognized in operating expenses for the year ended December 31, 2018 was \$807 (2017 - \$480).

NOTE 7. FINANCIAL INSTRUMENTS

In 2018, financial instruments consist of amortized cost assets, other liabilities and financial assets and liabilities at fair value through profit and loss.

Amortized Cost (Asset)

Cash and cash equivalents, restricted cash	The Corporation's cash and cash equivalents and restricted cash balances are invested in financial instruments of highly rated financial institutions and government securities with original maturities of 90 days or less. As at December 31, 2018, the carrying values of cash and cash equivalents and restricted cash are considered to approximate their fair values due to their short-term nature, which is consistent with the prior year.
Accounts receivable	The Corporation's accounts receivable, which consist of trade receivables, are recorded initially at fair value.

Other Liabilities

Accounts payable and other liabilities	The Corporation's accounts payable and other liabilities are short-term liabilities with carrying values that approximate their fair values as at December 31, 2018.
Long-term debt	The Corporation's long-term debt is recorded at amortized cost using the effective interest rate method. The fair value of the Corporation's long-term debt is determined using level 2 inputs as follows: <ul style="list-style-type: none"> • Floating rate debt approximates its carrying value. Use level 2 inputs: <ul style="list-style-type: none"> • Fixed-rate debt is determined through the use of a discounted cash flow analysis using relevant risk-free bond rates plus an estimated margin.

Financial assets and liabilities at fair value through profit and loss

Interest rate swaps

The Corporation has interest rate swap contracts to effectively fix the interest cost on its long-term debt with variable rates, specifically for Cardinal, GHG, Grey Highlands Clean, Snowy Ridge and Settlers Landing. Under these swap agreements, these projects receive Canadian Dollar Offered Rate ("CDOR") in exchange for fixed rate (refer to note 8a).

Whitecourt embedded derivative

On March 2, 2015, Whitecourt entered into a fuel supply agreement with Millar Western for 15 years, which is extendable to 20 years. The agreement, which was effective on January 1, 2015, includes power price support and revenue sharing mechanisms that reduce Whitecourt's exposure to merchant price risk in Alberta.

The price support and revenue sharing mechanisms are embedded derivatives that are measured at fair value and result in an asset during periods when the projected merchant power price is forecast to be lower than the price support and a liability during periods when the merchant power price is forecast to be higher.

On March 2, 2015, Capstone recognized an asset of \$5,297 based on the fair value of the Whitecourt fuel supply agreement, which was equal to and offset the fair value of the embedded derivative included in Whitecourt's fuel supply agreement at inception. Capstone amortizes the inception value to income over 15 years, representing the life of the fuel supply agreement.

The Corporation has determined the fair values of derivative financial instruments as follows:

Interest rate swaps	<ul style="list-style-type: none"> • The interest rate swap contract's fair value fluctuates with changes in market interest rates. • A discounted cash flow valuation based on a forward interest rate curve was used to determine their fair value.
Whitecourt embedded derivative	<ul style="list-style-type: none"> • The determination of the fair value of the embedded derivative requires the use of option pricing models involving significant judgment based on management's estimates and assumptions, including estimates on the forward Alberta power pool prices, volatility, credit spreads, cost and inflation escalators and fuel supply volumes, electricity sales and EPC generation.

Due to the lack of observable market quotes on the Whitecourt embedded derivatives, the contract has been classified as level 3 financial instruments.

Capstone, with the assistance of third-party experts, is responsible for performing the valuation of financial instruments, including level 3 fair values. The valuation processes and results are reviewed and approved each reporting period. These critical estimates are discussed as part of the Audit Committee's quarterly review of the financial statements.

The following table illustrates the classification of the Corporation's financial instruments, that have been recorded at fair value:

	Level 1 Quoted prices in active markets for identical assets	Level 2 Significant other observable inputs	Level 3 Significant unobservable inputs	Dec 31, 2018	Dec 31, 2017
Recurring measurements:					
Derivative contract assets:					
Whitecourt embedded derivative ⁽¹⁾	—	—	7,478	7,478	13,406
Interest rate swap contracts	—	6,373	—	6,373	7,958
Less: current portion	—	(1,996)	—	(1,996)	(1,130)
	—	4,377	7,478	11,855	20,234
Derivative contract liabilities:					
Interest rate swap contracts	—	2,144	—	2,144	2,144
	—	2,144	—	2,144	2,144

(1) Whitecourt's embedded derivative consists of a \$11,362 fair value asset and \$3,884 amortized contra-asset, set up on inception (2017 - \$17,643 fair value asset, offset by the \$4,237 of contra-asset).

Fair value continuity for Level 3 inputs

	2018	2017
Opening balance, January 1,	13,406	13,674
Change in value of the embedded derivative included in other gains and (losses) in net income	(3,841)	5,044
Settlement of Whitecourt embedded derivative during the period	(2,439)	(5,664)
Amortization of Whitecourt embedded derivative inception value included in other gains and (losses) in net income	352	352
Closing balance, December 31,	7,478	13,406

Income and Expenses From Financial Instruments

	Dec 31, 2018	Dec 31, 2017
Financial instruments designated as amortized cost:		
Interest income on cash and cash equivalents, restricted cash ^{(1), (2)}	1,265	653
Financial instruments classified as FVTPL (refer to note 22):		
Unrealized gain (loss) on the Whitecourt embedded derivative	(3,489)	5,396
Unrealized gain (loss) on interest rate swap contracts	(1,585)	4,534
	(5,074)	9,930
Other liabilities:		
Interest expense on long-term debt ⁽²⁾	(38,797)	(36,668)
	(38,797)	(36,668)

(1) Interest income for 2018 of \$5,139 includes the final payment of \$3,348 for full repayment of the Chapais loans and investments, which were previously written down to nil, interest income on cash balances of \$1,265 (2017 - \$653) and other interest payments from Chapais of \$526 (2017 - \$947).

(2) Interest expense on the long-term debt for 2018 of \$38,797 includes amortization of deferred financing fees and accretion on liability for asset retirement obligations of \$2,276 and \$436, respectively (2017 - \$2,121 and \$334).

NOTE 8. FINANCIAL RISK MANAGEMENT

The Corporation's normal operating, investing and financing activities expose it to a variety of financial risks, including market risk, credit risk, economic dependence and liquidity risk. The Corporation's overall risk management process is designed to identify, manage and mitigate business risk, which includes, among others, financial risk.

(A) Market Risk

Market risk is the risk or uncertainty arising from possible price movements and their impact on the future performance of the business. The Corporation is exposed to commodity price risk (electricity revenue), interest rate and inflation risk, foreign currency exchange risk and other indices that could adversely affect the value of the Corporation's financial assets, liabilities or expected future cash flows.

Commodity price risk

In 2018, both Cardinal and Whitecourt's revenues are exposed to price risk as follows:

- (i) Cardinal earns a portion of its revenue by supplying electricity to the Ontario grid only when profitable to do so.
- (ii) Whitecourt sells all electricity generated into the Power Pool of Alberta. Millar Western and Whitecourt's fuel supply agreement includes sharing mechanisms regarding the price received for electricity sold by Whitecourt.

