



## **CUC Announces Second Quarter Results for the Period Ended June 30, 2016**

Caribbean Utilities Company, Ltd. is listed for trading in United States dollars on the Toronto Stock Exchange.

**Grand Cayman, Cayman Islands - Caribbean Utilities Company, Ltd. (TSX: CUP.U)** (“CUC” or “the Company”) announced today its unaudited results for the Second Quarter ended June 30, 2016 (all figures in United States dollars).

Sales for the three months ended June 30, 2016 (“Second Quarter 2016”) totalled 156.2 million kilowatt-hour (“kWh”), an increase of 10.2 million kWh in comparison to 146.0 million kWh for the three months ended June 30, 2015 (“Second Quarter 2015”). This 7% sales growth was driven by warmer weather conditions and an increase in customer numbers.

Operating income for Second Quarter 2016 totalled \$7.2 million, an increase of \$0.8 million when compared to operating income of \$6.4 million for Second Quarter 2015. The increase is primarily attributable to the 7% kWh sales growth, partially offset by higher depreciation and general and administration costs.

In addition to the factors positively impacting operating income, net earnings increased as a result of higher capitalization of interest expenses through the Allowance for Funds Used During Construction (“AFUDC”) of \$1.7 million in Second Quarter 2016 when compared to \$1.0 million in Second Quarter 2015. The increase in AFUDC, and resulting reduction in Finance Charges, is due primarily to the Company’s 39.7 megawatts (“MW”) Generation Project. AFUDC is the capitalisation of Financing Cost which is calculated by multiplying the Company’s Cost of Capital rate by the average construction work in progress for each month.

**Caribbean Utilities Company, Ltd.**

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The Company anticipates a reduction in AFUDC and an increase in depreciation costs commencing with the completion of the Generation Project.

Net earnings for the Second Quarter 2016 totalled \$7.5 million, an increase of \$2.0 million when compared to net earnings of \$5.5 million for the three months ended June 30, 2015 (“Second Quarter 2015”).

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Second Quarter 2016 were \$7.4 million, or \$0.23 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$5.4 million or \$0.17 per Class A Ordinary Share for the Second Quarter 2015.

Sales for the six months ended June 30, 2016 totalled 291.7 million kWh, an increase of 16.7 million kWh in comparison to 275.0 million kWh for the six months ended June 30, 2015. The average monthly temperature for the first six months of 2016 was 82.1 degrees Fahrenheit as compared to an average monthly temperature of 81.3 degrees for the first six months of 2015. Warmer temperatures increase air conditioning load and can positively impact the Company’s sales.

Net earnings for the six months ended June 30, 2016 totalled \$12.5 million, an increase of \$3.7 million when compared to net earnings of \$8.8 million for the six months ended June 30, 2015. The increase is attributable to the 6% increase in kWh sales, higher other income, and lower interest costs. These items were partially offset by higher depreciation and transmission and distribution costs.



After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the six months ended June 30, 2016 were \$ 12.3 million, or \$ 0.38 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$8.6 million or \$0.28 per Class A Ordinary Share for the six months ended June 30, 2015.

The continued reduction in world market fuel prices as well as the 30 cents Government reduction in fuel duty have resulted in customers benefitting from significantly reduced electricity costs during the Second Quarter 2016. Residential customers who used an average of 1,000 kWh per month would have seen their monthly bills decline by approximately CI\$49 during the Second Quarter 2016 when compared to the same period in 2015.

However, historically, the world fuel market has been volatile and the Company continues to seek ways to connect other stable and competitively priced energy options to the grid to ensure that its commitment to provide a safe and reliable electricity service at least cost remains attainable.

The ground-breaking event for the 5 MW Solar Project at Bodden Town took place in May 2016. The project which is being developed by Entropy Cayman Solar Limited is progressing as planned and is expected to be operational by the end of 2016. The Company anticipates further renewable energy sources connected to the grid with a Request for Proposal for renewable energy being conducted by the Electricity Regulatory Authority (ERA) in the near future.



