

Caribbean Utilities Company, Ltd.

2013 First Quarter Report

March 31, 2013



Caribbean Utilities Company, Ltd., ("CUC" or "the Company") commenced operations as the only electric utility in Grand Cayman on May 10, 1966.

The Company currently has an installed generating capacity of 149.540 megawatts (MW) and a record peak load of 102.086 MW was experienced on June 3, 2010.

CUC is committed to providing a safe and reliable supply of electricity to over 27,000 customers. The Company has been through many challenging and exciting periods but has kept pace with Grand Cayman's development for over 45 years.

The Company's registered office address is 457 North Sound Road, P.O Box 38, Grand Cayman KY1-1101 and employs 196 employees.

About the Cayman Islands

The Cayman Islands, a United Kingdom Overseas Territory with a population of approximately 55,000, are comprised of three islands: Grand Cayman, Cayman Brac and Little Cayman. Located approximately 150 miles south of Cuba, 460 miles south of Miami and 167 miles northwest of Jamaica, the largest island is Grand Cayman with an area of 76 square miles.

A Governor, presently His Excellency Mr. Duncan Taylor, is appointed by her Majesty the Queen. A democratic society, the Cayman Islands have a Legislative Assembly comprised of representatives elected from each of Grand Cayman's five districts as well as two representatives from the Sister Islands of Cayman Brac and Little Cayman.

All dollar amounts in this Quarterly Report are stated in United States dollars unless otherwise indicated.

Readers should review the note, further in this Quarterly Report, in the Management Discussion and Analysis section, concerning the use of forward-looking statements, which applies to the entirety of this Quarterly Report.

Caribbean Utilities Company, Ltd.

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Fellow Shareholders,

Net earnings for the three months ended March 31, 2013 ("First Quarter 2013") totalled \$2.9 million, an increase of \$1.0 million when compared to \$1.9 million for the three months ended March 31, 2012 ("First Quarter 2012"). This increase was due primarily to lower general and administration and financing costs as well as an increase in other income. General and administrative expenses for the First Quarter 2012 included a one-time charge of \$0.3 million related to restructuring costs incurred to further streamline CUC's organisational structure. Maintenance costs also declined as a result of the ongoing capital-related projects that upgrade and improve the performance of the Company's fleet of generating units. These items were partially offset by a 1% decline in kilowatt-hour (kWh) sales and higher depreciation costs for the First Quarter 2013 when compared to the First Quarter 2012.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the First Quarter 2013 were \$2.8 million, or \$0.10 per Class A Ordinary Share, an increase of \$1.0 million when compared to \$1.8 million, or \$0.06 per Class A Ordinary Share for the First Quarter 2012.

Kilowatt-hour sales for the First Quarter 2013 totalled 125.5 million kWh, a decrease of 0.9 million kWh, or 1% when compared to 126.4 million kWh for the First Quarter of 2012.

First Quarter 2013 saw an increase in customer connections. The total number of customers as at March 31, 2013 was 27,086, an increase of 331 customers, or 1%, compared to 26,755 customers as at March 31, 2012. There was a net increase of 51 customers for the First Quarter 2013. This comprised of 23 residential connections and 28 commercial connections.

During this quarter fuel prices remained reasonably stable but relatively high. This has resulted in the continued efforts by customers to conserve energy usage.

CUC's average price per imperial gallon ("IG") of fuel for the First Quarter 2013 increased 3% to \$4.90, when compared to \$4.76 for the First Quarter 2012. The Company's average price per IG of lubricating oil for the First Quarter 2013 decreased 6% to \$13.12, compared to \$13.94 for the First Quarter 2012.

A Certificate of Need for generation capacity was issued to the Electricity Regulatory Authority ("ERA") by the Company in November 2011, driven primarily by the upcoming retirements of some of the Company's generating units due to begin in 2014.

In March 2012, the ERA solicited Request for Proposals (RFP) for an additional 36 megawatts ("MW") of generation capacity from qualified bidders (including CUC). In February 2013, the Company was advised that another local company, DECCO Ltd., had won the bid.

In April 2013 the ERA announced that it would be engaging an independent party to conduct an investigation into the 36 MW bid process following public statements being made by its former managing director concerning alleged irregularities with the process. The Company is becoming increasingly concerned that the ongoing delays in the process to secure firm generating capacity may lead to inadequate installed generation capacity given that 18 MW of the 36 MW capacity was intended to have been installed for July 2014 to serve the needs of Grand Cayman. However the Company will explore all options, including temporary generation solutions to mitigate the threat of extended power outages for the summer of 2014.

During the quarter under review the Company also continued discussions with prospective providers of alternative energy in the areas of solar and wind. Once the negotiations are completed and agreements have been reached with all parties, an announcement will be made. The addition of renewable sources will not allay concerns regarding reliability as these sources are not considered firm capacity. However, we believe there are economic and environmental benefits to engage renewable energy sources to displace some of the diesel fuel that our generators presently consume.

During the First Quarter 2013, the Company named the Business Systems Support Analyst, Mr. Richard Solomon of the Information Technology Department as CUC's "Unsung Hero". This award recognizes employees who go beyond the call of duty and make invaluable contributions, which are integral to the Company's operations.

The Company remains focused on providing a safe and reliable electricity service to its customers and will continue to do so in an efficient manner.

J.F. Richard Hew

President & Chief Executive Officer

had burned !

May 3, 2013

Interim Management's Discussion and Analysis

The following management's discussion and analysis ("MD&A") should be read in conjunction with the Caribbean Utilities Company, Ltd. ("CUC" or "the Company") interim unaudited consolidated financial statements and notes thereto for the three months ended March 31, 2013 and audited consolidated financial statements and notes thereto for the year ended December 31, 2012. The material has been prepared in accordance with National Instrument 51-102 - Continuous Disclosure Obligations ("NI 51-102") relating to Management's Discussion and Analysis.

Additional information in this MD&A has been prepared in accordance with US GAAP, including certain accounting practices unique to rate-regulated entities. These accounting practices, which are disclosed in the notes to the Company's 2012 annual financial statements, result in regulatory assets and liabilities which would not occur in the absence of rate regulation. In the absence of rate regulation the amount and timing of the recovery or refund would not be subject to regulatory approval.

Certain statements in this MD&A, other than statements of historical fact, are forwardlooking statements concerning anticipated future events, results, circumstances, performance or expectations with respect to the Company and its operations, including its strategy and financial performance and condition. Forward looking statements include statements that are predictive in nature, depend upon future events or conditions, or include words such as "expects", "anticipates", "plan", "believes", "estimates", "intends", "targets", "projects", "forecasts", "schedule", or negative versions thereof and other similar expressions, or future or conditional verbs such as "may", "will", "should", "would" and "could". Forward looking statements are based on underlying assumptions and management's beliefs, estimates and opinions, and are subject to inherent risks and uncertainties surrounding future expectations generally that may cause actual results to vary from plans, targets and estimates. Some of the important risks and uncertainties that could affect forward looking statements are described in the MD&A in the section labelled "Business Risks" and include but are not limited to operational, general economic, market and business conditions, regulatory developments and weather. CUC cautions readers that actual results may vary significantly from those expected should certain risks or uncertainties materialize, or should underlying assumptions prove incorrect. Forward-looking statements are provided for the purpose of providing information about management's current expectations and plans relating to the future. Readers are cautioned that such information may not be appropriate for other purposes. The Company disclaims any intention or obligation to update or revise any forwardlooking statements, whether as a result of new information, future events or otherwise except as required by law.

Financial information is presented in United States dollars unless otherwise specified. The consolidated financial statements and MD&A in this interim report were approved by the Audit Committee.

Financial and Operational Highlights

| (\$ thousands, except basic earnings per ordinary share, dividends paid per ordinary share and where otherwise indicated) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|---|---|---|--------|----------|
| Electricity Sales | 15,946 | 15,921 | 25 | 0% |
| Fuel Factor Revenues | 36,579 | 35,732 | 847 | 2% |
| Operating Revenues | 52,525 | 51,653 | 872 | 2% |
| Fuel and Lube Costs | 36,579 | 35,732 | 847 | 2% |
| Other Operating Expenses | 11,835 | 12,393 | (558) | -5% |
| Total Operating Expenses | 48,414 | 48,125 | 289 | 1% |
| Earnings for the Period | 2,898 | 1,907 | 991 | 52% |
| Basic Earnings per Class A Ordinary Share | 0.10 | 0.06 | 0.04 | 67% |
| Dividends paid per Class A Ordinary Share | 0.165 | 0.165 | - | 0% |
| Cash Flow from Operating Activities | 15,333 | 10,213 | 5,120 | 50% |
| Peak Load Gross (MW) | 88.6 | 84.3 | 4.3 | 5% |
| Net Generation (millions of kWh) | 134.4 | 135.4 | (1.0) | -1% |
| Kilowatt-Hour Sales (millions of kWh) | 125.5 | 126.4 | (0.9) | -1% |
| Total Customers | 27,086 | 26,755 | 331 | 1% |
| Customers per Employee (#) | 138 | 145 | (7) | -5% |
| Sales per employee (millions of kWh) | 0.64 | 0.68 | (0.04) | -6% |

Corporate and Regulatory Overview

The principal activity of the Company is to generate, transmit and distribute electricity in its licence area of Grand Cayman, Cayman Islands pursuant to a 20-year exclusive Transmission & Distribution ("T&D") Licence and a 21.5 year non-exclusive Generation Licence ("the Licences") granted by the Cayman Islands Government ("Government"), which expire in April 2028 and September 2029 respectively.

The Licences contain the provision for a rate cap and adjustment mechanism ("RCAM") based on published consumer price indices. CUC's return on rate base ("RORB") for 2012 was 6.9% (2011: 7.6%). CUC's RORB for 2012 was targeted in the 7.25% to 9.25% range (2011: 7.75% to 9.75%). CUC's RORB for 2013 is targeted in the 7.25% to 9.25% range.

CUC's base rates are designed to recover all non-fuel and non-regulatory costs and include per kilowatt-hour ("kWh") electricity charges and fixed facilities charges. Fuel cost charges and regulatory fees are billed as separate line items. Base rates are subject to an annual review and adjustment each June through the RCAM. In June 2012, following review and approval by the Electricity Regulatory Authority ("ERA"), the Company increased its base rates by 0.7% as a result of the 2011 RORB and the slight increase in the applicable United States and Cayman Islands consumer price indices, adjusted to exclude food and fuel, for calendar year 2011. All fuel and lubricating oil costs are passed through to customers without mark-up as a per kWh charge.

Rate base is the value of capital upon which the Company is permitted an opportunity to earn a return. The value of this capital is the average of the beginning and ending values for the applicable financial year of: fixed assets less accumulated depreciation, plus the allowance for working capital, plus regulatory assets less regulatory liabilities.

The ERA has the overall responsibility of regulating the electricity industry in the Cayman Islands in accordance with the ERA Law. The ERA oversees all licensees, establishes and enforces licence standards, enforces applicable environmental and performance standards, reviews the proposed RCAM, and sets the rate adjustment factors as appropriate.

The ERA also annually reviews and approves CUC's capital investment plan ("CIP"). The Company's CIP for 2012 to 2016 in the amount of \$122.0 million relating to non-generation installation expenditures were approved by the ERA in March 2012. Additional capital expenditures in respect of additional generation capacity are subject to ERA approval through a competitive bid process. The proposed 2013 - 2017 CIP totalling \$124.6 million of non-generation installation expenditures was submitted to the ERA in October 2012 for approval.

A Certificate of Need for generation capacity was issued to the ERA by the Company in November 2011, driven primarily by the upcoming retirements of some of the Company's diesel generating units due to begin in 2014.

In March 2012, the ERA solicited Request for Proposals (RFP) for an additional 36 megawatts ("MW") of generation capacity from qualified bidders (including CUC). In February 2013, the Company was advised that another local company, DECCO Ltd., had won the bid.

In April 2013 the ERA announced that it would be engaging an independent party to conduct an investigation into the 36 MW bid process following public statements being made by its former managing director concerning alleged irregularities with the process. The Company is becoming increasingly concerned that the ongoing delays in the process to secure firm generating capacity may lead to inadequate installed generation capacity given that 18 MW of the 36 MW capacity was intended to have been installed for July 2014 to serve the needs of Grand Cayman. However the Company will explore all options, including temporary generation solutions to mitigate the threat of extended power outages for the summer of 2014.