Interest rate and inflation risk

Interest rate risk arises as changes in market interest rates affect the Corporation's future payments on debt obligations. The Corporation is exposed to interest rate risk on its floating rate debt. Currently, the Corporation has interest rate swap contracts to mitigate some of the risks associated with its long-term debt.

The terms of the contracts are:

Entity	Maturity Date	Notional Amount	Swap Fixed Rate	Stamping Fee / Margin	Effective Interest Rate
GHG	Jun 30, 2021	67,657	1.34% - 1.45%	1.63% - 1.88%	2.97% - 3.33%
GHG	Jun 30, 2034	57,363	3.04% - 3.17%	1.88%	4.92% - 5.50%
Cardinal	Dec 30, 2022	60,728	1.24%	1.63%	2.87%
Cardinal	Jun 30, 2034	41,292	2.77%	1.63%	4.40%
Grey Highlands Clean	Sep 30, 2021	48,823	1.24%	1.63% - 1.88%	2.87% - 3.12%
Grey Highlands Clean	Sep 30, 2034	41,616	2.61%	1.88%	4.49%
Snowy Ridge	Dec 31, 2021	28,016	1.13%	1.63% - 1.88%	2.76% - 3.01%
Snowy Ridge	Dec 31, 2034	21,011	2.07%	1.88%	3.95%
Settlers Landing	Jun 30, 2022	24,077	1.71%	1.63% - 1.88%	3.34% - 3.59%
Settlers Landing	Jun 30, 2035	17,719	2.93%	1.88%	4.81%

Foreign currency exchange risk

Capstone's power assets have expenses or capital commitments in currencies other than the Canadian dollar; as new projects are built, expected additional purchases will be made in foreign currencies. To mitigate these risks Capstone monitors the risk associated with foreign exchange rate fluctuations and, from time to time, may enter into forward foreign exchange contracts or employ other hedging strategies.

(B) Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to honour a financial obligation.

Financial instruments that potentially subject the Corporation to concentrations of credit risk consist of cash and cash equivalents, restricted cash, accounts receivable and derivative contracts.

The Corporation deposits its cash with reputable financial institutions and limits the exposure by counterparty; management therefore believes the risk of loss to be remote.

Credit risk concentration with respect to power trade receivables is limited due to the Corporation's customer base being predominantly government authorities. The table below summarizes power trade receivables from the sale of electricity and government incentive programs by counterparty:

As at	Dec 31, 2018	Dec 31, 2017
Independent Electricity System Operator ("IESO")	12,642	13,759
Nova Scotia Power Inc. ("NSPI")	3,904	4,118
Natural Resources Canada Inc. ("NRC")	3,074	1,177
Ontario Electricity Financial Corporation ("OEFC")	1,597	1,711
Other	4,260	3,643
	<u>25,477</u>	<u>24,408</u>

There are no accounts receivable that are past due. Since the IESO, OEFC, and NRC are government agencies and NSPI is regulated by the provincial government, management considers credit risk to be minimal.

The Corporation's derivative agreements expose Capstone to losses under certain circumstances, such as the counterparty defaulting on its obligations under the swap agreements or if the swap agreements provide an imperfect hedge. Counterparties to the Corporation's derivative contracts are major financial institutions that have been accorded investment-grade ratings. Consequently, management believes there to be minimal credit risk associated with its derivative contracts.

(C) Economic Dependence

Economic dependence arises when an enterprise relies on a significant volume of business with another party that cannot be easily transferred at similar terms and conditions, or is abnormal relative to expectations of similar entities. The table below summarizes revenue from the sale of electricity by counterparty for the power segment:

For the year ended	Dec 31, 2018	Dec 31, 2017
IESO	119,522	112,160
NSPI	32,845	12,451
OEFC	7,521	8,855
Other	23,741	20,697
	<u>183,629</u>	<u>154,163</u>

(D) Liquidity Risk

Liquidity risk is the risk that the Corporation may have insufficient cash or other resources to meet obligations as they come due.

Compliance with debt covenants

The Corporation has financial liabilities in its power operating segments and at corporate. Refer to notes 14 accounts payable and other liabilities and 15 long-term debt for further details on financial liabilities. These financial liabilities contain a number of standard financial and other covenants.

Failure to comply with terms and covenants of the Corporation's credit agreements could result in a default, which, if not cured or waived, could result in accelerated repayment or the suspension of preferred dividends.

In the event of default, there can be no assurance that the Corporation could:

- (i) Generate sufficient cash flow from operations in amounts sufficient to pay outstanding indebtedness, or to fund any other liquidity needs; or
- (ii) Pay future preferred dividends; or
- (iii) Refinance these credit agreements or obtain additional financing on commercially reasonable terms, if at all. The credit agreements, and future borrowings may be at variable rates of interest, which exposes the Corporation to the risk of increased interest rates.

Contractual maturities

The contractual maturities of the Corporation's financial liabilities as at December 31, 2018 were as follows:

Financial Liabilities	Within one year	One year to five years	Beyond five years	Total
Accounts payable and other liabilities	19,468	—	—	19,468
Derivative financial instruments				
Interest rate swaps	—	1,079	1,065	2,144
Long-term debt				
Principal payments	49,355	247,003	472,207	768,565
Interest payments	31,422	106,486	130,126	268,034
	<u>80,777</u>	<u>353,489</u>	<u>602,333</u>	<u>1,036,599</u>

(E) Sensitivity Analysis

The sensitivity analysis provided below discloses the effect on net income for the year ended December 31, 2018, assuming that a reasonably possible change in the relevant risk variable has occurred during the year, and has been applied to the risk exposures in existence at that date to show the effects of reasonably possible changes. The changes in market variables used in the sensitivity analysis were determined based on implied volatilities, where available, or historical data.

The sensitivity analysis has been prepared based on December 31, 2018 balances and on the basis that the balances, the ratio of fixed to floating rates of debt and derivatives, the energy contracts that are financial instruments in place at December 31, 2018 are all constant. Excluded from this analysis are all non-financial assets and liabilities that are not classified as financial instruments under IFRS 9.

The sensitivity analysis provided is hypothetical and should be used with caution because the impacts provided are not necessarily indicative of the actual impacts that would be experienced, as the Corporation's actual exposure to market rates is constantly changing as the Corporation's portfolio of commodity, debt, foreign currency and equity contracts changes. Changes in fair values or cash flows based on a variation in a market variable cannot be extrapolated because the relationship between the change in the market variable and the change in fair value or cash flows may not be linear. In addition, the effect of a change in a particular market variable on fair values or cash flows is calculated without considering interrelationships between the various market rates, hedging strategies employed by the Corporation or other mitigating actions that would be taken by the Corporation.

The table summarizes the impact on fair value of changes in the Whitecourt embedded derivatives' significant unobservable inputs:

Dec 31, 2018	Unobservable inputs	Estimated input	Relationship of input to fair value
\$7,478	Forward Alberta power pool prices	From \$34/MWh to \$84/MWh over the next 11 years.	A reasonably possible increase in estimated forward prices of 5% or a decrease of 5%, would cause fair value to decrease by \$3,025 and increase by \$3,394, respectively.