The Consumer-Owned Renewable Energy Generation (“CORE”) programme which allows consumers to generate energy from renewable sources and be compensated through stable, long-term rates continues to attract participants. At June 30, 2016, 146 customers were connected with 2,080 kilowatts (“kW”) of renewable capacity. The CORE programme allows customers to connect small scale solar systems or wind turbines to CUC’s distribution system and to reduce their monthly energy bills by generating their own electricity while remaining connected to the CUC grid.

The Company’s new Power House building was completed and the new engine room handed over during the Second Quarter 2016. On June 21, 2016 the official commissioning ceremony was held. CUC now has an additional 39.7 MW of diesel power which includes a 2.7 MW waste heat recovery steam turbine.

CUC is committed to providing reliable electric service to its customers. During the Second Quarter 2016, some customers were affected by a communication systems problem around the commissioning of the new engines which caused the generating unit to disconnect for short periods of time, triggering outages. CUC and its partner MAN have put all of the necessary resources in place to address these issues and the Company is confident they have now been resolved.

The CUC system Average Service Availability Index was 99.89% for the six months ended June 30, 2016 compared to 99.96 % for the six months ended June 30, 2015.



President and CEO Mr. Richard Hew says, “The quarter was mainly positive as we had strong demand for electricity which we were able to meet with the successful completion of the 39.7 MW power plant. Unfortunately some of our customers were impacted by frequent, short duration outages in June and our usual high reliability standard was not met. However, we are confident that the longer term reliability outlook is very positive with the addition of the new units.”

The Advanced Metering Infrastructure (“AMI”) project will soon be completed. At the end of June 2016, over 23,000 new meters were installed to residential properties and businesses across Grand Cayman. The project, which is expected to be completed at the end of July 2016 provides real time electricity consumption information and brings efficiencies in meter reading. Customers who have the new AMI meters are now able to monitor their consumption through our website and better manage their usage.

Mr. Hew added, “I am also pleased to report that during the quarter another Caymanian, Mr. Sacha Tibbetts was promoted to the executive level as Vice President, Customer Service and Technology. Sacha’s appointment to this new role solidifies our Executive team structure and will better position our company to deliver on our key strategic initiatives which include Reliability, New Business and Technology, Human Capital and Brand. These are very exciting times for the energy business and our team is ready to deliver positive results to all of our stakeholders.”



CUC's Second Quarter results and related Management's Discussion and Analysis ("MD&A") for the period ended June 30, 2016 are attached to this release and incorporated by reference.

The MD&A section of this report contains a discussion of CUC's unaudited 2016 Second Quarter results, the Cayman Islands economy, liquidity and capital resources, capital expenditures and the business risks facing the Company. The release and Second Quarter MD&A can be accessed at [www.cuc-cayman.com](http://www.cuc-cayman.com) (Investor Relations/Press Releases) and at [www.sedar.com](http://www.sedar.com).

CUC provides electricity to Grand Cayman, Cayman Islands, under an Electricity Generation Licence expiring in 2039 and an exclusive Electricity Transmission and Distribution Licence expiring in 2028. Further information is available at [www.cuc-cayman.com](http://www.cuc-cayman.com).

*Certain statements in the MD&A, other than statements of historical fact, are forward-looking 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 labeled "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 forward-looking statements, whether as a result of new information, future events or otherwise except as required by law.*

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Celebrating



Ground-breaking



Commissioning



Rewarding

Caribbean Utilities Company, Ltd.

## 2016 Second Quarter Report

June 30, 2016



## General Data

### **About the Company**

Caribbean Utilities Company, Ltd., known locally as “CUC”, commenced operations as the only electric utility in Grand Cayman on May 10, 1966. The Company currently has an installed generating capacity of 161 megawatts (“MW”). The record peak load of 103.3 MW was experienced on July 8, 2016. CUC is committed to providing a safe and reliable supply of electricity to over 28,000 customers. The Company has been through many challenging and exciting periods but has kept pace with Grand Cayman’s development for the past 50 years.