A licence fee of 1%, payable to the Government, is charged on gross revenues, then prorated and applied only to customer billings with consumption over 1,000 kWh per month as a pass-through charge. In addition to the licence fee, a regulatory fee of $\frac{1}{2}$ of 1% is charged on gross revenues, then prorated and applied only to customer billings with consumption over 1,000 kWh per month.

In the event of a natural disaster as defined in the T&D Licence, the actual increase in base rates will be capped for the year at 60% of the change in the Price Level Index and the difference between the calculated rate increase and the actual increase expressed as a percentage, shall be carried over and applied in addition to the normal RCAM adjustment in either of the two following years if the Company's RORB is below the target range. In the event of a disaster the Company would also write-off destroyed assets over the remaining life of the asset that existed at time of destruction. Z Factor rate changes will be required for insurance deductibles and other extraordinary expenses. The Z Factor is the amount, expressed in cents per kwh, approved by the ERA to recover the costs of items deemed to be outside of the constraints of the RCAM.

In late March 2012 CUC's wholly owned subsidiary, DataLink, Ltd. ("DataLink"), received its licence from the Information and Communications Technology Authority ("ICTA"), which permits DataLink to provide fibre optic infrastructure and other information and communication technology (ICT) services to the ICT industry. The term of the licence is 15 years and expires on March 27, 2027.

The ICTA is an independent statutory body, which was created by the enactment of the Information and Communications Technology Authority Law on May 17, 2002 and is responsible for the regulation and licencing of Telecommunications, Broadcasting, and all forms of radio. The ICTA sets the standards under which ICT networks must be developed and operated.

Consolidation Accounting Policy

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiary DataLink. All significant intercompany balances and transactions have been eliminated on consolidation.

Earnings

Net earnings for the three months ended March 31. 2013 ("First Quarter 2013") totalled \$2.9 million, an increase of \$1.0 million, when compared to \$1.9 million for the three months ended March 31, 2012 ("First Quarter 2012"). This increase was due primarily to lower general and administration and financing costs as well as an increase in other income. General and administrative expenses for the First Quarter 2012 included a one-time charge of \$0.3 million related to restructuring costs incurred to further streamline CUC's organisational structure. Maintenance costs also declined as a result of the ongoing capital-related projects that upgrade and improve the performance of the Company's fleet of generating units. These items were partially offset by a 1% decline in kWh sales and higher depreciation costs for the First Quarter 2013 when compared to the First Quarter 2012.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the First Quarter 2013 were \$2.8 million, or \$0.10 per Class A Ordinary Share, an increase of \$1.0 million when compared to \$1.8 million, or \$0.06 per Class A Ordinary Share for the First Quarter 2012.

Sales

Sales for the First Quarter 2013 totalled 125.5 million kWh, a decrease of 0.9 million kWh, or 1%, in comparison to 126.4 million kWh for the First Quarter 2012.

Sales for the First Quarter 2012 were positively impacted by an additional leap year sales day in February. Excluding the impact of this additional day, the Company's kWh sales were 125.5 million kWh for the First Quarter 2013 when compared to 124.9 million kWh for the First Quarter 2012.

The average monthly temperature for the First Quarter 2013 was 79.3 degrees Fahrenheit as compared to an average temperature of 79.1 degrees for the same period last year. The average monthly rainfall for the First Quarter 2013 was 0.89 inches as compared to average monthly rainfall of 2.15 inches for First Quarter 2012.

Total customers as at March 31, 2013 were 27,086, an increase of 331 customers, or 1%, compared to 26,755 customers as at March 31, 2012. The Company had a net increase of 51 customers for the First Quarter 2013. This number comprised of 23 residential connections and 28 commercial connections.

The following tables present customer and sales highlights:

| Customers (#) | March 31, 2013 | March 31, 2012 | Change % |
|-----------------|----------------|----------------|----------|
| Residential | 23,098 | 22,894 | 1% |
| Commercial | <u>3,988</u> | <u>3,861</u> | 3% |
| Total Customers | 27,086 | 26,755 | 1% |

| Sales (thousands kWh) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | % Change |
|-------------------------------|---|---|----------|
| Residential | 56,761 | 55,898 | 1.5% |
| Commercial | 67,075 | 68,893 | -2.6% |
| Other (street lighting, etc.) | <u>1,619</u> | <u>1,574</u> | 2.9% |
| Total Sales | 125,455 | 126,365 | -0.7% |

Operating Revenues

Operating revenues for the First Quarter 2013 at \$52.5 million increased \$0.8 million from \$51.7 million for the First Quarter 2012 due to 2% higher fuel factor revenues.

Electricity sales revenues were \$15.9 million for the First Quarter 2013, comparable to the First Quarter 2012 as a 1% decline in kWh sales was offset by a 0.7% base rate increase effective June 1, 2012.

Fuel factor revenues for the First Quarter 2013 totalled \$36.6 million, a \$0.9 million increase from the \$35.7 million in fuel factor revenues for the First Quarter 2012. Fuel factor revenues for the First Quarter 2013 increased due to an increase in the cost of fuel when compared to the First Quarter 2012 (see the "Power Generation" section of this MD&A for further details). The average Fuel Cost Charge for the three months ended March 31, 2013 was \$0.28 per kWh, a 4% increase from \$0.27 per kWh for the three months ended March 31, 2012. CUC passes through all fuel costs to consumers on a two-month lag basis with no mark-up.

Total operating revenues were as follows:

| Revenues (thousands \$) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|---------------------------------|---|---|------------|----------|
| Residential | 7,493 | 7,333 | 160 | 2% |
| Commercial | 8,343 | 8,478 | -135 | -2% |
| Other (street lighting, etc.) | <u>110</u> | <u>110</u> | <u>o</u> | 0% |
| Electricity Sales Revenues | 15,946 | 15,921 | 25 | 0% |
| Fuel Factor Revenues | <u>36,579</u> | <u>35,732</u> | <u>847</u> | 2% |
| Total Operating Revenues | 52,525 | 51,653 | 872 | 2% |

Operating Expenses

Operating expenses for the First Quarter 2013 totalled \$48.4 million, a \$0.3 million increase from \$48.1 million for the First Quarter 2012. The major contributing factors to this increase are higher power generation and depreciation costs, which were partially offset by decreased general and administration and maintenance costs for the First Quarter 2013 when compared to the First Quarter 2012.

Operating expenses were as follows:

| Operating Expenses (\$ thousands) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|-----------------------------------|---|---|--------|----------|
| Power Generation Expenses | 37,323 | 36,644 | 679 | 2% |
| General and Administration | 2,080 | 2,777 | (697) | -25% |
| Consumer Service | 409 | 385 | 24 | 6% |
| Transmission and Distribution | 601 | 615 | (14) | -2% |
| Depreciation | 6,376 | 5,678 | 698 | 12% |
| Maintenance | 1,546 | 1,927 | (381) | -20% |
| Amortization of Intangible Assets | <u>79</u> | <u>99</u> | (20) | -20% |
| Total Operating Expenses | 48,414 | 48,125 | 289 | 1% |

Power Generation

Power generation costs for the First Quarter 2013 increased \$0.7 million, to \$37.3 million when compared to \$36.6 million for the First Quarter 2012. The increase is a result of an increase in the cost of fuel. The peak load for the First Quarter 2013 was 88.6 MW, a 5% increase compared to the peak load for the same period last year of 84.3 MW.

Power generation expenses were as follows:

| Power Generation (\$ thousands) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|---|---|---|--------|----------|
| Fuel costs (net of deferred fuel charges) | 35,996 | 34,954 | 1,042 | 3% |
| Lubricating Oil costs (net of deferred lubricating oil charges) | 583 | 778 | (195) | -25% |
| Other generation expenses | <u>744</u> | <u>912</u> | (168) | -18% |
| Total power generation expenses | 37,323 | 36,644 | 679 | 2% |

The Company's average price per imperial gallon ("IG") of fuel for the First Quarter 2013 increased 3% to \$4.90, when compared to \$4.76 for the First Quarter 2012.

The Company's average price per IG of lubricating oil for the First Quarter 2013 decreased 6% to \$13.12, compared to \$13.94 for the First Quarter 2012.

The Fuel Tracker Account (see Note 6 of "Notes to Interim Consolidated Financial Statements" for further details) is comprised of total diesel fuel and lubricating oil costs to be recovered from consumers.

In March 2011 the ERA approved the Fuel Price Volatility Management Programme. The objective of the programme is to reduce the impact of volatility in the Fuel Cost Charge paid by the Company's customers for the fuel that the Company must purchase in order to provide electric service. Contracts initiated in May 2012 and November 2012 utilize call spreads to promote transparency in pricing. The monthly hedging costs and returns are also included within the Fuel Tracker Account.

Other generation expenses for the First Quarter 2013 declined \$0.2 million to \$0.7 million from \$0.9 million for the First Quarter 2012. This decrease primarily relates to lower costs associated with the disposal of lubricating oils in the First Quarter 2013 compared to the First Quarter 2012.

General and Administration ("G&A")

G&A expenses for the First Quarter 2013 totalled \$2.1 million, a decrease of \$0.7 million when compared to the First Quarter 2012. This decrease was due primarily to higher general expenses capitalized ("GEC") in First Quarter 2013; restructuring costs incurred in First Quarter 2012 and lower pension costs associated with the Company's defined benefit plans in First Quarter 2013.

GEC totalled \$0.9 million for the First Quarter 2013, an increase of \$0.1 million when compared to GEC for the First Quarter 2012. GEC is calculated as a percentage, up to 10% of Non-Fuel Operating Expenses, varying annually depending on the level of capital activity.

First Quarter 2012 included a one-time charge of \$0.3 million related to restructuring costs incurred to further streamline the Company's organizational structure. These costs related to redundancy and early retirement payments to four employees. The restructuring process resulted in a decline in the general and administrative expenses in the amount of \$0.1 million for the First Quarter 2013 when compared to the First Quarter 2012.

The Company established a defined benefit pension plan for the retired Chairman during 2003. In May 2005, CUC's Board of Directors approved the establishment of a defined benefit pension plan for the retired President and Chief Executive Officer. The pension costs of the defined benefit pension plans are actuarially determined using the projected benefits method. A defined pension expense of \$0.09 million has been recorded for the First Quarter 2013, a decrease of \$0.15 million when compared to \$0.24 million for First Quarter 2012.

Consumer Services ("CS")

CS expenses for the First Quarter 2013 totalled \$0.4 million, comparable to CS expenses for the First Quarter 2012.

Transmission and Distribution ("T&D")

T&D expenses for the First Quarter 2013 totalled \$0.6 million, comparable to T&D expenses for the First Quarter 2012.

Depreciation

Depreciation expenses for the First Quarter 2013 totalled \$6.4 million, an increase of \$0.7 million from \$5.7 million for the First Quarter 2012. The increase in depreciation is related to capital projects completed in prior periods.

Maintenance

Maintenance expenses for the First Quarter 2013 totalled \$1.5 million, a decrease of \$0.4 million when compared to \$1.9 million for the First Quarter 2012.

Maintenance expenses for the First Quarter 2013 were expected to be lower than those seen in 2012 due to the nature of certain scheduled projects for 2013 which are deemed to result in upgrades to generating units. The costs of such upgrades are considered capital in nature as the upgrades extend the life or increase the output of the unit.

Amortization

Amortization of intangible assets for the First Quarter 2013 totalled \$0.08 million, a decrease of \$0.02 million when compared to \$0.1 million for the First Quarter 2012.

Amortization represents the monthly recognition of the expense associated with software purchases as well as other intangible assets such as the costs associated with the licence negotiations. The negotiations for the Company's electricity licence ceased in 2008 and the costs associated with the negotiations are being amortized over 20 years on a straight-line basis. The negotiations associated with DataLink's ICT licence ceased in 2012 and these costs are being amortized over 15 years on a straight-line basis.