Changes in these estimates may have a significant impact on the fair value of the embedded derivative given the length of contract involved. As new information becomes available, management may choose to revise these estimates where there is an absence of reliable observable market data.

The table summarizes the impact on fair value of changes in observable inputs:

For the year ended Dec 31, 2018	Carrying Amount	Interest Rate Risk (0.5)%	0.5%
Financial assets:			
Interest rate swap assets, net	4,229	(8,709)	8,251
Financial liabilities:			
Long-term debt ⁽¹⁾	45,000	225	(225)

(1) Long-term debt excludes all fixed-rate debt totaling \$496,852 and variable rate debt that is covered by a swap for fixed-rate debt totaling \$226,713.

NOTE 9. EQUITY ACCOUNTED INVESTMENTS

Beginning December 31, 2017, Capstone no longer follows the equity accounting method for any of its investments. This is a result of the March 3, 2017 sale of Capstone's interest in Värmevärden and the December 31, 2017 acquisition of the remaining interests in the Glen Dhu and Fitzpatrick wind facilities. As a result, the statement of financial position no longer holds an interest in Värmevärden and Capstone consolidates the wind facilities. In addition, Capstone's income statement includes equity accounting for the periods up to the disposal or acquisition of the respective investments. Refer to note 3 for details of both transactions.

The changes in the Corporation's total equity accounted investments for the year ended were as follows:

For the year ended	Opening Balance	Equity Accounted Income (Loss)	Distributions Received ⁽¹⁾	Acquisition of remaining interests	Ending Balance
Dec 31, 2017	22,464	935	(2,352)	(21,047)	—

(1) Distributions received were from Glen Dhu.

The Corporation has summarized its equity accounted investments using their gross values as follows:

For the year ended	Dec 31, 2017		
	Glen Dhu	Fitzpatrick	Total
Summarized Statements of Income			
Revenue	21,214	237	21,451
Net income and total comprehensive income	3,874	(91)	3,783
Capstone's interest (refer to note 3)	49%	50%	
Subtotal	1,898	(46)	1,852
Amortization of fair value adjustments and other	(876)	(41)	(917)
Total	1,022	(87)	935
Net income to Capstone			935

NOTE 10. CAPITAL ASSETS

(A) Continuity

	Jan 1, 2018	Additions	Disposals	Transfers (ref. to note 12)	Business Acquisition	Dec 31, 2018
Cost						
Land	1,084	—	—	—	—	1,084
Equipment and vehicles	10,877	179	(44)	—	—	11,012
Property and plant	1,220,000	3,356	(3,884)	1,427	—	1,220,899
	1,231,961	3,535	(3,928)	1,427	—	1,232,995
Accumulated depreciation						
Equipment and vehicles	(7,181)	(330)	38	—	—	(7,473)
Property and plant	(328,403)	(66,455)	3,135	—	—	(391,723)
	(335,584)	(66,785)	3,173	—	—	(399,196)
Net carrying value	896,377	(63,250)	(755)	1,427	—	833,799

	Jan 1, 2017	Additions	Disposals	Transfers (ref. to note 11)	Business Acquisition	Dec 31, 2017
Cost						
Land	1,051	—	—	—	33	1,084
Equipment and vehicles	10,542	364	(29)	—	—	10,877
Property and plant	1,062,391	17,603	(11,829)	33,633	118,202	1,220,000
	1,073,984	17,967	(11,858)	33,633	118,235	1,231,961
Accumulated depreciation						
Equipment and vehicles	(6,126)	(1,084)	29	—	—	(7,181)
Property and plant	(280,587)	(55,878)	8,062	—	—	(328,403)
	(286,713)	(56,962)	8,091	—	—	(335,584)
Net carrying value	787,271	(38,995)	(3,767)	33,633	118,235	896,377

(B) Reconciliation to Cash Additions for the Cash Flow Statement

For the year ended	Dec 31, 2018	Dec 31, 2017
Additions	3,535	17,967
Adjustment for change in capital asset additions included in accounts payable and accrued liabilities	486	(1,942)
Cash additions	4,021	16,025

NOTE 11. PROJECTS UNDER DEVELOPMENT

(A) Continuity

	2018	2017
As at January 1	730	22,267
Capitalized costs during the year ⁽¹⁾	865	14,383
Costs transferred to capital assets ⁽²⁾ (refer to note 10)	—	(33,633)
Costs transferred to intangibles ⁽²⁾ (refer to note 12)	—	(2,287)
As at December 31 ⁽³⁾	1,595	730

(1) There were no capitalized borrowing costs in 2018 (2017 - includes \$123 of capitalized borrowing costs during the construction of the Settlers Landing).

(2) In 2017, amounts were transferred on the COD of Settlers Landing.

(3) PUD balance as at December 31, 2018 relates to the Riverhurst and Buffalo Atlee 1, 2 and 3 (collectively "Buffalo Atlee") wind development projects. In December 2018, Capstone and its 25% partner Sawridge First Nation ("Sawridge") confirmed that the Buffalo Atlee wind development projects executed Renewable Electricity Support Agreements in Alberta.

(B) Reconciliation to Cash Additions for the Cash Flow Statement

For the year ended	Dec 31, 2018	Dec 31, 2017
Additions	865	14,383
Adjustment for change in additions to PUD included in accounts payable and accrued liabilities	(72)	3,853
Cash additions	793	18,236

NOTE 12. INTANGIBLE ASSETS

	Jan 1, 2018	Additions	Disposals	Transfers (ref. to note 10)	Dec 31, 2018
Assets					
Computer software	257	7	—	—	264
Electricity supply and other contracts	173,103	—	(269)	(1,427)	171,407
Water rights	73,018	—	—	—	73,018
	246,378	7	(269)	(1,427)	244,689
Accumulated amortization					
Computer software	(257)	(2)	—	—	(259)
Electricity supply and other contracts	(56,130)	(9,063)	—	—	(65,193)
Water rights	(22,259)	(2,117)	—	—	(24,376)
	(78,646)	(11,182)	—	—	(89,828)
Net carrying value	167,732	(11,175)	(269)	(1,427)	154,861

	Jan 1, 2017	Additions	Transfers (ref. to note 11)	Business Acquisition	Dec 31, 2017
Assets					
Computer software	257	—	—	—	257
Electricity supply and other contracts	149,039	281	2,287	21,496	173,103
Water rights	73,018	—	—	—	73,018
	222,314	281	2,287	21,496	246,378
Accumulated amortization					
Computer software	(257)	—	—	—	(257)
Electricity supply and other contracts	(48,427)	(7,703)	—	—	(56,130)
Water rights	(20,137)	(2,122)	—	—	(22,259)
	(68,821)	(9,825)	—	—	(78,646)
Net carrying value	153,493	(9,544)	2,287	21,496	167,732

NOTE 13. INCOME TAXES

(A) Deferred Income Tax

As at	Dec 31, 2018	Dec 31, 2017
Deferred income tax assets	125	—
Deferred income tax liabilities	(89,962)	(89,243)
Net deferred income tax liability	(89,837)	(89,243)