### **About the Cayman Islands**

The Cayman Islands, a United Kingdom Overseas Territory with a population of approximately 54,000, 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 Her Excellency Mrs. Helen Kilpatrick, 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 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 in the Management Discussion and Analysis section, concerning the use of forward-looking statements, which applies to the entirety of this Quarterly Report.



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## **Fellow Shareholders,**

During the Second Quarter 2016, Caribbean Utilities Company, Ltd. (“CUC” or “the Company”) recorded an increase in earnings, buoyed by growth in residential and commercial customer sales.

For the three months ended June 30, 2016 (“Second Quarter 2016”) the Company recorded a 7% increase in kilowatt-hour (“kWh”) sales. Sales for the Second Quarter 2016 totalled 156.2 million kWh in comparison to 146.0 million kWh for the three months ended June 30, 2015 (“Second Quarter 2015”) driven primarily by warmer weather conditions and an increase in customer numbers.

Operating income for Second Quarter 2016 totalled \$7.2 million, an increase of \$0.8 million when compared to operating income of \$6.4 million for Second Quarter 2015. The increase is primarily attributable to the 7% increase in kWh sales partially offset by higher depreciation and general and administration costs.

In addition to the factors positively impacting operating income, net earnings increased as a result of higher capitalization of interest expenses through the Allowance for Funds Used During Construction (“AFUDC”) of \$1.7 million in Second Quarter 2016 when compared to \$1.0 million in Second Quarter 2015. The increase in AFUDC, and resulting reduction in Finance Charges, is due primarily to the Company’s 39.7 megawatts (“MW”) Generation Project which was completed in June 2016. AFUDC is the capitalisation of Financing Cost which is calculated by multiplying the Company’s Cost of Capital rate by the average construction work in progress for each month.

The Company anticipates a reduction in AFUDC and an increase in depreciation costs commencing with the completion of the Generation Project.

Net earnings for the three months ended June 30, 2016 totalled \$7.5 million, an increase of \$2.0 million when compared to net earnings of \$5.5 million for the three months ended June 30, 2015 (“Second Quarter 2015”).

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Second Quarter 2016 were \$7.4 million, or \$0.23 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$5.4 million or \$0.17 per Class A Ordinary Share for Second Quarter 2015.

Sales for the six months ended June 30, 2016 totalled 291.7 million kWh, an increase of 16.7 million kWh in comparison to 275.0 million kWh for the six months ended June 30, 2015. The average monthly temperature for the first six months of 2016 was 82.1 degrees Fahrenheit as compared to an average monthly temperature of 81.3 degrees for the first six months of 2015. Warmer temperatures increase air conditioning load and positively impact the Company’s sales. In Second Quarter 2016 customer numbers increased to 28,372, an increase of 1% when compared to 28,008 customers as at June 30, 2015.

Net earnings for the six months ended June 30, 2016 totalled \$12.5 million, an increase of \$3.7 million when compared to net earnings of \$8.8 million for the six months ended June 30, 2015. The increase is attributable to the 6% increase in kWh sales, higher other income,

lower interest on long term debt and lower maintenance costs. These items were partially offset by higher depreciation and transmission and distribution costs.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the six months ended June 30, 2016 were \$ 12.3 million, or \$0.38 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$8.6 million or \$0.28 per Class A Ordinary Share for the six months ended June 30, 2015.

The new engine room houses two 18.5 MW diesel generating units, one 2.7 MW waste heat recovery steam turbine and associated auxiliary equipment replaces retiring generators and provides firm capacity to meet anticipated load growth. The new engine room has been described as the most fuel efficient plant of its kind in the region.

With the reduction in world fuel prices and the further 30 cents reduction in Government fuel duty in January, customers benefited from significantly reduced electricity costs during the Second Quarter 2016. The residential consumers who used an average of 1,000 kWh per month would have seen their monthly bills decline by approximately CI\$49 during the Second Quarter 2016 when compared to the same period in 2015.