Other Income and Expenses

Net Other Expenses for the First Quarter 2013 totalled \$1.2 million, a decrease of \$0.4 million from \$1.6 million for the First Quarter 2012.

| Other Income & Expenses (\$ thousands) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|--|---|---|--------|----------|
| Total interest costs | (3,032) | (3,190) | 158 | -5% |
| AFUDC | 789 | 745 | 44 | 6% |
| Total finance charges | (2,243) | (2,445) | 202 | -8% |
| Foreign exchange gain | 472 | 500 | (28) | -6% |
| Other income | 558 | 324 | 234 | 72% |
| Total Net Other Expense | (1,213) | (1,621) | 408 | -25% |

Finance charges for the First Quarter 2013 totalled \$2.2 million, a \$0.2 million decrease from \$2.4 million for the First Quarter 2012.

Under the T&D Licence there is a provision for an Allowance for Funds Used During Construction ("AFUDC"). This capitalisation of the Financing Cost is calculated by multiplying the Company's Cost of Capital rate by the average work in progress for each month. The cost of capital rate for 2013 is 7.50% as agreed with the ERA, in accordance with the T&D Licence, and will be reviewed annually. The cost of capital rate for 2012 was 8.25%. The AFUDC amount for the First Quarter 2013 totalled \$0.8 million, a \$0.1 million increase when compared to AFUDC of \$0.7 million for the First Quarter 2012.

Foreign exchange gains and losses are the result of monetary assets and liabilities denominated in foreign currencies that are translated into United States dollars at the exchange rate prevailing on the Balance Sheet date. Revenue and expense items denominated in foreign currencies are translated into United States dollars at the exchange rate prevailing on the transaction date. Foreign exchange gains for the First Quarter 2013 totalled \$0.5 million, comparable to foreign exchange gains for the First Quarter 2012.

Other income is comprised of income from pipeline operations, sale of meter sockets, sale of recyclable materials and other miscellaneous income. Other Income totalled \$0.6 million for the First Quarter 2013 a \$0.3 million increase when compared to other income for the First

Quarter 2012. Other income for the First Quarter 2013 includes a billing adjustment for a commercial customer. The impact of this adjustment to other income totalled \$0.1 million.

In March 2012 the ERA acknowledged the creation of DataLink, CUC's wholly owned subsidiary. Subsequently the ICTA granted Datalink a licence to provide fibre optic infrastructure in Grand Cayman. Revenues from DataLink are recorded in "Other Income"

CUC and DataLink have entered into three agreements;

- 1. The Management and Maintenance agreement
- 2. The Pole Attachment agreement, and
- 3. The Fibre Optic agreement

All three agreements have been approved by the ERA. The ICTA licence allowed DataLink to assume full responsibility for the existing Pole Attachment Agreements and Optical Fibre Lease Agreement with third party information and communications technology service providers. The novation and reassignment of existing contracts from CUC to DataLink was completed in 2012.

The Economy

Financial services and tourism are the two main industries of the Cayman Islands. The recession that has impacted the global economy has also impacted the Cayman Islands and these sectors. In January 2013 the Cayman Islands Government ("Government") released the 2012 Third Quarter Economic Report. The Third Quarter Economic Report indicated that the Cayman Islands Gross Domestic Product ("GDP") grew by an estimated annualised rate of 0.8% for the first nine months of 2012. The report also indicated the growth outlook for 2012 as 1.2%. GDP is considered by many to be the broadest indicator of economic output and growth.

In March 2013, the Government released the 2012 Consumer Price Index ("CPI") Report. The annual percentage change in a CPI is used as a measure of inflation. The CPI for 2012 was reported at 1.2%. The overall CPI stood at 102.5 in December 2012 and at 100.4 in December 2011.

Cayman has a high proportion of foreign nationals that provide labour in various sectors of the economy. Foreign workers as at December 2012 totalled 20,743 a 4% increase when compared to 19,927 at the close of 2011 and a 9% increase when compared to 19,106 at the close of 2010. The number of foreign nationals is an indicator of the state of the economy as well as a factor; significant increases and decreases affect the population and subsequently the local economy. Additional residents impact consumption in varying areas of the economy.

Some of the key indicators for the Financial Services industry are shown in the table below:

| | As at March 2013 | As at December 2012 | As at December 2011 | As at December 2010 | As at December 2009 |
|-----------------------------|------------------------|---------------------------|---------------------------|---------------------------|---------------------------|
| Bank Licences | 222 | 226 | 234 | 246 | 266 |
| Mutual Funds* | 10,932 | 10,841 | 9,258 | 9,438 | 9,523 |
| Mutual Fund Administrators | 123 | 124 | 129 | 134 | 141 |
| Captive Insurance Companies | 768 | 741 | 739 | 738 | 780 |

^{*} The Cayman Islands Mutual Funds (Amendment) Law, 2011, dated December 22, 2011, amended the Mutual Funds Law (2009 Revision) to require all Master Funds, as defined therein, to become registered by the Cayman Islands Monetary Authority ("CIMA"). Registration for these funds was required for the first time in 2012; previously registration of any such funds was voluntary in nature. As at December 31, 2012 there were 1,891 registered Master Mutual Funds compared to nil as at December 31, 2011).

The tourist demographic is largely comprised of visitors from the United States of America ("US"). For First Quarter 2013 78% of air arrivals to the country were citizens of the US. As such the US economy largely impacts that of the Cayman Islands. First Quarter 2013 air arrivals were up 8% and cruise arrivals decreased by 4%, when compared to First Quarter 2012. Air arrivals have a direct impact on the Company's sales growth as these visitors are stay-over visitors who occupy the hotels. Cruise arrivals have an indirect impact as they affect the opening hours of the establishments operating for that market.

The following table presents statistics for tourist arrivals in the Cayman Islands for the three months ending March 31:

| Arrivals | 2013 | 2012 | 2011 | 2010 | 2009 |
|----------|----------------|----------------|----------------|----------------|---------|
| By Air | 104,029 | 96,187 | 93,822 | 87,841 | 81,080 |
| By Sea | <u>532,263</u> | <u>553,347</u> | <u>510,648</u> | <u>472,036</u> | 465,884 |
| Total | 636,292 | 649,534 | 604,470 | 559,877 | 546,964 |

All data is sourced from the Cayman Islands Government, Cayman Islands Economics & Statistics Office, Cayman Islands Monetary Authority and Cayman Islands Department of Tourism websites; www.cimonev.com.ky and www.caymanislands.ky.

Liquidity and Capital Resources

The following table outlines the summary of cash flow:

| Cash Flows (\$ thousands) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 | Change | % Change |
|-----------------------------|---|---|---------|----------|
| Beginning cash | 694 | 424 | 270 | 64% |
| Cash provided by/(used in): | | | | |
| Operating activities | 15,333 | 10,213 | 5,120 | 50% |
| Investing activities | (6,402) | (5,930) | (472) | 8% |
| Financing activities | (6,675) | (3,109) | (3,567) | 115% |
| Ending cash | 2,950 | 1,598 | 1,351 | 85% |

Operating Activities:

Cash flow provided by operations, after working capital adjustments, for the First Quarter 2013, was \$15.3 million, an increase of \$5.1 million from \$10.2 million for the First Quarter 2012. This increase is attributable to the movement in non-cash working capital balances and higher earnings in the First Quarter 2013.

Investing Activities:

Cash used in investing activities for the First Quarter 2013 totalled \$6.4 million, an increase of \$0.5 million from \$5.9 million for the First Quarter 2012. This increase is attributable to the impact of insurance funds received in the First Quarter 2012 partially offset by lower capital expenditures in the First Quarter 2013.

Financing Activities:

Cash used in financing activities for the First Quarter 2013 totalled \$6.7 million an increase of \$3.6 million from cash used in financing activities of \$3.1 million for the First Quarter 2012. This increase is attributable to the repayment of \$1.8 million on the overdraft facility in First

Quarter 2013 compared to the utilisation of \$1.7 million of the overdraft facility in First Quarter 2012.

Transactions with Related Parties

Miscellaneous payables to Fortis Turks & Caicos, also a subsidiary of Fortis Inc., were nil at March 31, 2013 (\$0.001 million as at December 31, 2012). Prior period amounts related to travel expenses and were included within the Accounts Payable and Accrued Expenses on the Balance Sheet. Miscellaneous receivables from Fortis Turks & Caicos totalling \$0.012 million were outstanding at March 31, 2013 (nil as at December 31, 2012) for equipment testing and are included within Accounts Receivable on the Balance Sheet. Miscellaneous payables to Fortis Inc., the Company's majority shareholder, totalling \$0.017 million were outstanding at March 31, 2013 (\$0.05 million as at December 31, 2012) for labour, software, insurance and travel expenses are included within the Accounts Payable and Accrued Expenses on the Balance Sheet. Miscellaneous receivables from Fortis Inc. were \$0.009 million at March 31, 2013 (\$0.01 million as at December 31, 2012) for travel expenses and are included within Accounts Receivable on the Balance Sheet.

Contractual Obligations

The contractual obligations of the Company over the next five years and periods thereafter, as at March 31, 2013, are outlined in the following table:

| (\$ millions) | Total | < 1 year | 1 to 3 years | 4 to 5 years | > 5 years |
|-------------------------|-------|----------|--------------|--------------|-----------|
| Total debt | 219.5 | 50.5 | 31.0 | 25.0 | 113.0 |
| Defined benefit pension | 0.3 | 0.3 | - | - | - |
| Total | 219.8 | 50.8 | 31.0 | 25.0 | 113.0 |

The Company executed a primary fuel supply contract with Rubis Cayman Islands Limited ("Rubis") in September 2012 upon the expiration of its previous fuel supply contracts. Under the agreement the Company is committed to purchase approximately 60% of its diesel fuel requirements for its generating plant from Rubis. The approximate quantities per the contract on an annual basis are, by fiscal year in millions of IGs: 2013 - 19.4, 2014 - 11.3. The Company also executed a secondary fuel supply contract with Esso Cayman Limited ("Esso") in September 2012 and is committed to purchase approximately 40% of the Company's diesel fuel requirements for its generating plant from Esso. The approximate quantities per the contract on an annual basis are, by fiscal year in millions of IGs: 2013 - 13.0, 2014 - 7.6. Both contracts expire July 2014 with the option to renew for two additional 18 month terms. Renewal cannot occur more than six months in advance of the current contract expiry date.

Financial Position

The following table is a summary of significant changes to the Company's balance sheet from December 31, 2012 to March 31, 2013:

| Significant changes in Balance Sheets between December 31, 2012 and March 31, 2013 | Increase (Decrease) | Explanation |
|--|------------------------|---|
| (\$ millions) | | |
| Cash and Cash Equivalents | 2.3 | Increase due to cash provided by operating activities of \$15.3 million offset by cash used in financing activities of \$6.4 million and by cash used in investing activities of \$6.6 million. |
| Accounts Receivable | (2.3) | Decrease due to lower fuel billings in the First Quarter 2013. |
| Regulatory Assets | 1.2 | In accordance with regulatory treatment the fuel tracker account is classified as a regulatory asset. This amount represents fuel costs incurred by the Company that are recoverable from the customer. |
| Prepayments | (1.2) | Decrease due to recognition of the Company's insurance plan. |
| Property, Plant and Equipment | 0.2 | Net increase is comprised of (1) capital expenditures of \$6.4 million (2) depreciation expense of \$6.4 million (3) \$0.2 million in accrued capital expenditure. |
| Bank Overdraft | (1.8) | Decrease in bank overdraft. |
| Accounts Payable and Accrued Expenses | 3.3 | Increase in accrued interest. |
| Share Premium | 0.5 | The Company issued 47,431 shares through its share purchase plans. |
| Retained Earnings | (2.0) | Decrease due to dividends of \$4.9 million, partially offset by earnings of \$2.9 million. |

Capital Resources

The Company's principal activity of generation, transmission and distribution of electricity in Grand Cayman requires CUC to have ongoing access to capital to build and maintain the electrical system for the community it serves.

To help ensure access to capital, the Company targets a long-term capital structure containing approximately 45% equity, including preference shares, and 55% debt. The Company's objective is to maintain investment-grade credit ratings. The Company sets the amount of capital in proportion to risk. The debt to equity ratio is managed through various methods such as the rights offering that occurred in 2008 and through the Company's Share Purchase Plans.