The net deferred income tax liability, without taking into consideration the offsetting of balances within the same jurisdiction, are detailed as follows:

As at	Dec 31, 2018	Dec 31, 2017
Non-capital loss carry forwards	23,435	27,375
Other	3,464	420
Asset retirement obligations	2,543	2,294
Deferred income tax assets	29,442	30,089
Capital assets	(72,720)	(75,349)
Intangibles	(40,807)	(36,853)
Financial instruments	(3,119)	(5,011)
Loan premium and deferred financing costs	(2,137)	(1,600)
Other	(496)	(519)
Deferred income tax liabilities	(119,279)	(119,332)
Net deferred income tax liability	(89,837)	(89,243)

A continuity of the net deferred income tax liability follows:

	2018	2017
Net deferred income tax liability as at January 1	(89,243)	(57,923)
Business acquisition ⁽¹⁾	203	(15,060)
Recorded in earnings	(1,745)	(17,170)
Other	948	910
Net deferred income tax liability as at December 31	(89,837)	(89,243)

(1) Refer to note 3.

(B) Timing of Deferred Income Tax Reversal

The timing of deferred income tax reversal is summarized as follows:

As at	Dec 31, 2018	Dec 31, 2017
Within 12 months	40,542	46,488
After more than 12 months	(130,379)	(135,731)
Net deferred income tax liability	(89,837)	(89,243)

(C) Tax Loss Carry Forwards

Capstone's tax loss carry forwards and the portion recognized in deferred income tax assets were as follows:

	Expiry	Recognized	Unrecognized	Dec 31, 2018	Dec 31, 2017
Canadian – non-capital losses	2025 – 2037	87,910	63,973	151,883	169,340
US – non-capital losses	2023 – 2027	—	19,730	19,730	18,143
Canadian – capital losses	No expiry	—	—	—	908

The Corporation also has \$2,080 of unrecognized deferred tax assets, which have not been recognized as at December 31, 2018 (2017 - \$1,699).

(D) Rate Reconciliation

The following table reconciles the expected income tax expense using the statutory tax rate to the expense:

For the year ended	Dec 31, 2018	Dec 31, 2017
Income (loss) before income taxes ⁽¹⁾	5,912	6,600
Statutory income tax rate	26.65%	26.50%
Income tax expense based on statutory income tax rate	1,576	1,749
Permanent differences	203	861
Tax rate differentials	266	(38)
Change in unrecognized deferred tax assets	55	(4,628)
Impact of sale of Värmevärdan	—	20,901
Other	(85)	(1,304)
Total income tax expense (recovery)	2,015	17,541

(1) Income (loss) before income taxes excludes discontinued operations.

The statutory income tax rate of 26.65% (2017 - 26.50%) changes in response to Capstone's allocation of taxable income to different tax jurisdictions.

(E) Current Income Taxes

Current income taxes payable of \$2,150 are included in accounts payable and other liabilities on the statement of financial position (refer to note 14) (2017 - \$2,439).

NOTE 14. ACCOUNTS PAYABLE AND OTHER LIABILITIES

	Dec 31, 2018	Dec 31, 2017
Dividends payable	409	409
Income taxes payable	2,150	2,439
Other accounts payable and accrued liabilities	16,909	17,409
	19,468	20,257

Income taxes payable	Dec 31, 2018	Dec 31, 2017
Canadian Renewable and Conservation Expense ("CRCE") penalties ⁽¹⁾	1,708	2,274
Taxes payable (recovery) on preferred share dividends	138	24
Current income taxes payable (recovery)	304	141
	2,150	2,439

(1) CRCE penalties related to flow-through shares originally issued by Renewable Energy Developers Inc., which was acquired by Capstone in 2013.

NOTE 15. LONG-TERM DEBT

(A) Power

As at	Dec 31, 2018		Dec 31, 2017	
	Fair Value	Carrying Value	Fair Value	Carrying Value
CPC credit facilities	45,000	45,000	65,915	65,915
Wind - Operating	520,080	511,927	551,782	544,382
Solar	73,772	76,093	78,772	81,632
Hydros	75,045	74,817	77,092	77,502
Gas	60,728	60,728	64,259	64,259
	774,625	768,565	837,820	833,690
Less: deferred financing costs		(13,871)		(15,148)
Long-term debt		754,694		818,542
Less: current portion		(49,355)		(86,208)
		705,339		732,334

Capstone has a cumulative \$51,168 utilized on its letter of credit facilities.

The respective project debt within the power segment have regular principal and interest payments over the term to maturity and are secured only by the assets of respective project, with no recourse to the Corporation's other assets, except as noted.

In addition, the individual project debt agreements require the respective projects to maintain certain restrictive covenants including a minimum debt service coverage ratio to allow distributions to Capstone.

(i) CPC Credit Facilities

	Interest Rate ⁽¹⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Total available credit - all facilities			140,000	145,000
Amount drawn				
Term credit facility ⁽²⁾	3.74%	Dec 15, 2021	45,000	50,000
Revolving credit facility ⁽³⁾			—	15,915
Letter of credit facility ⁽⁴⁾			36,859	27,812
Remaining available credit			58,141	51,273

(1) The effective rate was 3.74% in 2018 based on a variable rate plus an applicable margin.

(2) In Q2 2018, CPC repaid \$5,000 of its term credit facility.

(3) In Q1 2018, CPC repaid \$15,915 of its revolving credit facility under the CPC Credit Facilities, increasing the revolving credit facility capacity.

(4) As at December 31, 2018, Capstone had 21 letters of credit authorized under the revolving facility.

The CPC Credit Facilities mature on December 15, 2021, bear interest at a variable rate plus an applicable margin and have a minimum annual principal repayment of \$5,000 on the term facility. Subsequent to 2021, the CPC Credit Facilities have a rolling one-year extension option, subject to lender approval.

Under the CPC Credit Facilities, CPC is subject to customary covenants, including specific limitations on leverage and interest coverage ratios, and a minimum cash flow profile. The collateral for the CPC Credit Facilities is provided by Capstone, CPC, and its material subsidiaries. CPC and its material subsidiary guarantors (with the exception of certain subsidiaries, including previously encumbered project financed subsidiaries) provided demand debentures granting a first ranking security interest in all present and future property and a floating charge over real property and first ranking securities pledge agreements (subject to certain permitted liens). Capstone provided a limited recourse guarantee, a securities pledge agreement, and an assignment of indebtedness owed to Capstone by CPC.

(ii) Wind - Operating

Project debt	Dec 31, 2018	Dec 31, 2017
Glen Dhu	83,220	88,885
Goulais	68,354	72,169
GHG	66,934	70,647
Erie Shores	61,655	67,977
Saint-Philémon	50,469	52,952
Grey Highlands Clean	46,827	49,320
Amherst	34,948	37,223
Snowy Ridge	27,877	29,083
Settlers Landing	24,347	25,160
SkyGen ⁽¹⁾	18,597	20,360
Skyway 8 ⁽¹⁾	17,658	18,337
Glace Bay	11,041	12,269
	<u>511,927</u>	<u>544,382</u>

(1) SkyGen project debt includes financing related to the Ferndale, Ravenswood, and Proof Line facilities. Skyway 8 was financed separately as it reached COD at a later date.