The Company's average price per Imperial Gallon (IG) of fuel for the Second Quarter 2016 decreased 33% to \$2.06, compared to \$3.08 for the Second Quarter 2015. The Company's average price per IG of lubricating oil for the Second Quarter 2016 decreased 10% to \$10.59 when compared to \$11.75 for the Second Quarter 2015.

While current fuel prices remain low today, historically, the world fuel market has been volatile and the Company's efforts to connect other stable and competitively priced energy options to the grid have not been deterred.

The ground-breaking event for the 5 MW Solar Project at Bodden Town took place in May 2016. The project which is being developed by Entropy Cayman Solar Limited is progressing as planned and is expected to be operational by the end of 2016. The Company anticipates further renewable energy sources connected to the grid with a Request for Proposal for renewable energy being conducted by the Electricity Regulatory Authority (ERA) in the near future.

The Consumer-Owned Renewable Energy Generation (CORE) programme which allows consumers to generate energy from renewable sources and be compensated through stable, long-term rates continues to attract participants. At June 30, 2016, 146 customers were connected with 2,080 kilowatts ("kW") of renewable capacity. The CORE programme allows customers to connect small scale solar systems or wind turbines to CUC's distribution system and to reduce their monthly energy bills by generating their own electricity while remaining connected to the CUC grid.

The Advanced Metering Infrastructure (AMI) project will soon be completed. At the end of June 2016, over 23,000 new meters were installed to residential properties and businesses across Grand Cayman. The project, which is expected to be completed at the end of July provides real time electricity consumption information and brings efficiencies in meter reading. Customers who have the new AMI meters are now able to monitor their consumption through our website and better manage their usage.

The Company celebrated 50 years of operations on May 10, 2016 and continues to play a vital role in the development of the Island. CUC has progressed from 650 connected customers in 1966 to over 28,000 customers and from a peak demand of 0.9 MW, 50 years ago, to 103.3 MW in July 2016. As a result of the quality of the infrastructure, including a reliable and efficient electricity service, Grand Cayman has attracted investors and residents over the years.

During Second Quarter 2016, CUC honoured 27 employees for their many years of service and dedication. Collectively, they have given 485 years of service to the Company. We are grateful to them for the significant contribution they have made and continue to make to the Company. One such long serving employee, Mr. Sacha Tibbetts, was also promoted to the position of VP Customer Service and Technology during the period and is a welcomed addition to the executive team.

Our Company remains focussed on providing a safe and reliable electricity service to our customers at least cost and with respect to the environment, while at the same time delivering a fair return to you our shareholders.

J.F. Richard Hew  
President & Chief Executive Officer

July 29, 2016

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## 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") consolidated financial statements for the twelve months ended December 31, 2015 ("Fiscal 2015"). 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 accounting principles generally accepted in the United States ("US GAAP"), including certain accounting practices unique to rate-regulated entities. These accounting practices, which are disclosed in the notes to the Company's 2015 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 recovery or refund by the Company of costs of providing services, including a fair return on rate base assets, from customers through appropriate billing rates would not be subject to regulatory approval.*

*Certain statements in this MD&A, other than statements of historical fact, are forward-looking 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 sections labelled "Business Risks", "Capital Resources" and "Corporate and Regulatory Overview" 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 forward-looking 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.*

July 29, 2016

## Financial and Operational Highlights

(\$ thousands, except basic earnings per ordinary share, dividends paid per ordinary share and where otherwise indicated)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Electricity Sales Revenues	20,592	19,182	38,609	36,226	2,383	7%
Fuel Factor Revenues	17,323	24,866	39,039	56,530	(17,491)	-31%
Operating Revenues	37,915	44,048	77,648	92,756	(15,108)	-16%
Fuel and Lube Costs	17,323	24,866	39,039	56,530	(17,491)	-31%
Other Operating Expenses	13,381	12,799	26,302	25,349	953	4%
Total Operating Expenses	30,704	37,665	65,341	81,879	(16,538)	-20%
Earnings for the Period	7,544	5,514	12,475	8,795	3,680	42%
Cash Flow from Operating Activities	10,053	8,768	29,808	24,165	5,643	23%
<i>Per Class A Ordinary Share:</i>						
Basic Earnings	0.23	0.17	0.38	0.28	0.10	36%
Dividends Paid	0.170	0.165	0.335	0.330	0.005	2%
Total Customers	28,372	28,008	28,372	28,008	364	1%
Total Full Time Employees	201	200	201	200	1	1%
Customers per Employee (#)	141	140	141	140	1	1%
System Availability (%)	99.88	99.95	99.89	99.96	(0.06)	0%
Peak Load Gross (MW)	101.8	99.1	101.8	99.1	2.7	3%
<i>Millions of kWh:</i>						
Net Generation	167.4	156.5	312.7	294.7	18.0	6%
Kilowatt-Hour Sales	156.2	146.0	291.7	275.0	16.7	6%
Sales per employee	0.78	0.73	1.45	1.38	0.07	5%