Certain of the Company's long-term debt obligations have covenants restricting the issuance of additional debt such that consolidated debt cannot exceed 65% of the Company's consolidated capital structure, as defined by the long-term debt agreements. As at March 31, 2013, the Company was in compliance with all debt covenants.

The Company's capital structure is presented in the following table:

| Capital structure | March 31, 2013 (\$ millions) | 0/0 | December 31, 2012 (\$ millions) | % |
|----------------------|---------------------------------|-----------|------------------------------------|-----------|
| Total debt | 219.5 | 56 | 219.5 | 56 |
| Shareholders' equity | <u>172.5</u> | <u>44</u> | <u>173.9</u> | <u>44</u> |
| Total | 392.0 | 100 | 393.4 | 100 |

The Company's credit ratings are as follows:

Standard and Poor's ("S&P")

Dominion Bond Rating Service ("DBRS")

A-/Stable
A (low)

The S&P rating is in relation to long-term corporate credit and unsecured debt while the DBRS rating relates to senior unsecured debt.

In March 2013 S&P affirmed the Company's 'A Negative' rating and stable outlook. This rating reflects S&P's positive view of the Company's current position as the sole provider of electricity in Grand Cayman, and regulation based on full cost recovery. The stable outlook reflects S&P's assessment of predictable, regulated cash flow and the expectation that management will continue to focus on its core, regulated business.

In February 2013 DBRS affirmed the Company's 'A' credit rating while maintaining the categorisation of low with a Stable trend. Considerations for the rating were a supportive regulatory regime, solid credit metrics and a stable island economy and demand for electricity. Impacting the rating were such factors as hurricane event risk and small size of the customer base.

Liquidity Risk

The Company's financial position could be adversely affected if it failed to arrange sufficient and cost-effective financing to fund, among other things, capital expenditures and the repayment of maturing debt. The ability to arrange such financing is subject to numerous factors, including the results of operations and financial position of the Company, conditions in the capital and bank credit markets, ratings assigned by ratings agencies and general economic conditions. These factors are mitigated by allowances in the Licences for review of the RCAM by the ERA in order to enable the Company to maintain sound credit ratings.

Credit Facilities

In May 2012 the Company renegotiated and increased the credit facilities agreement with the Royal Bank of Canada ("RBC"). The Company currently has \$47.0 million of unsecured credit financing facilities with RBC. The financing facilities are comprised of:

| Credit Facilities | (\$ millions) |
|---|---------------|
| Corporate Credit Card Line | \$0.4 |
| Letters of Credit | \$0.6 |
| Operating, Revolving Line of Credit | \$7.5 |
| Catastrophe Standby Loan | \$7.5 |
| Demand Loan Facility- Interim Funding of Capital Expenditures | <u>\$31.0</u> |
| Total | \$47.0 |

Of the total above, \$10.6 million was available at March 31, 2013.

Capital Expenditures

Capital expenditures for the three months ended March 31, 2013 were \$6.4 million, a \$0.5 million, or 7% decrease from \$6.9 million in capital expenditures for the three months ended March 31, 2012. The capital expenditures for the three months ended March 31, 2013 primarily relate to:

Distribution system extension and upgrades - \$3.4 million

- Generation Replacement Cost \$1.8 million
- AFUDC of \$0.8 million was capitalized in the three months ended March 31, 2013

| Capital expenditures (\$ Millions) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|---------------------------------------|--------------------------------------|--------------------------------------|
| Transmission | - | - |
| Distribution | 3.4 | 2.6 |
| Generation | 2.9 | 3.8 |
| Other | <u>0.1</u> | <u>0.5</u> |
| Total | 6.4 | 6.9 |

Off Balance-Sheet Arrangements

Disclosure is required of all off-balance sheet arrangements such as transactions, agreements or contractual arrangements with unconsolidated entities, structured finance entities, special purpose entities or variable interest entities that are reasonably likely to materially affect liquidity of or the availability of, or requirements for, capital resources. The Company has no such off-balance sheet arrangements as at March 31, 2013.

Business Risks

The following is a summary of the Company's significant business risks:

Operational Risks

Operational risks are those risks normally inherent in the operation of generating, transmission and distribution facilities. The Company's facilities are subject to the risk of equipment failure due to deterioration of the asset from use or age, latent defects and design or operator error, among other factors. These risks could lead to longer-than-forecast equipment downtimes for maintenance and repair, disruptions of power generation, customer service interruptions and could result in injury to employees and the public. Accordingly, to ensure the continued safe and efficient performance of the physical assets, the Company determines expenditures that must be made to maintain and replace the assets.

The Company continually develops capital expenditure, safety management and risk controls programs and assesses current and future operating and maintenance expenses that will be incurred in the ongoing operation of its systems. The Company also has an insurance program that provides coverage for business interruption, liability and property damage, although the coverage offered by this program is limited. (See "Insurance" for discussion of insurance terms and coverage). In the event of a large uninsurable loss, the Company would apply to the ERA for recovery of these costs through higher rates. However, there is no assurance that the ERA will approve any such application (See "Regulation" for discussion of regulatory risk).

Economic Conditions

The general economic condition of CUC's service area, Grand Cayman, influences electricity sales as with most utility companies. Changes in consumer income, employment and housing are all factors in the amount of sales generated. As the Company supplies electricity to all

hotels and large properties, its sales are therefore partially based on tourism and related industry and seasonal fluctuations.

Regulation

The Company operates within a regulated environment. As such the operations of the Company are subject to the normal uncertainties faced by regulated companies. Such uncertainties include approval by the ERA of billing rates that allow a reasonable opportunity to recover on a timely basis the estimated costs of providing services, including a fair return on rate base assets. The Company's capital expenditure plan requires regulatory approval. There is no assurance that capital projects perceived as required by the management of the Company will be approved.

Weather

CUC's facilities are subject to the effects of severe weather conditions principally during the hurricane season months of June through November. Despite preparations for disasters such as hurricanes, adverse conditions will always remain a risk. In order to mitigate some of this risk, the Company maintains insurance coverage which Management believes is proper and consistent with insurance policies obtained by similar companies.

Environmental Matters

CUC's operations are subject to local environmental protection laws concerning emissions to the air, discharges to surface and subsurface waters, land use activities, and the handling, storage, processing, use, emission and disposal of materials and waste products.

In 2004, CUC was initially registered to the ISO 14001:2007 which is the international standard for Environmental Management Systems ("EMS"). Under the ISO 14001 standard CUC is required to adhere to all applicable local legislation to prevent pollution to the environment as well as any self determined procedures, practices, and policies. The Company continuously adheres with the standard, and recertification must occur every three years. The Company has most recently received a recertification audit in March 2013, and zero non-conformances were identified, allowing CUC to be eligible for recertification.

In March 2007 the Kyoto Protocol was signed by the Cayman Islands; this framework aims to reduce Greenhouse Gas ("GHG") emissions produced by certain industries. As an overseas territory the Cayman Islands are required to give available national statistics on an annual basis to the UK which will be added to its inventory and reported to the United Nations Framework Convention on Climate Change (UNFCCC) Secretariat. Under the Convention governments are obligated to gather and report information on GHG emissions through the preparation of a national greenhouse gas inventory. The inventory primarily requires the Cayman Islands Government to quantify as best as possible the country's fuel consumption across a variety of sectors, production processes and distribution means. CUC has been in full cooperation with the Cayman Islands Government with supplying information requested for our industry to address this inventory.

Through adhering to local environmental legislation, cooperating with the Cayman Islands government departments and authorities, and by registering our EMS with an international standard CUC has determined that its exposure to environmental risks is not significant and does not have an impact on financial reporting including the recording of any Asset Retirement Obligations ("ARO's").

Insurance - Terms and Coverage

The Company renewed its insurance policy as at July 1, 2012 for one year under similar terms and coverage as in prior years. Insurance terms and coverage include \$100.0 million in property and machinery breakdown insurance and business interruption insurance per annum with a 24-month indemnity period and a waiting period on Non-Named Wind, Quake and Flood of 60-days. Any named Wind, Quake and Flood deductible has a 45-day waiting period. All T&D assets outside of 1,000 feet from the boundaries of the main power plant and substations are excluded, as the cost of such coverage is not considered economical. There is a single event cap of \$100 million. Each "loss occurrence" is subject to a deductible of \$1.0 million, except for windstorm (including hurricane) and earth movement for which the deductible is 2% of the value of each location that suffers loss, but subject to a minimum deductible of \$1.0 million and maximum deductible of \$4.0 million for all interests combined.

In accordance with the T&D Licence when an asset is impaired or disposed of, within the original estimated useful life, the cost of the asset is reduced and the net book value is charged to accumulated depreciation. This treatment is in accordance with rate regulated accounting and differs from the GAAP treatment of a loss being recognised on the statement of earnings. The amount charged to accumulated depreciation is net of any proceeds received in conjunction with the disposal of the asset. Insurance proceeds are included within the criteria.

In addition to the coverage discussed above, the Company has also purchased an excess layer of an additional \$100.0 million limit on property and business interruption (excluding windstorm, earth movement and flood).

The Company's insurance policy includes business interruption which covers losses resulting from the necessary interruption of business caused by direct physical loss or damage to CUC's covered property and loss of revenues resulting from damage to customers' property.

Defined Benefit Pension Plan

The Company maintains a defined benefit pension plan. There is no assurance that the pension plan assets will be able to earn the assumed rate of returns. The assumed long-term rate of return on pension plan assets, for the purposes of estimating pension expense for 2013, is 5%. This compares to assumed long-term rates of return of 5% used during 2012. The gain on pension plan assets during 2012 was 7% (2011: loss of 6%).

Market driven changes impacting the performance of the pension plan assets may result in material variations in actual return on pension plan assets from the assumed return on the assets causing material changes in consolidated pension expense and funding requirements. Net pension expense is impacted by, among other things, the amortization of experience and actuarial gains or losses and expected return on plan assets. Market driven changes impacting other pension assumptions, including the assumed discount rate, may also result in future consolidated contributions to pension plans that differ significantly from current estimates as well as causing material changes in consolidated pension expense. The discount rate assumed for 2013 is 3.7% compared to the discount rate assumed during 2012 which was 4.5%.

There is also measurement uncertainty associated with pension expense, future funding requirements, the accrued benefit asset, accrued benefit liability and benefit obligation due to measurement uncertainty inherent in the actuarial valuation process.

A discussion of the critical accounting estimates associated with pensions is provided in the "Critical Accounting Estimates" section of this MD&A.

CHANGES IN ACCOUNTING POLICIES

New US GAAP Accounting Pronouncements: The following new US GAAP accounting pronouncements that are applicable to, and were adopted by, CUC effective beginning January 1, 2013 are described as follows:

Disclosures About Offsetting Assets and Liabilities

Effective January 1, 2013, the Company adopted the amendments to Accounting Standards Codification ("ASC") Topic 210, Balance Sheet – Disclosures About Offsetting Assets and Liabilities as outlined in Accounting Standards Updates ("ASU") No. 2011-11 and 2013-01. The amendments improve the transparency of the effect or potential effect of netting arrangements on a company's financial position by expanding the level of disclosures required by entities for such arrangements. The amended disclosures are intended to assist financial statement users in understanding significant quantitative differences between balance sheets prepared under US GAAP and International Financial Reporting Standards ("IFRS"). ASU No. 2013-01 limits the scope of the new offsetting disclosure requirements previously issued in ASU No. 2011-11, to certain derivative instruments, repurchase and reverse repurchase agreements, and securities borrowing and lending arrangements that are either offset on the balance sheet or subject to an enforceable master netting or similar arrangement. The abovenoted amendments were applied retrospectively and did not materially impact the Company's interim consolidated financial statements for the three months ended March 31, 2013.

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income

Effective January 1, 2013, the Company adopted the amendments to ASC Topic 220, Other Comprehensive Income – Reporting of Amounts Out of Accumulated Other Comprehensive Income ("AOCI") as outlined in ASU No. 2013-02. The amendments improve the reporting of reclassifications out of AOCI and require entities to report, in one place, information about reclassifications out of AOCI and to present details of the reclassifications in the disclosure for changes in AOCI balances. The effect of the reclassification of significant items to net income in their entirety during the reporting period must be reported in the respective line items in the statement where net income is presented. The effect of items not reclassified to net income in their entirety during the reporting period are to be presented in the notes to the consolidated financial statements. The amendments were applied by the Company prospectively and did not materially impact the Company's interim consolidated financial statements for the three months ended March 31, 2013.