Glen Dhu	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	5.33%	Dec 31, 2030	83,220	88,885

(1) In 2018, Glen Dhu replaced its standby loan facility with a \$5,310 letter of credit to fund its debt service reserve requirement. There were no draws on the standby loan facility during the year prior to the cancellation of the standby loan facility.

Goulais	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	5.16%	Sep 30, 2034	68,354	72,169

(1) Goulais is required to set aside \$3,392 as restricted cash to cover the debt service reserve.
(2) Goulais is required to set aside \$1,000 as letters of credit to cover the operating and maintenance reserves.

GHG	Interest Rate ⁽²⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	3.08%	Aug 26, 2021	66,934	70,647

(1) GHG has \$3,200 as letters of credit to cover the debt service reserve.
(2) As at December 31, 2018, GHG had swap contracts to convert interest to a fixed rate (See note 8a).

Erie Shores ⁽³⁾	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Tranche A	5.96%	Apr 1, 2026	37,159	40,982
Tranche C	6.15%	Apr 1, 2026	24,496	26,995
			<u>61,655</u>	<u>67,977</u>

(1) Erie Shores project debt has a \$5,000 limited recourse guarantee provided by CPC to the lenders of the Erie Shores project debt.
(2) Erie Shores is required to set aside \$5,269 as restricted cash and \$550 as letters of credit against the borrowing capacity of the CPC revolving credit facility to cover the debt service and maintenance reserves.
(3) Tranche B matured on April 1, 2016.

Saint-Philémon	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	5.49%	May 31, 2034	50,469	52,952

(1) Saint-Philémon is required to set aside \$1,224 as letters of credit against the borrowing capacity of the CPC revolving credit facility to cover the debt service reserve.

Grey Highlands Clean	Interest Rate ⁽²⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	2.87%	Dec 23, 2021	46,827	49,320

(1) Grey Highlands Clean is required to set aside \$2,100 as letters of credit to cover the debt service reserve.
(2) As at December 31, 2018, Grey Highlands Clean had swap contracts to convert interest to a fixed rate (See note 8a).

Amherst	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	6.20%	Apr 30, 2032	34,948	37,223

(1) Amherst's project debt has a \$1,000 limited recourse guarantee provided by CPC to the lenders of the Amherst project debt.
(2) Amherst is required to set aside \$1,102 as letters of credit against the borrowing capacity of the CPC revolving credit facility to cover the debt service and maintenance reserves.

Snowy Ridge	Interest Rate ⁽²⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	2.75%	Dec 23, 2021	27,877	29,083

- (1) Snowy Ridge is required to set aside \$3,443 as restricted cash to cover construction holdbacks with vendors and \$1,300 as letters of credit to cover the debt service reserve.
(2) As at December 31, 2018, Snowy Ridge had swap contracts to convert interest to a fixed rate (See note 8a).

Settlers Landing	Interest Rate ⁽²⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	3.34%	Aug 31, 2022	24,347	25,160

- (1) Settlers Landing is required to set aside \$2,023 as restricted cash to cover construction holdbacks with vendors and \$1,100 as letters of credit to cover the debt service reserve.
(2) As at December 31, 2018, Settlers Landing had swap contracts to convert interest to a fixed rate (See note 8a).

SkyGen	Interest Rate	Maturity ⁽²⁾	Dec 31, 2018	Dec 31, 2017
Term loans	4.90%	Jul 17, 2021	18,597	20,360

- (1) SkyGen is required to set aside \$1,334 as letters of credit to cover the debt service reserve.
(2) On July 17, 2018, the SkyGen project debt was refinanced, decreasing the current portion by \$18,565. The new debt matures in 2021 and amortizes over the same period as the prior debt, carrying a fixed interest rate of 4.90%.

Skyway 8	Interest Rate	Maturity ⁽²⁾	Dec 31, 2018	Dec 31, 2017
Term loan	4.90%	Jul 17, 2021	17,658	18,337

- (1) Skyway 8 is required to set aside \$766 as letters of credit to cover the debt service reserve.
(2) On July 17, 2018, the Skyway 8 project debt was refinanced, decreasing the current portion by \$17,658. The new debt matures in 2021 and amortizes over the same period as the prior debt, carrying a fixed interest rate of 4.90%.

Glacé Bay	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	5.99%	Mar 15, 2027	6,145	6,685
Term loan	6.36%	Apr 21, 2019	230	799
Term loan	4.72%	Oct 1, 2032	4,666	4,785
			<u>11,041</u>	<u>12,269</u>

- (1) Glacé Bay is required to set aside \$2,501 as restricted cash to cover the debt service and operating and maintenance reserves.

(iii) Solar

Amherstburg project debt	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Amherstburg project debt	3.49%	Dec 31, 2030	76,093	81,632

- (1) Amherstburg is required to set aside \$4,527 as letters of credit against the borrowing capacity of the CPC revolving credit facility to cover the debt service and maintenance reserves.

(iv) Hydros

	Interest Rate	Maturity	Dec 31, 2018	Dec 31, 2017
Senior secured bonds	4.56%	Jun 30, 2040	55,493	57,693
Subordinated secured bonds	7.00%	Jun 30, 2041	19,324	19,809
			<u>74,817</u>	<u>77,502</u>

- (1) The hydro facilities are required to set aside \$10,102 as letters of credit against the borrowing capacity of the CPC revolving credit facility to cover the debt service and maintenance reserves.

(v) Gas

Term loan	Interest Rate ⁽²⁾	Maturity	Dec 31, 2018	Dec 31, 2017
Term loan	2.87%	Mar 18, 2023	60,728	64,259

- (1) Cardinal is required to set aside \$1,558 as restricted cash to cover the operating and maintenance reserves and \$2,700 as letters of credit to cover the debt service reserve.
(2) As at December 31, 2018, Cardinal had swap contracts to convert interest to a fixed rate (See note 8a).

(B) Long-term Debt Covenants

For the year ended and as at December 31, 2018, the Corporation and its subsidiaries complied with all financial and non-financial debt covenants.

(C) Long-term Debt Repayments

The following table summarizes total principal payments required under each of the Corporation's facilities in the next five years and thereafter:

Year of Repayment	Within one year	One year to five years	Beyond five years	Total
Power	49,355	247,003	472,207	768,565

NOTE 16. LIABILITY FOR ASSET RETIREMENT OBLIGATION

The carrying value of these obligations is based on estimated cash flows required to settle these obligations in present day costs. The costs relate to site restoration and decommissioning of Cardinal and the operating wind and hydro power facilities. The following table provides the underlying assumptions and reconciles the Corporation's total asset retirement obligation activity:

	Dec 31, 2018	Dec 31, 2017
Assumptions:		
Expected settlement date	2020– 2078	2020– 2062
Inflation rate	2.0%	2.0%
Credit adjusted discount rate	4.75% - 5.75%	3.5% - 5.75%
Balance, beginning of year	10,161	7,165
Business acquisition	—	1,598
Revision of estimates	(1,155)	1,009
Liabilities incurred	—	55
Accretion expense	436	334
Balance, end of year	<u>9,442</u>	<u>10,161</u>

NOTE 17. SHAREHOLDERS' EQUITY

The following table summarizes the Corporation's share capital:

As at	Dec 31, 2018	Dec 31, 2017
Common and Class A shares	62,270	62,270
Preferred shares	72,020	72,020
	<u>134,290</u>	<u>134,290</u>

(A) Common and Class A Shares

Capstone is authorized to issue an unlimited number of common and Class A shares, all of which have the same rights and attributes.