## 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 25 year non-exclusive Generation Licence (“the Licences”) granted by the Cayman Islands Government (“Government”), which expire in April 2028 and November 2039, 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 2015 was 7.4% (2014: 7.4%). CUC’s RORB for 2016 is targeted in the 6.75% to 8.75% range (2015: 7.25% to 9.25%).

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 2016, following review and approval by the Electricity Regulatory Authority (“ERA”), the Company increased its base rates by 0.1%. This increase is a result of the 2015 RORB and the increase in the applicable United States (“US”) and Cayman Islands consumer price indices, adjusted to exclude food and fuel, for calendar year 2015. The change in the base rates as a percentage of the US and Cayman Islands consumer price indices was 80% based on the range of the RORB values. The required rate adjustment of 0.1% can be calculated by applying 80% to the total price

level index (60% of the Cayman Islands CPI and 40% of the US CPI) of 0.12%. 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 for regulating the electricity industry in the Cayman Islands in accordance with the ERA Law. The ERA oversees all licencees, establishes and enforces licence standards, enforces applicable environmental and performance standards, reviews the proposed RCAM, and sets the rate adjustment factors as appropriate.

In December 2015 the ERA approved CUC's 2016-2020 Capital Investment Plan in the amount of \$204 million. Costs related to the competitive bid award to install 39.7 megawatts ("MW") of generation capacity are included in the approved CIP in the amount of CUC's competitive bid.

As a result of CUC's successful bid, the Company entered into a design-build contract agreement for the generation project with the consortium of Burmeister & Wain Scandinavian Contractor A/S ("BWSC") of Denmark and MAN Diesel & Turbo SE ("MAN") of Germany. The agreement covers the purchase and turnkey installation of a new 39.7 MW power plant which is comprised of two 18.5 MW V48/60 medium-speed diesel generating units, one 2.7 MW waste heat recovery steam turbine, and associated auxiliary equipment. This contract with variation orders is now valued at approximately \$56.1 million, previously \$55.4 million. On this contract a total of \$11.1 million was spent in 2014, an additional \$38.8 million was spent during the year ended December 31, 2015, an additional \$5.1 million was spent during the six months ended June 30, 2016 and the remaining amount of \$1.1 million is expected to be spent during the last six months of 2016.

The total project cost was estimated at \$85 million and the actual overall costs are expected to amount to \$79.0 million. A total of \$11.6 million was spent in 2014, an additional \$47.9 million was spent on the project during the year ended December 31, 2015 and \$13.9 million was spent during the six months ended June 30, 2016 and the remaining amount of \$5.6 million is expected to be spent during 2016. This positive variance in actual costs compared to the bid is due primarily to a favourable exchange rate on the EURO portion of the MAN/BWSC contract and a shortened construction period resulting in lower financing costs. The project was completed in eighteen months, compared to an original estimated construction period of twenty-four months.

The generating units are housed in a new purpose built power house at the Company's North Sound Road Power Plant. The units were commissioned in May and June 2016.

CUC had also secured the supply of 7.5 MW of temporary mobile generation following the retirement of 17.5 MW of generation in early 2014. This retirement relates to units 14 and 16 which exhausted their useful lives in accordance with the Company's Generation Licence.