Critical Accounting Estimates

The preparation of the Company's financial statements in accordance with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Estimates are based on historical experience, current conditions and various other assumptions believed to be reasonable under the circumstances. Due to changes in facts and circumstances and the inherent uncertainty involved in making estimates, actual results may differ significantly from the current estimates. Estimates are reviewed periodically and, as adjustments become necessary, are reported in earnings in the period in which they become known. The Company's critical accounting estimates relate to:

Revenue Recognition

Revenue derived from the sale of electricity is taken to income on a bills-rendered basis, adjusted for unbilled revenues. Customer bills are issued throughout the month based on meter readings that establish electricity consumption since the last meter reading. The

unbilled revenue accrual for the period is based on estimated electricity sales to customers since the last meter reading. The estimation process for accrued unbilled electricity consumption will result in adjustments of electricity revenue in the periods they become known when actual results differ from the estimates. As at March 31, 2013, the amount of unbilled revenue recorded in Electricity Sales was \$3.7 million (March 31, 2012: \$4.5 million).

Kilo-watt Hour ("kWh") Sales

Kilowatt-hour sales throughout the month are based on meter readings that establish electricity consumption since the last meter reading. The kWh accrual for the period is based on estimated electricity sales to customers since the last meter reading. The estimation process for electricity consumption will result in adjustments of kWh sales statistics in the periods they become known when actual results differ from the estimates. As at March 31, 2013, the amount of estimated kWh sales was 26.4 million kWh (March 31, 2012: 27.9 million kWh).

Employee Future Benefits

The Company's defined benefit pension plan is subject to judgments utilised in the actuarial determination of the expense and related obligation. There are currently two participants in the Company's defined benefit pension plan. The main assumptions utilized by Management in determining pension expense and obligations were the discount rate for the accrued benefit obligation, pension commencement date, inflation and the expected rate of return on plan assets. As at March 31, 2013, the Company has a long-term liability of \$1.9 million (December 31, 2012: \$1.9 million).

Property, Plant and Equipment ("PP&E") Depreciation

Depreciation, by its very nature is an estimate based primarily on the estimated useful life of the asset. Estimated useful lives are based on current facts and historical information and take into consideration the anticipated physical life of the assets. As at March 31, 2013, the net book value of the Company's PP&E was \$377.3 million compared to \$377.1 million as at December 31, 2012, increasing as a result of the Company's generation and T&D capital expenditures. Depreciation expense for the First Quarter 2013 was \$6.4 million (\$5.7 million First Quarter 2012). Due to the value of the Company's PP&E, changes in depreciation rates can have a significant impact on the Company's depreciation expense.

Quarterly Results

The table "Quarterly Results" summarises unaudited quarterly information for each of the eight quarters ended June 30, 2011 through March 31, 2013. This information has been obtained from CUC's unaudited interim Financial Statements which, in the opinion of Management, have been prepared in accordance with US GAAP. These operating results are not necessarily indicative of results for any future period and should not be relied upon to predict future performance.

| Quarterly results (\$ thousands, except basic and diluted earnings per ordinary share) | Operating Revenue | Net earnings | Income applicable to ordinary shares | Earnings per ordinary share | Diluted earnings per ordinary share |
|--|----------------------|-----------------|--|-----------------------------------|---|
| March 31, 2013 | 52,525 | 2,898 | 2,785 | 0.10 | 0.10 |
| December 31, 2012 | 59,087 | 4,061 | 3,468 | 0.11 | 0.11 |
| September 30, 2012 | 58,870 | 6,582 | 6,469 | 0.22 | 0.22 |
| June 30, 2012 | 53,940 | 5,146 | 5,033 | 0.18 | 0.18 |
| March 31, 2012 | 51,653 | 1,907 | 1,794 | 0.06 | 0.06 |
| December 31, 2011 | 57,733 | 5,082 | 4,489 | 0.15 | 0.15 |
| September 30, 2011 | 62,453 | 6,253 | 6,140 | 0.22 | 0.22 |
| June 30, 2011 | 53,945 | 5,924 | 5,811 | 0.20 | 0.20 |

March 2013/March 2012

Net earnings for the three months ended March 31. 2013 ("First Quarter 2013") totalled \$2.9 million, an increase of \$1.0 million, when compared to \$1.9 million for the three months ended March 31, 2012 ("First Quarter 2012"). This increase was due primarily to lower general and administration and financing costs as well as an increase in other income. General and administrative expenses for the First Quarter 2012 included a one-time charge of \$0.3 million related to restructuring costs incurred to further streamline CUC's organizational structure. Maintenance costs also declined as a result of the ongoing capital-related projects that upgrade and improve the performance of the Company's fleet of generating units. These items were partially offset by a 1% decline in kWh sales and higher depreciation costs for the First Quarter 2013 when compared to the First Quarter 2012.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the First Quarter 2013 were \$2.8 million, or \$0.10 per Class A Ordinary Share, an increase of \$1.0 million when compared to \$1.8 million, or \$0.06 per Class A Ordinary Share for the First Quarter 2012.

December 2012/December 2011

Net earnings for the Fourth Quarter 2012 were \$4.1 million, a 20% or \$1.0 million decrease when compared to \$5.1 million for the Fourth Quarter 2011. Higher depreciation and T&D costs for the Fourth Quarter 2012 when compared to the Fourth Quarter 2011 were partially offset by higher electricity sales revenues.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Fourth Quarter 2012 were \$3.5 million, or \$0.11 per Class A Ordinary Share, as compared to \$4.5 million, or \$0.15 per Class A Ordinary Share for the Fourth Quarter 2011.

September 2012/September 2011

Net earnings for the three months ended September 30, 2012 ("Third Quarter 2012") totalled \$6.6 million, an increase of \$0.3 million, or 5%, when compared to \$6.3 million for the three months ended September 30, 2011 ("Third Quarter 2011"). Lower finance charges and an increase in other income were partially offset by a 1% decline in kWh sales and higher depreciation costs for the Third Quarter 2012 when compared to the Third Quarter 2011.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Third Quarter 2012 were \$6.5 million, an increase of \$0.4 million, or 7%, from \$6.1 million, for the Third Quarter 2011. Earnings per Class A Ordinary Share for the Third Quarter 2012 were \$0.22, comparable to Earnings per Class A Ordinary Share for the Third Quarter 2011.

June 2012/June 2011

Net earnings for the three months ended June 30, 2012 ("Second Quarter 2012") totalled \$5.1 million, a decrease of \$0.8 million, or 14%, when compared to \$5.9 million for the three months ended June 30, 2011 ("Second Quarter 2011"). A 3% decline in kWh sales and higher depreciation costs and finance charges were partially offset by decreased general and administration, consumer service and maintenance costs for the Second Quarter 2012 when compared to the Second Quarter 2011.

Net earnings in the Second Quarter 2011 were positively impacted by the temporary cessation of depreciation expenses on a damaged generating unit which has since been returned to service (see the "Depreciation" section of this MD&A for further details). In mid-2011, the Company closed on \$40 million of long-term financing resulting in higher interest costs for the Second Quarter of 2012 when compared to the Second Quarter 2011 (see the "Other Income and Expenses" section of this MD&A for further details).

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Second Quarter 2012 were \$5.0 million, or \$0.18 per Class A Ordinary Share, a decrease of \$0.8 million when compared to \$5.8 million, or \$0.20 per Class A Ordinary Share for the Second Quarter 2011.

Disclosure Controls and Procedures

The President and Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), together with Management, have established and maintained the Company's disclosure controls and procedures, to provide reasonable assurance that material information relating to the Company is made known to them by others, particularly during the quarter ending March 31, 2013 and information required to be disclosed by the issuer in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

Internal Controls over Financial Reporting ("ICFR")

The CEO and CFO of the Company, together with Management, have established and maintained the Company's internal control over financial reporting (ICFR), as defined in National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with US GAAP.

The design of CUC's internal controls over financial reporting has been established and evaluated using the criteria set forth in the Internal Control-Integrated Framework by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). There was no material weakness relating to design existing as of March 31, 2013. There has been no change in the Company's ICFR that occurred during the period beginning on January 1, 2013 and ended on March 31, 2013 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Outlook

A Certificate of Need for generation capacity was issued to the Electricity Regulatory Authority ("ERA") by the Company in November 2011, driven primarily by the upcoming retirements of some of the Company's generating units due to begin in 2014.

In March 2012, the ERA solicited Request for Proposals (RFP) for an additional 36 MW of generation capacity from qualified bidders (including CUC). In February 2013, the Company was advised that another local company, DECCO Ltd., had won the bid.

In April 2013 the ERA announced that it would be engaging an independent party to conduct an investigation into the 36 MW bid process following public statements being made by its former managing director concerning alleged irregularities with the process. The Company is becoming increasingly concerned that the ongoing delays in the process to secure firm generating capacity may lead to inadequate installed generation capacity given that 18 MW of the 36 MW capacity was intended to have been installed for July 2014 to serve the needs of Grand Cayman. However the Company will explore all options, including temporary generation solutions to mitigate the threat of extended power outages for the summer of 2014.

Outstanding Share Data

At May 3, 2013 the Company had issued and outstanding 28,853,387 Ordinary Shares and 250,000 9% cumulative Participating Class B Preference Shares.

Additional information, including CUC's Annual Information Form, is available on SEDAR at www.sedar.com and on the Company's website at www.cuc-cayman.com.

Letitia T. Lawrence

Vice President Finance & Chief Financial Officer

May 3, 2013

Consolidated Balance Sheets (expressed in thousands of United States Dollars)

| Unaudited | Note | As at March 31, 2013 | As at December 31, 2012 |
|---|------|-------------------------|-------------------------|
| Assets | | | |
| Current Assets | | | |
| Cash and Cash Equivalents | | 2,950 | 694 |
| Accounts Receivable | 4 | 17,675 | 20,002 |
| Other Receivable – Insurance | 5 | 124 | 123 |
| Regulatory Assets | 6 | 26,973 | 25,795 |
| Inventories | 7 | 4,630 | 4,380 |
| Prepayments | | <u>1,355</u> | <u>2,558</u> |
| | | 53,707 | 53,552 |
| Property, Plant and Equipment | 8 | 377,258 | 377,106 |
| Other Assets | 9 | 1,338 | 1,388 |
| Intangible Assets | 10 | 2,860 | 2,926 |
| Total Assets | | 435,163 | 434,972 |
| Liabilities and Shareholders' Equity | | | |
| Current Liabilities | | | |
| Bank Overdraft | | 4,378 | 6,200 |
| Accounts Payable and Accrued Expenses | 11 | 31,897 | 28,550 |
| Regulatory Liabilities | 6 | 315 | 345 |
| Short-Term Debt | 12 | 31,000 | 31,000 |
| Current Portion of Long-Term Debt | | 19,500 | 19,500 |
| Consumers' Deposits and Advances for Construction | | 4,662 | 4,585 |
| | | 91,752 | 90,180 |
| Defined Benefit Pension Liability | 18 | 1,918 | 1,926 |
| Long-Term Debt | | <u>169,000</u> | <u>169,000</u> |
| Total Liabilities | | 262,670 | 261,106 |
| Shareholders' Equity | | | |
| Share Capital | | 1,967 | 1,965 |
| Share Premium | | 79,014 | 78,524 |
| Additional Paid in Capital | 13 | 457 | 450 |
| Retained Earnings | | 92,680 | 94,647 |
| Accumulated Other Comprehensive Loss | | (1,625) | (1,720) |
| Total Shareholders' Equity | | 172,493 | 173,866 |
| Total Liabilities and Shareholders' Equity | | 435,163 | 434,972 |