Continuity for the year ended (000s shares and \$000s)	Dec 31, 2018		Dec 31, 2017	
	Shares	Carrying Value	Shares	Carrying Value
Opening balance	304,609	62,270	227,733	40,433
Issuance of Class A shares ⁽¹⁾	—	—	76,876	86,332
Return of capital ⁽¹⁾	—	—	—	(86,332)
Business acquisition ⁽²⁾	—	—	—	21,837
Ending balance	<u>304,609</u>	<u>62,270</u>	<u>304,609</u>	<u>62,270</u>

- (1) On March 31, 2017, Irving converted the remaining SEK tranche of the promissory note payable into 76,876 newly issued Class A shares, which increased share capital by \$86,332. Additionally, Capstone distributed \$86,332 to Irving as a return of capital which impacted share capital. The transaction did not change the value of Capstone's Class A shares. Refer to note 3 for details.
- (2) Refer to note 3 for changes related to the acquisition of remaining interests of wind facilities.

(B) Preferred Shares

Capstone is authorized to issue preferred shares equal to 50% of the outstanding common shares. As at December 31, 2018 and 2017, there were 3,000 series A preferred shares issued and outstanding, with a carrying value of \$72,020.

The series A preferred shares have a cumulative discretionary dividend, which resets on each 5-year anniversary; the next anniversary date is July 31, 2021. The shares are non-voting and redeemable at the Corporation's discretion.

In accordance with the terms of the share agreement, all preferred shares accrue dividends at a fixed rate of 3.271% per annum and preferred dividends are paid quarterly.

(C) Dividends

No dividends were declared in 2018 or 2017 in respect of the Corporation's common shareholders.

For the year ended	Dec 31, 2018	Dec 31, 2017
Preferred shares declared ^{(1), (2)}	2,486	2,523

(1) Includes \$34 of deferred income taxes for the year ended December 31, 2018 (2017 - \$71).

(2) Capstone has included \$409 of accrued preferred dividends as declared on November 14, 2018 (2017 - \$409).

(D) Capital Management

The Corporation manages its capital, which is defined as the aggregate of long-term debt and preferred shareholders' equity, to achieve the following objectives:

- Maintain a capital structure that provides financial flexibility to the Corporation to ensure access to debt on commercially reasonable terms, without exceeding its debt capacity;
- Maintain financial flexibility in order to preserve its ability to meet financial obligations, including debt servicing payments and distribution payments; and
- Deploy capital to provide an appropriate investment return to its security holders.

The Corporation's financial strategy is designed to maintain a capital structure consistent with the objectives stated above and to respond to changes in economic conditions. In doing so, the Corporation may receive capital contributions from its common shareholder, issue additional shares, issue additional debt, issue debt to replace existing debt with similar or different characteristics, or adjust the amount of dividends paid to shareholders.

The Corporation's financing and refinancing decisions are made on a specific transaction basis and depend on such things as the Corporation's needs and economic conditions at the time of the transaction.

The Corporation is not subject to any external capital requirements and is in compliance with all debt covenants as described in note 15.

NOTE 18. NON-CONTROLLING INTERESTS

(A) Non-controlling Interests

Non-controlling interests represent ownership interests by third parties in businesses consolidated by Capstone. Amherst, Saint-Philémon, Chi-Wiikwedong, GHG, Snowy Ridge ("SR"), Settlers Landing ("SL"), and Buffalo Atlee non-controlling interests as at December 31, 2018 were:

- Amherst is 49% owned by Firelight Infrastructure Partners LP ("Firelight").
- Saint-Philémon is 48.9% owned by Municipalité Régionale de Comté de Bellechasse and 0.1% owned by Municipalité de Saint-Philémon (the "Municipal partners").
- Goulais is 49% owned by Batchewana First Nation ("BFN").
- GHG, SR and SL have a debenture with a subsidiary of One West Holdings Ltd. ("Concord"), convertible into a 50% ownership interest in the projects.
- Buffalo Atlee is 25% owned by Sawridge First Nation ("Sawridge").

Capstone has agreements with each partner that govern distributions from these investments. In addition, distributions must also comply with the respective debt agreements.

The balances and changes in non-controlling interests are:

	Firelight's interest in Amherst	Municipal interest in Saint- Philémon	BFN's interest in Goulais ⁽¹⁾	Concord's interest in GHG, SR & SL	Total
January 1, 2017	9,574	2,335	20,038	29,470	61,417
NCI portion of net income	736	196	61	—	993
Dividends declared	(931)	(1,035)	(1,274)	—	(3,240)
Net convertible debenture repayments	—	—	—	(3,921)	(3,921)
As at December 31, 2017	9,379	1,496	18,825	25,549	55,249
NCI portion of net income	1,313	162	118	—	1,593
Dividends declared	(1,764)	(764)	(1,265)	—	(3,793)
Net convertible debenture repayments	—	—	—	(2,963)	(2,963)
As at December 31, 2018	8,928	894	17,678	22,586	50,086

(1) Net income is allocated based on pro-rata share of distributions.

(B) Summarized Information for Material Partly Owned Subsidiaries

As at	December 31, 2018				December 31, 2017			
	Amherst	Saint-Philémon	Goulais	GHG, SR & SL	Amherst	Saint-Philémon	Goulais	GHG, SR & SL
Summarized Statements of Financial Position								
Assets								
Current	2,113	1,953	1,831	405	2,503	2,766	4,225	969
Non-current	54,537	53,419	1,248	68,704	57,532	56,711	2,054	68,704
Liabilities								
Current	(2,588)	(2,276)	(193)	—	(2,768)	(3,410)	(2,494)	—
Non-current	(33,499)	(48,000)	—	—	(35,785)	(49,871)	—	—
Total equity	20,563	5,096	2,886	69,109	21,482	6,196	3,785	69,673
Attributable to:								
Shareholders of Capstone	11,635	4,202	(14,792)	46,523	12,103	4,700	(15,040)	44,115
NCI	8,928	894	17,678	22,586	9,379	1,496	18,825	25,549
	20,563	5,096	2,886	69,109	21,482	6,196	3,785	69,664