This temporary generation had ensured the continuity of supply until the installation of the firm capacity. CUC understands that reliability of service is critical to Grand Cayman's continued growth and development. The Company continues to focus on maintaining and

improving the level of service we offer to our customers. The temporary generating units were returned in June 2016.

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 ½ 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.

Performance standards provide a balanced framework of potential penalties or rewards compared to historical performance in the areas of planning, reliability, operating and overall performance. Standards include "zones of acceptability" where no penalties or rewards would apply.

CUC's wholly owned subsidiary, DataLink, Ltd. ("DataLink"), was granted a licence in 2012 from the Information and Communications Technology Authority ("ICTA") permitting 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. 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.

### **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.

### **Sales**

Sales for the three months ended June 30, 2016 ("Second Quarter 2016") totalled 156.2 million kWh, an increase of 10.2 million kWh in comparison to 146.0 million kWh for the Second Quarter 2015 driven primarily by growth in residential and commercial customer sales and higher customers numbers.



Sales for the six months ended June 30, 2016 totalled 291.7 million kWh, an increase of 16.7 million kWh in comparison to 275.0 million kWh for the six months ended June 30, 2015. The average monthly temperature for the first six months of 2016 was 82.1 degrees Fahrenheit as compared to an average monthly temperature of 81.3 degrees for the first six months of 2015. Warmer temperatures increase air conditioning load and can positively impact the Company's sales.

Total customers as at June 30, 2016 were 28,372, an increase of 364 customers, or 1%, compared to 28,008 customers as at June 30, 2015.

The following tables present customer and sales highlights:

Customers (#)	June 30, 2016	June 30, 2015	Change %
Residential	24,154	23,845	1%
Commercial	4,218	4,163	1%
<b>Total Customers</b>	<b>28,372</b>	<b>28,008</b>	<b>1%</b>

Sales (thousands kWh)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Residential	76,120	68,556	140,273	126,749	13,524	11%
Commercial	78,356	75,744	148,065	144,891	3,174	2%
Other (street lighting, etc.)	1,714	1,684	3,410	3,365	45	1%
<b>Total Sales</b>	<b>156,190</b>	<b>145,984</b>	<b>291,748</b>	<b>275,005</b>	<b>16,743</b>	<b>6%</b>

Average Consumption per Customer (thousands kWh)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Residential	1,051	960	969	889	80	9%
Commercial	60,941	58,834	58,101	56,636	1,465	3%

## Earnings

Operating income for Second Quarter 2016 totalled \$7.2 million, an increase of \$0.8 million when compared to operating income of \$6.4 million for Second Quarter 2015. The increase is attributable to the 7% increase in kWh partially offset by higher depreciation and general and administration costs.

In addition to the factors positively impacting operating income, net earnings increased as a result of higher capitalization of interest expenses through the Allowance for Funds Used During Construction ("AFUDC") of \$1.7 million in Second Quarter 2016 when compared to \$1.0 million in Second Quarter 2015. The increase in AFUDC, and resulting reduction in Finance Charges, is due primarily to the Company's 39.7 MW Generation Project which was completed in June 2016. AFUDC is the capitalisation of Financing Cost which is calculated by multiplying the Company's Cost of Capital rate by the average construction work in progress for each month.

The Company anticipates a reduction in AFUDC and an increase in depreciation costs commencing with the completion of the Generation Project.

Net earnings for Second Quarter 2016 totalled \$7.5 million, an increase of \$2.0 million when compared to net earnings of \$5.5 million for Second Quarter 2015.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Second Quarter 2016 were \$7.4 million, or \$0.23 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$5.4 million or \$0.17 per Class A Ordinary Share for the Second Quarter 2015.

Net earnings for the six months ended June 30, 2016 totalled \$12.5 million, an increase of \$3.7 million when compared to net earnings of \$8.8 million for the six months ended June 30, 2015. The increase is attributable to the 6% increase in kWh sales, higher other income, lower interest on long term debt and lower maintenance costs. These items were partially offset by higher depreciation and transmission and distribution costs.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the six months ended June 30, 2016 were \$ 12.3 million, or \$0.38 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$8.6 million or \$0.28 per Class A Ordinary Share for the six months ended June 30, 2015.