Consolidated Statements of Earnings(expressed in thousands of United States Dollars, except basic and diluted earnings per ordinary share and the Weighted Average of Class A Ordinary Shares issued and fully paid)

| Unaudited | Note | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|---|------|---|---|
| Operating Revenues | | | |
| Electricity Sales | | 15,946 | 15,921 |
| Fuel Factor | | <u>36,579</u> | <u>35,732</u> |
| Total Operating Revenues | | 52,525 | 51,653 |
| Operating Expenses | | | |
| Power Generation | | 37,323 | 36,644 |
| General and Administration | | 2,080 | 2,777 |
| Consumer Services | | 409 | 385 |
| Transmission and Distribution | | 601 | 615 |
| Depreciation | | 6,376 | 5,678 |
| Maintenance | | 1,546 | 1,927 |
| Amortization of Intangible Assets | | <u>79</u> | <u>99</u> |
| Total Operating Expenses | | 48,414 | 48,125 |
| Operating Income | | 4,111 | 3,528 |
| Other (Expenses)/Income: | | | |
| Finance Charges | 17 | (2,243) | (2,445) |
| Foreign Exchange Gain | 19 | 472 | 500 |
| Other Income | | <u>558</u> | <u>324</u> |
| Total Net Other (Expenses)/Income | | (1,213) | (1,621) |
| | | | |
| Earnings for the Period | | 2,898 | 1,907 |
| Preference Dividends Paid- Class B | | <u>(113)</u> | <u>(113)</u> |
| Earnings on Class A Ordinary Shares | | 2,785 | 1,794 |
| Weighted-Average Number of Class A Ordinary Shares Issued and | | | |
| Fully Paid (in thousands) | 14 | 28,806 | 28,625 |
| Earnings per Class A Ordinary Share | 14 | 0.10 | 0.06 |
| Diluted Earnings per Class A Ordinary Share | 14 | 0.10 | 0.06 |
| Dividends Declared per Class A Ordinary Share | | 0.165 | 0.165 |

Consolidated Statements of Comprehensive Income

(expressed in thousands of United States Dollars)

| Unaudited | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|-------------------------------------|---|---|
| Earnings for the Period | 2,898 | 1,907 |
| Other Comprehensive Income/(Loss): | | |
| Amounts arising during the period: | | |
| Reclassification to net income: | | |
| Defined Benefit Pension plans: | | |
| Amortization of prior service costs | 62 | 62 |
| Amortization of net actuarial loss | <u>33</u> | <u>156</u> |
| Total Other Comprehensive Income | 95 | 218 |
| Comprehensive Income | 2,993 | 2,125 |

Consolidated Statements of Shareholders' Equity (expressed in thousands of United States Dollars except Common Shares)

| Unaudited | Common Shares (in thousands) | Common Shares Value (\$) | Preference Shares (\$) | Share premium (\$) | Additional paid-in capital (\$) | Accumulated Other Comprehensive Loss (\$) | Retained Earnings (\$) | Total Equity (\$) |
|---|------------------------------------|--------------------------------|---------------------------|--------------------------|---------------------------------------|--|------------------------------|-------------------------|
| As At January 1, 2013 | 28,806 | 1,715 | 250 | 78,524 | 450 | (1,720) | 94,647 | 173,866 |
| Net Earnings | - | - | - | - | - | - | 2,898 | 2,898 |
| Common Share Issuance & stock options plans | 47 | 2 | - | 490 | 7 | - | - | 499 |
| Defined benefit plans | - | - | | | - | 95 | - | 95 |
| Dividends on common shares | | | | | | | (4,752) | (4,752) |
| Dividends on preference shares | | | | | | - | (113) | (113) |
| As At March 31, 2013 | 28,853 | 1,717 | 250 | 79,014 | 457 | (1,625) | 92,680 | 172,493 |
| As At January 1, 2012 | 28,625 | 1,704 | 250 | 76,806 | 415 | (2,747) | 96,827 | 173,255 |
| Net Earnings | - | - | - | - | - | | 1,907 | 1,907 |
| Common Share Issuance & stock options | | | | | | | | |
| plans Defined benefit plans | 48 | 3 | , | 491 | 12 | 218 | , | 218 |
| Dividends on common shares | | - | - | - | - | | (4,721) | (4,721) |
| Dividends on preference shares | | | | | | | (113) | (113) |
| As At March 31, 2012 | 28,673 | 1,707 | 250 | 77,297 | 427 | (2,529) | 93,900 | 171,052 |

Consolidated Statements of Cash Flows

(expressed in thousands of United States Dollars)

| Unaudited | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|---|---|---|
| | | |
| Operating Activities | | |
| Earnings for the period | 2,898 | 1,907 |
| Items not affecting cash: | | |
| Depreciation | 6,376 | 5,678 |
| Amortization of Intangible Assets | 79 | 99 |
| Non-cash Pension Expenses | (87) | 242 |
| Amortization of Deferred Financing Costs | 49 | 51 |
| Stock-based compensation | <u>7</u> | <u>12</u> |
| | 9,322 | 7,989 |
| Net change in non-cash working capital balances related to operations | 7,220 | 2,263 |
| Net Change in Regulatory Deferrals | (1,209) | <u>(39)</u> |
| Cash flow related to operating activities | 15,333 | 10,213 |
| Investing Activities | | |
| Purchase of property, plant and equipment | (6,399) | (6,902) |
| Costs related to intangible assets | (18) | (80) |
| Insurance funds received | - | 1,052 |
| Proceeds on sale of property, plant and equipment | <u>15</u> | Ξ |
| Cash flow related to investing activities | (6,402) | (5,930) |
| Financing Activities | | |
| (Decrease)/Increase in bank overdraft | (1,822) | 1,714 |
| Dividends paid | (5,345) | (5,317) |
| Net proceeds from share issues | <u>492</u> | <u>494</u> |
| Cash flow related to financing activities | (6,675) | (3,109) |
| Increase/(Decrease) in net cash and cash equivalents | 2,256 | 1,174 |
| • | | |
| Cash and cash equivalents - Beginning of period | <u>694</u> | <u>424</u> |
| Cash and cash equivalents - End of period | 2,950 | 1,598 |
| Supplemental disclosure of cash flow information: Interest paid during the period | 62 | 70 |

Notes to Interim Consolidated Financial Statements

Unaudited - March 31, 2013 (expressed in thousands of United States dollars unless otherwise stated)

1. Nature of Operations and Consolidated Financial Statement Presentation

These consolidated financial statements have been prepared in accordance with United States Generally Accepted Accounting Principles ("US GAAP") and reflect the decisions of the Electricity Regulatory Authority ("ERA"). The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary DataLink, Ltd. ("DataLink"). These decisions affect the timing of the recognition of certain transactions resulting in the recognition of regulatory assets and liabilities, which Caribbean Utilities Company Ltd., ("CUC" or "the Company") considers it is probable to recover or settle subsequently through the rate-setting process.

The principal activity of the Company is to generate and distribute electricity in its licence area of Grand Cayman, Cayman Islands, pursuant to a 20-year exclusive Transmission & Distribution ("T&D") Licence and a 21.5 year non–exclusive Generation Licence (collectively the "Licences") with the Cayman Islands Government ("Government"), which expire in April 2028 and September 2029 respectively. These consolidated interim financial statements do not include all of the disclosures normally found in the Company's annual financial statements and should be read in conjunction with the MD&A and audited financial statements and notes thereto for the year ended December 31, 2012, with 2011 comparatives, prepared in accordance with US GAAP included in the Company's 2012 Annual Report.

In late March 2012 CUC's wholly owned subsidiary, DataLink, received its licence from the Information and Communications Technology Authority ("ICTA") which permits DataLink to provide fibre optic infrastructure and other information and communication technology (ICT) services to the ICT industry.

The ICTA is an independent statutory Authority which was created by the enactment of the Information and Communications Technology Authority Law on May 17 2002 and is responsible for the regulation and licensing of Telecommunications, Broadcasting, and all forms of radio. The ICTA sets the standards by which ICT networks must be developed and operated under.

All significant intercompany balances and transactions have been eliminated on consolidation.

Rate Regulated Operations

CUC's base rates are designed to recover and earn a return on all non-fuel and regulatory costs and include per kilowatt-hour ("kWh") electricity charges and fixed facilities charges. Fuel cost charges and license and regulatory fees are billed as separate line items. Base rates are subject to an annual review and adjustment each June through the rate cap and adjustment mechanism ("RCAM"). The ERA reviewed and approved a rate increase for June 2012 of 0.7% as a result of the 2011 RORB and the slight increase in the applicable United States and Cayman Islands consumer price indices, adjusted to exclude food and fuel, for calendar year 2011. All fuel and lubricating oil costs are passed through to customers without markup as a per kWh charge.

For regulatory purposes fixed assets comprise the completed Property, Plant and Equipment ("PP&E") and intangible assets acquired or constructed by the Company as reported in the Company's consolidated financial statements. The original book value of these fixed assets include an Allowance for Funds Used During Construction ("AFUDC") (Note 8) and an allowance for General Expenses Capitalised ("GEC") (Note 8). GEC is calculated as a percentage of up to 10% of Non-Fuel Operating Expenses, varying annually depending on the level of capital activity.

Seasonality

Interim results will fluctuate due to the seasonal nature of electricity consumption. In Grand Cayman, demand is highest in the summer months due to air-conditioning load. Consequently, interim results are not necessarily indicative of annual results.

2. <u>Summary of Significant Accounting Policies</u>

The preparation of financial statements in conformity with US GAAP requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Changes in Accounting Policies

The following new US GAAP accounting pronouncements that are applicable to, and were adopted by, CUC effective beginning January 1, 2013 are described as follows:

Disclosures About Offsetting Assets and Liabilities

Effective January 1, 2013, the Company adopted the amendments to Accounting Standards Codification ("ASC") Topic 210, Balance Sheet – Disclosures About Offsetting Assets and Liabilities as outlined in Accounting Standards Updates ("ASU") No. 2011-11 and 2013-01. The amendments expand the level of disclosures required by entities for such arrangements. ASU No. 2013-01 limits the scope of the new offsetting disclosure requirements previously issued in ASU No. 2011-11, to certain derivative instruments, repurchase and reverse repurchase agreements, and securities borrowing and lending arrangements that are either offset on the balance sheet or subject to an enforceable master netting or similar arrangement.

Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income

Effective January 1, 2013, the Company adopted the amendments to ASC Topic 220, Other Comprehensive Income - Reporting of Amounts Out of Accumulated Other Comprehensive Income ("AOCI") as outlined in ASU No. 2013-02. The amendments improve the reporting of reclassifications out of AOCI and require entities to report, in one place, information about reclassifications out of AOCI and to present details of the reclassifications in the disclosure for changes in AOCI balances. The effect of the reclassification of significant items to net income in their entirety during the reporting period must be reported in the respective line items in the statement where net income is presented. The effect of items not reclassified to net income in their entirety during the reporting period are to be presented in the notes to the consolidated financial statements.

The above-noted changes did not materially impact the Company's consolidated financial statements for the three months ended March 31, 2013.

4. Accounts Receivable

| | As at March 31, 2013 | As at December 31, 2012 |
|---------------------------------|----------------------|-------------------------|
| Billings to consumers | 11,514 | 14,106 |
| Unbilled revenues | 3,709 | 3,757 |
| Other receivables | 2,618 | 2,314 |
| Related Parties | 20 | 9 |
| Allowance for doubtful accounts | <u>(186)</u> | <u>(184)</u> |
| Total Accounts Receivable | 17,675 | 20,002 |

Unbilled Revenues

Revenue derived from the sale of electricity is taken to income on a bills-rendered basis, adjusted for unbilled revenues. Customer bills are issued throughout the month based on meter readings that establish electricity consumption since the last meter reading. The unbilled revenue accrual for the period is based on estimated electricity sales to customers since the last meter reading. The estimation process for accrued unbilled electricity consumption will result in adjustments of electricity revenue in the periods they become known when actual results differ from the estimates. Consumers are billed at the beginning of each month leading to the accrual of approximately three weeks of unbilled revenue.

Other receivables

Other receivables relate to amounts due outside of the normal course of operations. Items in other receivables include sale of inventory, machine break-down costs covered by warranties and amounts due from related parties. Other receivables at March 31, 2013 also include billing adjustments for commercial customers.

5. Other Receivable - Insurance

| | As At March 31, 2013 | As At December 31, 2012 |
|------------------------|----------------------|-------------------------|
| Other Insurance claims | <u>124</u> | <u>123</u> |
| Total | 124 | 123 |

Other insurance claims relate to incidents experienced in 2011. The claims process is expected to be completed during 2013.