For the year ended	December 31, 2018				December 31, 2017			
	Amherst	Saint-Philémon	Goulais	GHG, SR & SL	Amherst	Saint-Philémon	Goulais	GHG, SR & SL
Summarized Statements of Income								
Revenue	9,130	7,795	2,810	5,925	8,662	7,934	2,677	7,418
Total net income and comprehensive income	2,679	330	366	5,928	1,508	401	118	7,408
Attributable to:								
Shareholders of Capstone	1,366	168	248	5,928	772	205	57	7,408
NCI	1,313	162	118	—	736	196	61	—
	2,679	330	366	5,928	1,508	401	118	7,408

For the year ended	December 31, 2018				December 31, 2017			
	Amherst	Saint-Philémon	Goulais	GHG, SR & SL	Amherst	Saint-Philémon	Goulais	GHG, SR & SL
Summarized Statements of Cash Flows								
Operating	5,533	3,347	1,369	5,928	3,440	4,618	6,025	7,421
Investing	(105)	(46)	—	—	—	(36)	—	(1,807)
Financing	(5,752)	(3,912)	(3,750)	(5,925)	(3,804)	(3,017)	(4,210)	(7,418)
Net increase / (decrease) in cash and equivalents	(324)	(611)	(2,381)	3	(364)	1,565	1,815	(1,804)

(C) Convertible debentures with Concord

On November 16, 2015, a subsidiary of CPC issued an unsecured convertible debenture to a subsidiary of Concord. The debenture allows Concord to eventually acquire a 50% interest in the GHG, Snowy Ridge and Settlers Landing projects. Under the terms of the debenture, both Capstone and Concord will equally fund ongoing equity requirements relating to the these projects. In addition, Capstone and Concord will equally share any distributions made from the projects, which are based on the availability of cash from the projects. Distributions to Concord prior to conversion of the debenture are principal repayments. At either Capstone or Concord's option, subject to limited conditions, the debenture is convertible into 50% of the outstanding equity of the entities holding the GHG, Snowy Ridge and Settlers Landing projects. The debenture is classified as an equity instrument in accordance with IAS 32 because there are no fixed payment obligations, including principal and interest. The debenture is included in the non-controlling interest component within the consolidated statement of shareholders' equity because it is attributable to Concord's interest in the GHG, Snowy Ridge and Settlers Landing projects. The initial principal contribution of the debenture was \$31,408. The face value decreased to \$25,549 as at December 31, 2017 and \$22,586 as at December 31, 2018.

NOTE 19. SHARE-BASED COMPENSATION

(A) Share Appreciation Rights Plan

On April 1, 2017, a SAR plan was approved by the board. The SAR plan allows up to 15,230,458 SAR units, or 5% of the number of shares issued, to be granted. At the beginning of 2018, there were 9,899,791 units outstanding, 380,761 were granted during the year, and there were 10,280,552 units outstanding as at December 31, 2018. A SAR unit entitles the holder to the appreciation in value of one unit over a period of time. The SAR units have a maximum life of 13 years and vest upon a sale transaction, defined as more than 50% of the equity securities of Capstone being sold to a third party. The sale price will determine the ultimate fair value of the SAR units on the vesting date. The SAR units will be settled in cash for individuals who meet the vesting conditions on the vesting date. No liability has been recorded as a sale transaction is not currently probable.

(B) Long-term Incentive Plans

On April 1, 2017, Capstone awarded a discretionary cash-based LTIP to members of senior management. The LTIP accrues based on passage of time, until the vesting date of December 31, 2019. Employees who depart prior to the vesting date will forfeit their LTIP. The LTIP expense included in wages and benefits was \$139 in 2018 (2017 - \$104).

NOTE 20. REVENUE BY NATURE

Capstone's power segment revenue is generated through long-term power contracts which vary in nature as disaggregated below. The corporate activities do not generate revenue.

	For the year ended	
	Dec 31, 2018	Dec 31, 2017
Wind ⁽¹⁾	113,566	93,512
Gas ⁽²⁾	25,269	21,160
Biomass ⁽³⁾	15,402	8,640
Solar	15,059	15,747
Hydro	14,333	15,104
Total Revenue	183,629	154,163

(1) Wind revenue for 2017 excludes the results of Glen Dhu and Fitzpatrick wind facilities, which were equity accounted.

(2) Gas revenue at Cardinal consists of fixed payments for providing capacity and availability based on its PPA and other contracts; the remaining revenue is variable based on production.

(3) Biomass revenue includes \$3,553 of grant funding eligibility for Whitecourt for the year (2017 - \$4,800).

As at December 31, 2018, Capstone has trade receivable balances of \$25,156 (2017 - \$23,723).

NOTE 21. EXPENSES BY NATURE

	For the year ended				For the year ended			
	Dec 31, 2018				Dec 31, 2017			
	Operating	Admin.	Project Development Costs	Total	Operating	Admin.	Project Development Costs	Total
Maintenance & supplies	16,987	—	—	16,987	9,442	—	—	9,442
Wages and benefits	9,918	5,310	—	15,228	9,301	5,787	562	15,650
Property expenses ⁽¹⁾	8,948	490	98	9,536	7,996	497	—	8,493
Fuel and transportation	6,939	—	—	6,939	5,581	—	—	5,581
Professional fees ⁽²⁾	95	364	2,653	3,112	2,492	1,053	1,250	4,795
Power facility administration	2,797	—	—	2,797	2,366	—	—	2,366
Insurance	2,182	120	—	2,302	2,430	129	—	2,559
Other	2,522	1,245	170	3,937	2,682	1,252	278	4,212
Total	50,388	7,529	2,921	60,838	42,290	8,718	2,090	53,098

(1) Property expenses include leases, utilities, and property taxes.

(2) Professional fees include legal, audit, tax and other advisory services.

NOTE 22. OTHER GAINS AND LOSSES

	For the year ended	
	Dec 31, 2018	Dec 31, 2017
Unrealized gains (losses) on derivative financial instruments ⁽¹⁾	(5,074)	9,930
Losses on disposal of capital assets ⁽²⁾	(437)	(3,507)
Other	253	14
Other gains and (losses), net	(5,258)	6,437

(1) Unrealized losses on derivative financial instruments were attributable to a decrease in the Whitecourt embedded derivative asset primarily due to the introduction of EPCs and decreases in assets related to the interest rate swap contracts due to lower long-term interest rates since December 31, 2017.

(2) Losses in 2017 primarily relate to capital assets replaced as part of Whitecourt's refurbishment.

NOTE 23. COMMITMENTS AND CONTINGENCIES

The Corporation, either directly or indirectly through its subsidiaries, has entered into various contracts and commitments in addition to the commitments described in note 7 financial instruments, note 8 financial risk management, notes 15 long-term debt, 16 liability for asset retirement obligation and 17 shareholders' equity as at December 31, 2018 were as follows:

(A) Leases

Minimum operating lease payments comprised:

	Within one year	One year to five years	Beyond five years	Total
Operating leases	4,503	18,271	37,013	59,787

The following leases have been included in the table based on known minimum operating lease commitments as follows:

- Capstone's operating wind facilities and wind development projects have entered into agreements for the use, or option to use, land in connection with the operation of existing and future wind facilities. Payment under these agreements is typically a minimum amount with additional payments dependent on the amount of power generated by the wind facility. The agreements can be renewed and extend as far as 2061.
- Cardinal leases the site on which it is located from Ingredion Canada Corporation ("Ingredion"). Under the lease, Cardinal pays monthly rent. The lease extends through 2034 and expires concurrently with the Energy Savings Agreement between Ingredion and Cardinal.
- Amherstburg leases the land on which its operating facilities are located. The terms of the lease agreements extend to 2036.
- The Corporation has an operating lease for the corporate office ending in 2023.