6. Regulatory Assets and Liabilities

| Asset/Liability | Description | As At March 31, 2013 | As at December 31, 2012 |
|--|--|-------------------------|----------------------------|
| Regulatory Assets | Fuel Tracker Account (a) | 24,979 | 23,694 |
| Regulatory Assets | Derivative contract (b) | 543 | 837 |
| Regulatory Assets | Miscellaneous Regulatory Assets (c) | 370 | 384 |
| Regulatory Assets | Government & Regulatory Tracker Account (d) | <u>1,081</u> | <u>880</u> |
| Total Regulatory Assets | | 26,973 | 25,795 |
| Regulatory Liabilities Total Regulatory Liabilities | Miscellaneous Regulatory Liabilities (e) | (315) (315) | (345) (345) |

- a) Fuel Tracker Account The 2008 T&D Licence established a fuel tracker mechanism to ensure the Company and the consumers neither gain nor lose from the pass through of fuel costs. The purpose of the fuel tracker account is to accumulate actual fuel costs incurred less fuel factor revenues collected. This account represents deferred accumulated fuel costs to be recovered from or reimbursed to the consumers. The receivable or payable value represents a regulatory asset or liability. The net position of the fuel tracker accounts fluctuates monthly and is affected by fuel prices and electricity consumption.
- b) Derivative contract The Company's purpose of hedging is to reduce the impact of volatility in the Fuel Cost Charge paid by the Company's customers in the face of price volatility for the fuel that the Company must purchase in order to provide electric service. This account represents the fair value adjustments for the call options. The Company's call option contracts will expire on October 31, 2013.
- c) Miscellaneous regulatory assets represent costs incurred by the Company, other than fuel and the specifically itemised licence and regulatory fees, to be recovered through the Company's base rates on terms as agreed with the ERA.
- d) Government and Regulatory Tracker Account A licence fee of 1% of gross revenues applies to customer billings for consumption over 1,000 kWh per month as a pass-through charge on a per kWh basis. Additionally, a regulatory fee of ½ of 1% is charged on gross revenues then prorated and applied only to customer billings with consumption over 1,000 kWh per month. The government and regulatory tracker account is the actual fee incurred less the amount of funds received from consumers. The per kWh charge is then adjusted quarterly for the balance of this account.
- e) Miscellaneous regulatory liabilities represent costs owed by the Company, other than licence and regulatory fees, to be recovered through the Company's base rates on terms as agreed with the ERA.

7. Inventories

The composition of inventories is shown in the table below:

| Inventories | | |
|-------------|----------------------|-------------------------|
| | As At March 31, 2013 | As at December 31, 2012 |
| Fuel | 3,876 | 3,643 |
| Lube | 640 | 636 |
| Line spares | 88 | 75 |
| Other | <u>26</u> | <u>26</u> |
| Total | 4,630 | 4,380 |

8. Property, Plant and Equipment ("PP&E")

| Property, Plant and Equipment | Cost | Accumulated Depreciation | Net Book Value March 31, 2013 |
|---|----------------|--------------------------|-------------------------------------|
| Transmission & Distribution (T&D) | 276,223 | 87,972 | 188,251 |
| Generation | 279,227 | 111,108 | 168,119 |
| Other: | | | |
| Land | 5,304 | - | 5,304 |
| Buildings | 20,017 | 9,632 | 10,385 |
| Equipment, motor vehicles and computers | 19,243 | 14,044 | 5,199 |
| Total Other | 44,564 | <u>23,676</u> | 20,888 |
| Property, plant and equipment | 600,014 | 222,756 | 377,258 |
| Property, Plant and Equipment | Cost | Accumulated Depreciation | Net Book Value December 31, 2012 |
| Transmission & Distribution (T&D) | 274,398 | 87,826 | 186,572 |
| Generation | 276,637 | 107,474 | 169,163 |
| Other: | | | |
| Land | 5,304 | - | 5,304 |
| Buildings | 20,017 | 9,469 | 10,548 |
| Equipment, motor vehicles and computers | 19,384 | 13,865 | 5,519 |
| Total Other | 44,705 | 23,334 | <u>21,371</u> |
| Property, plant and equipment | <u>595,740</u> | <u>218,634</u> | <u>377,106</u> |

Included in PP&E are a number of capital projects in progress with a total cost to date of \$25.1 million (December 31, 2012: \$36.8 million). These projects primarily relate to various improvements to the Distribution System.

Also included in Generation and T&D is freehold land with a cost of \$5.0 million (December 31, 2012: \$5.0 million). In addition, line inventory with a cost of \$5.0 million (December 31, 2012: \$5.5 million) is included in T&D. Engine spares with a net book value of \$15.9 million (December 31, 2012: \$15.9 million) are included in Generation.

The capitalisation of 'Financing Costs' is calculated by multiplying the Company's Cost of Capital rate by the average work in progress for each month. The cost of capital rate for fiscal 2013 is 7.5% (2012: 8.25%) and will be adjusted annually. As a result, during the three month period ended March 31, 2013, the Company recognised \$0.8 million in AFUDC. The Company recognised an amount of \$0.7 million for the three month period ended March 31, 2012 under the provision for AFUDC.

GEC is calculated as a percentage of up to 10% of Non-Fuel Operating Expenses, varying annually depending on the level of capital activity. GEC totalled \$0.9 million for the three months ended March 31, 2013, comparable to GEC for the three months ended March 31, 2012.

In accordance with the Licences, when an asset is impaired or disposed of before the original estimated useful life, the cost of the asset is reduced and the net book value is charged to accumulated depreciation. This treatment is in accordance with the rate regulations standard under US GAAP and differs from non-regulatory treatment of a loss being recognized on the statement of earnings. The amount charged to accumulated depreciation is net of any proceeds received in conjunction with the disposal of the asset. This amount within accumulated depreciation is to be depreciated as per the remaining life of the asset based on

the original life when the unit was initially placed into service. In June 2012, the Company retired a 7.59 MW unit, with an original book value of \$6.7 million. The remaining net book value of the unit was charged to accumulated depreciation.

9. Other Assets

| | As at March 31, 2013 | As at December 31, 2012 |
|----------------------------|-------------------------|----------------------------|
| Deferred debt issue costs | 1,307 | 1,356 |
| Miscellaneous other assets | <u>31</u> | <u>32</u> |
| Total | 1,338 | 1,388 |

Deferred debt issue costs relate to transaction costs incurred in respect of financial liabilities. These costs are deferred on the balance sheet and are being amortized over the life of the related note using the effective-interest rate method.

10. Intangible Assets

| Intangible Assets | Cost | Accumulated Amortization | Net Book Value March 31, 2013 |
|--|-----------|-----------------------------|----------------------------------|
| Deferred licence renewal costs | 1,890 | 463 | 1,427 |
| Datalink Ltd. Deferred licence renewal costs | 231 | 14 | 217 |
| Computer Software | 4,666 | 3,652 | 1,014 |
| Other Intangible Assets in progress | 127 | - | 127 |
| Trademark Costs | <u>75</u> | <u>=</u> | <u>75</u> |
| Total | 6,989 | 4,129 | 2,860 |

| Intangible Assets | Cost | Accumulated Amortization | Net Book Value December 31, 2012 |
|--|-----------|--------------------------|-------------------------------------|
| Deferred licence renewal costs | 1,890 | 439 | 1,451 |
| Datalink Ltd. deferred licence renewal costs | 231 | 10 | 221 |
| Computer Software | 4,654 | 3,599 | 1,055 |
| Other Intangible Assets in progress | 124 | - | 124 |
| Trademark Costs | <u>75</u> | Ξ | <u>75</u> |
| Total | 6,974 | 4,048 | 2,926 |

Deferred licence renewal costs relate to negotiations with the Government for licences for the Company. Amortization of deferred licence renewal costs commenced upon conclusion of licence negotiations in April 2008 and extends over the life of the T&D Licence. Amortization of Datalink's deferred licence renewal costs commenced upon conclusion of licence negotiations in March 2012 and extends over the life of its ICTA licence.

11. Accounts Payable and Accrued Expenses

| | As at March 31, 2013 | As at December 31, 2012 |
|---|-------------------------|-------------------------|
| Fuel Cost Payable | 22,869 | 21,790 |
| Trade Accounts Payable & Accrued expenses | 2,562 | 2,594 |
| Accrued Interest | 3,726 | 891 |
| Dividends Payable | 111 | 592 |
| Other Accounts Payable | <u>2,629</u> | <u>2,683</u> |
| Total Accounts Payable | 31,897 | 28,550 |

Included in Other Accounts Payable is an amount related to fuel option contracts (see Note 15) of \$0.5 million at March 31, 2013 (\$0.8 million at December 31, 2012).

12. Short-Term Financing

The Company has \$47.0 million of unsecured credit financing facilities with the Royal Bank of Canada ("RBC"). In May 2012 the Company renegotiated and increased the credit facilities agreement with RBC. The total available was \$10.6 million at March 31, 2013 (\$8.8 million at December 31, 2012).

| | Total Credit Financing Facilities | Total Utilised March 31, 2013 | Total Available March 31, 2013 |
|--|--------------------------------------|----------------------------------|-----------------------------------|
| Corporate Credit Card Line* | 400 | 400 | - |
| Letters of Credit | 602 | 602 | - |
| Operating, Revolving Line of Credit | 7,500 | 4,378 | 3,122 |
| Catastrophe Standby Loan | 7,500 | - | 7,500 |
| Demand Loan Facility- Interim Funding of Capital Expenditures Total | 31,000 47,002 | 31,000 36,380 | - 10,622 |

^{*.} Included in Accounts payable and accrued expenses

A stand-by fee of 1/5 of 1% per annum in arrears is applied to the unused portion of the capital expenditure and catastrophe lines of the facility. A review fee of 1/8 of 1% of the total credit facilities is incurred annually in arrears.

13. Share Options

The shareholders of the Company approved an Executive Stock Option Plan on October 24, 1991, under which certain employees and officers may be granted options to purchase Class A Ordinary Shares of the Company.

The exercise price per share in respect of options is equal to the fair market value of the Class A Ordinary Shares on the date of grant. Each option is for a term not exceeding ten years, and will become exercisable on a cumulative basis at the end of each year following the date of grant. The maximum number of Class A Ordinary Shares under option shall be fixed and approved by the shareholders of the Company from time to time and is currently set at 1,220,100. Options are forfeited if they are not exercised prior to their respective expiry date or upon termination of employment prior to the completion of the vesting period.

| Share Options | March 31, 2013 Number of options | March 31, 2013 Weighted average exercise price per share | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value (\$ millions) |
|------------------------------------|-------------------------------------|---|--|---|
| Outstanding at beginning of period | 605,900 | 11.18 | | |
| Granted | - | - | | |
| Exercised | (4,000) | 8.76 | | |
| Forefeited | - | - | | |
| Expired | Ξ | Ξ. | | |
| Outstanding, end of period | 601,900 | 11.19 | 5.20 | 0.75 |
| Vested, end of the period | 414,900 | 11.89 | 3.45 | 0.80 |

Under the fair value method, the compensation expense was \$0.01 million for the three month period ended March 31, 2013 (March 31, 2012: \$0.01 million), resulting in a corresponding increase of Additional Paid in Capital.

14. Earnings per Share

The Company calculates earnings per share on the weighted average number of Class A Ordinary Shares outstanding. The weighted average Class A Ordinary Shares outstanding were 28,805,956 and 28,624,677 for the three month period ended March 31, 2013 and March 31, 2012 respectively.

The weighted average of Class A Ordinary Shares used for determining diluted earnings were 28,822,691 and 28,638,678 for the three month period ended March 31, 2013 and March 31, 2012 respectively. Diluted earnings per Class A Ordinary Share was calculated using the treasury stock method.

As at March 31, 2013 the outstanding options are not materially dilutive as the market price of common shares is below or marginally higher than the exercise price.

| | Earnings (in thousands) March 31, 2013 | Weighted average shares (in thousands) March 31, 2013 | Earnings per Common Shares March 31, 2013 |
|--|--|--|---|
| Net earnings applicable to common shares | 2,785 | | |
| Weighted Average share outstanding | | 28,806 | |
| Basic Earnings Per Common Share | | | 0.10 |
| Effect of potential dilutive securities: | | | |
| Stock Options | Ξ. | <u>17</u> | Ξ |
| Diluted Earnings per Common Share | 2,785 | 28,823 | 0.10 |
| | | Weighted average | |
| | | | |
| | Earnings (in thousands) March 31, 2012 | shares (in thousands) March 31, 2012 | Earnings per Common Shares March 31, 2012 |
| Net earnings applicable to common shares | thousands) March | shares (in thousands) March | Common Shares |
| Net earnings applicable to common shares Weighted Average share outstanding | thousands) March 31, 2012 | shares (in thousands) March | Common Shares |
| | thousands) March 31, 2012 | shares (in thousands) March 31, 2012 | Common Shares |
| Weighted Average share outstanding | thousands) March 31, 2012 | shares (in thousands) March 31, 2012 | Common Shares March 31, 2012 |
| Weighted Average share outstanding Basic Earnings Per Common Share | thousands) March 31, 2012 | shares (in thousands) March 31, 2012 | Common Shares March 31, 2012 |

15. Fair Value Measurement

Fair value is the price at which a market participant could sell an asset or transfer a liability to an unrelated party. A fair value measurement is required to reflect the assumptions that market participants would use in pricing an asset or liability based on the best available information. These assumptions include the risks inherent in a particular valuation technique, such as a pricing model, and the risks inherent in the inputs to the model. A fair value hierarchy exists that prioritizes the inputs used to measure fair value. The Company is required to determine the fair value of all derivative instruments in accordance with the following hierarchy:

The three levels of the fair value hierarchy are defined as follows:

- Level 1: Fair value determined using unadjusted quoted prices in active markets.
- Level 2: Fair value determined using pricing inputs that are observable.
- Level 3: Fair value determined using unobservable inputs only when relevant observable inputs are not available.

The fair values of the Company's financial instruments, including derivatives, reflect a point-in-time estimate based on current and relevant market information about the instruments as at the balance sheet dates. The estimates cannot be determined with precision as they involve uncertainties and matters of judgment and, therefore, may not be relevant in predicting the Company's future earnings or cash flows.

The estimated fair values of the Company's financial instruments, including derivative financial instruments, are as follows:

| | As at March 31 | , 2013 | As at December 31, 2012 | | |
|---|----------------|------------|-------------------------|------------|--|
| | Carrying Value | Fair Value | Carrying Value | Fair Value | |
| Long-term debt, including current portion | 188,500 | 212,153 | 188,500 | 214,647 | |
| Fuel Option Contracts ¹ | 543 | 543 | 837 | 837 | |

¹ Carrying value of fuel option contracts included in Accounts Payable and Accrued expenses

The fair value of long-term debt is determined by discounting the future cash flows of each debt instrument at an estimated yield to maturity equivalent to benchmark government bonds or treasury bills, with similar terms to maturity, plus a market credit risk premium equal to that of issuers of similar credit quality. Since the Company does not intend to settle the long-term debt prior to maturity, the fair value estimate does not represent an actual liability and, therefore, does not include exchange or settlement costs.

The Company measures the fair value of commodity contracts on a daily basis using the closing values observed on commodities exchanges and in over-the-counter markets, or through the use of industry-standard valuation techniques, such as option modelling or discounted cash flow methods, incorporating observable valuation inputs. The resulting measurements are the best estimate of fair value as represented by the transfer of the asset or liability through an orderly transaction in the marketplace at the measurement date.

The fair value of the fuel option contract reflects only the value of the heating oil derivative and not the offsetting change in the value of the underlying future purchases of heating oil. The derivatives' fair value shown in the below table reflects the estimated amount the Company would pay to terminate the contract at the stated date. The fair value has been determined using published market prices for heating oil commodities. The Company's option contracts will expire in October 2013.

The derivatives entered into by the Company relate to regulated operations and any resulting gains or losses and changes to fair value are recorded in the regulatory asset/regulatory liability accounts, subject to regulatory approval and passed through to customers in future rates.

The following table summarizes the fair value measurements of the Company's long term debt and fuel derivative contracts based on the three levels that distinguish the level of pricing observability utilized in measuring fair value.

| Financial Liability | March 31, 2013 Total Fair Value | Level 1 - Quoted Prices in active markets for identical assets | Level 2 - Significant Other inputs | Level 3 - Significant unobservable inputs |
|---|------------------------------------|--|--|--|
| Long-term debt, including current portion | 212,153 | - | 212,153 | - |
| Option Contracts ¹ 1 Carrying value of fuel option contracts included in Accounts Pa | 543 | - | 543 | - |

16. Financial Risk Management

The Company is primarily exposed to credit risk, liquidity risk and interest rate risk as a result of holding financial instruments in the normal course of business.

Credit Risk

The Company is exposed to credit risk in the event of non-performance by counterparties to derivative financial instruments which include fuel option contracts. If counterparty fails to perform on its contractual obligation to deliver payment when the market price of fuel is greater than the strike price, the Company may find it necessary to purchase diesel at the market price, which will be higher than the contract price. The Company manages this credit risk associated with counterparties by conducting business with high credit-quality institutions. The Company does not expect any counterparties to fail to meet their obligations.

There is risk that CUC may not be able to collect all of its accounts receivable and other assets. This does not represent a significant concentration of risk. The requirements for security deposits for certain customers, which are advance cash collections from customers to guarantee payment of electricity billings; reduces the exposure to credit risk. CUC manages credit risk primarily by executing its credit collection policy, including the requirement for security deposits, through the resources of its customer service department.

Liquidity Risk

The Company's financial position could be adversely affected if it failed to arrange sufficient and cost-effective financing to fund, among other things, capital expenditures and the repayment of maturing debt. The ability to arrange such financing is subject to numerous factors, including the results of operations and financial position of the Company, conditions in the capital and bank credit markets, ratings assigned by ratings agencies and general economic conditions. These factors are mitigated by the legal requirement per the Licences which requires rates be set to enable the Company to achieve and maintain a sound credit rating in the financial markets of the world.

| (\$millions) | Total | 2013 | 2014-2015 | 2016-2017 | 2018 |
|---|-------------|-------------|-------------|-------------|-------------|
| | | | | | Onward |
| Bank Overdraft | 4.4 | 4.4 | - | - | - |
| Accounts payable and accrued expenses | 31.9 | 31.9 | - | - | - |
| Consumer's Deposits and Advances for Construction | 4.7 | 4.7 | - | - | - |
| Short term debt | 31.0 | 31.0 | - | - | - |
| Letter of credit | 0.6 | 0.6 | - | - | - |
| Long term debt | 188.5 | 19.5 | 31.0 | 25.0 | 113.0 |
| Long term debt interest | <u>73.8</u> | <u>10.8</u> | <u>18.5</u> | <u>15.2</u> | <u>29.3</u> |
| Total | 334.9 | 102.9 | 49.5 | 40.2 | 142.3 |

Interest Rate Risk

Long-term debt is issued at fixed interest rates, thereby minimising cash flow and interest rate exposure. The Company is primarily exposed to risks associated with fluctuating interest rates on its short-term borrowings and other variable interest credit facilities. The current amount of short-term borrowings is \$31.0 million.

17. Finance Charges

The composition of finance charges were as follows:

| (\$ thousands) | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|---------------------------------|--------------------------------------|--------------------------------------|
| Interest costs - long-term debt | 2,884 | 3,077 |
| Other interest costs | 148 | 113 |
| AFUDC * | <u>(789)</u> | <u>(745)</u> |
| Total | 2,243 | 2,445 |

^{*}Refer to PP&E with regards to AFUDC (Note 8) methodology.

18. Defined Benefit Pension Plan

The pension costs of the defined benefit plan are actuarially determined using the projected benefits method. Compensation expense of \$0.09 million was recognised for the three months ended March 31, 2013 (\$0.24 million March 31, 2012).

The composition of the expense was as follows:

| | Three Months Ended March 31, 2013 | Three Months Ended March 31, 2012 |
|------------------------------------|--------------------------------------|--------------------------------------|
| Interest cost | 67 | 80 |
| Expected return on plan assets | (75) | (56) |
| Amortisation of past service costs | 62 | 62 |
| Amortisation of actuarial losses | <u>33</u> | <u>156</u> |
| Total | 87 | 242 |

This expense has been recorded in general and administrative expenses.

19. Foreign Exchange

The closing rate of exchange on March 31, 2013 as reported by the Bank of Canada for the conversion of US dollars into Canadian dollars was Cdn\$1.00705 per US\$1.00. The official exchange rate for the conversion of Cayman Islands dollars into US dollars as determined by the Cayman Islands Monetary Authority is fixed at CI\$1.00 per US\$1.20. Thus, the rate of exchange as of March 31, 2013 for conversion of Cayman Islands dollars into Canadian dollars was Cdn\$1.20846 per CI\$1.00 (December 31, 2012: Cdn\$1.194).

20. Taxation

Under current laws of the Cayman Islands, there are no; income, estate, corporate, capital gains or other taxes payable by the Company.

The Company is levied custom duties of \$0.89 per IG of diesel fuel it imports. In addition, the Company pays customs duties of 15% on all other imports.

21. <u>Commitments</u>

The Company executed a primary fuel supply contract with Rubis Cayman Islands Limited ("Rubis") in September 2012 upon the expiration of its previous fuel supply contracts. Under the agreement the Company is committed to purchase approximately 60% of its diesel fuel requirements for its generating plant from Rubis. The approximate quantities per the contract on an annual basis are, by fiscal year in millions of IGs: 2013 – 19.4, 2014 – 11.3. The Company also executed a secondary fuel supply contract with Esso Cayman Limited ("Esso") in September 2012 and is committed to purchase approximately 40% of the Company's diesel fuel requirements for its generating plant from Esso. The approximate quantities per the contract on an annual basis are, by fiscal year in millions of IGs: 2013 – 13.0, 2014 – 7.6.

Both contracts expire July 31, 2014 with the option to renew for two additional 18 month terms. Renewal cannot occur more than six months in advance of the current contract expiry date. The point of delivery for fuel billing purposes is at the suppliers terminal. The Company is also responsible for the management of the fuel pipeline and ownership of bulk fuel inventory at the North Sound Road Power Plant.

As a result of the Company's bulk fuel inventory, the value of CUC's closing stock of diesel at March 31, 2013 was \$3.9 million (December 31, 2012: \$3.6 million). This amount includes all diesel held in CUC's bulk fuel storage tanks, service tanks and day tanks located at the North Sound Road Power Plant.

22. Comparative Figures

Certain comparative figures have been reclassified to conform with current year disclosure.

Shareholder Information

Shareholder Plans

CUC offers its Shareholders a Dividend Reinvestment Plan. Please contact one of CUC's Registrar and Transfer Agents or write to CUC's Assistant to the Company Secretary if you would like to receive information about the plan or obtain an enrolment form.

CUC also has a Customer Share Purchase Plan for customers resident in Grand Cayman. Please contact our Customer Service Department at (345) 949-5200 if you are interested in receiving details.

Shareholder Information

Duplicate Annual Reports

While every effort is made to avoid duplications, some shareholders may receive extra reports as a result of multiple share registrations. Shareholders wishing to consolidate these accounts should contact the Registrar and Transfer Agents.

Our Registrar and Transfer Agents are as follows:

CIBC Mellon Trust Company

P.O. Box 4202 Postal Station A Toronto, Ontario M5W 0E4, Canada Tel: (416) 682-3825-5500

Fax: (888) 249-6189

E-mail: inquiries@canstockta.com

Caribbean Utilities Company, Ltd.

Company Secretary P.O. Box 38 Grand Cayman KY1-1101 CAYMAN ISLANDS

Tel: (345) 949-5200 Fax: (345) 949-4621 E-mail: *investor@cuc.ky*

Website: www.cuc-cayman.com

If you require further information or have any questions regarding CUC's Class A Ordinary Shares (listed in US funds on the Toronto Stock Exchange), please contact:

Caribbean Utilities Company, Ltd.

Assistant to the Company Secretary P.O. Box 38 Grand Cayman KY1-1101 CAYMAN ISLANDS

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