Capstone's operating lease commitments with no minimum operating lease commitments required were:

- Capstone has agreements with the Provinces of Ontario and British Columbia for the lease of certain lands and water rights necessary for the operation of its hydro power facilities. The payments under these agreements vary based on actual power production. The terms of the lease agreements extend between 2033 and 2042.

(B) Capital Commitments

Capstone enters into capital commitments in the normal course of operations. As part of Capstone's power development operations, Capstone enters various construction and purchase agreements.

(C) Power Purchase Agreements

A significant portion of the Corporation's electricity revenue is earned through long-term PPAs. The majority of these contracts include terms and conditions customary to the industry. For Cardinal's contract, the nature of the material commitments includes: electricity capacity; availability; and production targets. For the remaining power facilities, Capstone is not obligated to deliver electricity; however, in certain circumstances, if a facility fails to meet the performance requirements, the operating facilities' PPA may be terminated after a specified period of time.

(D) Management Services Agreements

Capstone has agreements with all the partially owned wind facilities and development projects, including Amherst, Saint-Philémon, Goulais, GHG, Snowy Ridge and Settlers Landing. For the operating projects, these agreements are primarily for the provision of management and administration services and are based on an agreed percentage of revenue. The development projects additionally include a development fee for the successful completion of the projects, which pays an agreed fee per MW on completion of development.

(E) Wood Waste Supply Agreement

The Whitecourt and Millar Western fuel supply agreement for wood waste includes sharing mechanisms regarding the price received for electricity sold by Whitecourt.

(F) Operations and Maintenance ("O&M") Agreements

Cardinal has a maintenance contract with Siemens Canada Limited covering the gas turbine at Ingredion's 15 MW facility. The contract expires on November 24, 2023.

Capstone has several service and maintenance agreements covering the turbines in operation on various wind facilities. The agreements provide for scheduled and unscheduled maintenance and require annual minimum payments, subject to inflationary increases, as applicable.

Capstone has an O&M agreement with Regional Power OPCO Inc. ("Regional") to operate and maintain the hydro power facilities. Regional is paid a monthly management fee and is eligible for an annual incentive fee. The original agreement expires on November 30, 2021.

(G) Energy Savings Agreement ("ESA")

Cardinal has an ESA with Ingredion which matures on December 31, 2034. Under the terms of the ESA, Cardinal is required to provide O&M services in respect of the 15 MW plant, and supply steam and compressed air to Ingredion for the use of its manufacturing facility. Cardinal entered into a maintenance contract with Siemens Canada Limited in connection with the operation and maintenance of the 15 MW plant in order to support Cardinal's satisfaction of the O&M terms of the ESA.

(H) Guarantees

Capstone has provided limited recourse guarantees on the project debt of certain wind projects totalling \$6,000 as at December 31, 2018. Capstone has also provided a guarantee to the former 25% owner of the Grey Highlands Clean wind facility which provides future contractual payments subsequent to 2019 based on operational performance up to an aggregate amount of \$4,614. The guarantee terminates when the final payment is made on March 21, 2021.

NOTE 24. RELATED PARTY TRANSACTIONS

(A) Transactions with iCON Infrastructure LLP and subsidiaries ("iCON")

Fees earned from iCON Infrastructure Canada Inc. ("iCON Canada"), a subsidiary of iCON, under a shared service arrangement, are reported in the consolidated statements of income as an administrative expense recovery. During 2018, Capstone earned fees of \$232 from iCON Canada (2017 - \$174). As at December 31, 2018, accounts receivable included \$124 due from iCON Canada. Refer to note 3 for a series of equity transactions with iCON.

(B) Compensation of Key Management

Key management includes the Corporation's directors, Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") during the year. Compensation awarded to key management consisted of salaries, directors' fees, short-term employee benefits, long-term incentive plans, and termination benefits paid.

Key Management Compensation for the year ended	Dec 31, 2018	Dec 31, 2017
Salaries, directors' fees and short-term employee benefits	1,173	1,295
Termination benefits	—	1,140
	<u>1,173</u>	<u>2,435</u>

NOTE 25. SEGMENTED INFORMATION

The Corporation's business has one reportable segment, which contains the power operations in order to assess performance and allocate capital, as well as the remaining corporate activities. Management evaluates performance primarily on revenue, expenses and EBITDA. In 2017, there was one other reporting segment which was sold on March 3, 2017 and thus presented as discontinued operations. Cash generating units within the power segment have similar economic characteristics based on the nature of the products or services they provide, the customers they serve, the method of distributing those products or services and the prevailing regulatory environment.

Segments consist of:	Geographical Location
Power The Corporation's investments in natural gas, wind, hydro, biomass and solar power, as well as project development. Discontinued operations (refer to note 3)	Canada
Utilities – district heating ("DH") The district heating business (Värmevärdan), in which the Corporation holds a 33.3% indirect interest until March 3, 2017.	Sweden

For the year ended	Dec 31, 2018			Dec 31, 2017			Discontinued Operations ⁽²⁾	Total
	Continuing Operations			Continuing Operations				
	Power	Corporate	Total	Power	Corporate	Total		
Revenue ⁽¹⁾	183,629	—	183,629	154,163	—	154,163	—	154,163
Expenses	(51,990)	(8,848)	(60,838)	(44,322)	(8,776)	(53,098)	—	(53,098)
EBITDA	130,790	(8,114)	122,676	118,567	(8,512)	110,055	—	110,055
Interest expense	(38,797)	—	(38,797)	(36,668)	—	(36,668)	—	(36,668)
Income tax recovery (expense)	(4,165)	2,150	(2,015)	(4,027)	(13,514)	(17,541)	—	(17,541)
Net income (loss)	9,974	(6,077)	3,897	11,147	(22,088)	(10,941)	129,317	118,376
Additions to capital assets, net	3,535	—	3,535	17,967	—	17,967	—	17,967
Additions to PUD	865	—	865	14,383	—	14,383	—	14,383

(1) Power revenue includes \$3,553 of grant funding eligibility for Whitecourt for the year (2017 - \$4,800).

(2) Relates to the utilities - DH segment.

NOTE 26. SUBSEQUENT EVENTS

Watford Wind Facility Acquisition

On February 1, 2019, Capstone acquired the assets of the Watford Wind Facility from Zephyr Farms Limited. The 10MW operating wind facility is located near the municipality of Brooke-Alvinston in Ontario and operates under a PPA that expires in 2032. Funding for the asset purchase came from existing cash.

INVESTOR INFORMATION

Quick Facts

Preferred shares outstanding	3,000,000
Securities exchange and symbols	Toronto Stock Exchange: CSE.PR.A

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