## Operating Revenues

Total operating revenues were as follows:

Revenues (\$ thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Residential	9,878	8,879	18,270	16,459	1,811	11%
Commercial	10,544	10,132	20,022	19,404	618	3%
Other (street lighting, etc.)	170	171	317	363	(46)	-13%
<b>Electricity Sales Revenues</b>	<b>20,592</b>	19,182	<b>38,609</b>	36,226	<b>2,383</b>	7%
<b>Fuel Factor Revenues</b>	<b>17,323</b>	24,866	<b>39,039</b>	56,530	<b>(17,491)</b>	-31%
<b>Total Operating Revenues</b>	<b>37,915</b>	44,048	<b>77,648</b>	92,756	<b>(15,108)</b>	-16%

Operating revenues for the Second Quarter 2016 were \$37.9 million, a decrease of \$6.1 million from \$44.0 million for the Second Quarter 2015. Operating revenues for the six months ended June 30, 2016 were \$77.6 million, a decrease of \$15.2 million from \$92.8 million for the six months ended June 30, 2015. The decrease in operating revenues for the three and six months ended June 30, 2016 was due primarily to lower fuel factor revenues which was partially offset by an increase in electricity sales.

Other revenues (street lighting, etc.) for the Second Quarter 2016 totalled \$0.2 million, comparable to \$0.2 million for the Second Quarter 2015. Other revenues for the six months ended June 30, 2016 totalled \$0.3 million, a decrease of \$0.1 million from \$0.4 million for the six months ended June 30, 2015.

Electricity sales revenues were \$20.6 million for the Second Quarter 2016, an increase of \$1.4 million from \$19.2 million for the Second Quarter 2015. Electricity sales revenues were \$38.6 million for the six months ended June 30, 2016, an increase of \$2.4 million from \$36.2 million for the six months ended June 30, 2015. Electricity sales revenues for the three and six months ended June 30, 2016 increased when compared to the same periods last year due to the increase in kWh sales and the 0.1% and 0.9% base rate increases effective June 1, 2016 and June 1, 2015 respectively.

Fuel factor revenues for the Second Quarter 2016 totalled \$17.3 million, a decrease of \$7.6 million, compared to fuel factor revenues of \$24.9 million for the Second Quarter 2015. The average Fuel Cost Charge rate billed to consumers for the Second Quarter 2016 was \$0.12 per kWh, compared to the average Fuel Cost Charge rate of \$0.18 per kWh for the Second Quarter 2015. CUC passes through all fuel costs to consumers on a two-month lag basis with no mark-up.

Fuel factor revenues for the six months ended June 30, 2016 totalled \$39.0 million, a decrease of \$17.5 million compared to fuel factor revenues of \$56.5 million for the six months ended June 30, 2015. Fuel factor revenues for the six months ended June 30, 2016 decreased when compared to the six month period ended June 30, 2015 due to a reduction in global oil prices and a reduction in custom duties levied on diesel fuel imports by the Government. The average Fuel Cost Charge rate billed to consumers for the six months ended June 30, 2016 was \$0.14 per kWh, compared to the average Fuel Cost Charge rate of \$0.21 per kWh for the six months ended June 30, 2015.

## Operating Expenses

Operating expenses were as follows:

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
<b>Operating Expenses (\$ thousands)</b>						
Power Generation Expenses	<b>18,324</b>	25,918	<b>41,087</b>	58,514	<b>(17,427)</b>	-30%
General and Administration	<b>2,373</b>	2,068	<b>4,460</b>	4,510	<b>(50)</b>	-1%
Consumer Service	<b>722</b>	760	<b>1,352</b>	1,401	<b>(49)</b>	-3%
Transmission and Distribution	<b>864</b>	707	<b>1,621</b>	1,433	<b>188</b>	13%
Depreciation	<b>6,830</b>	6,578	<b>13,598</b>	12,888	<b>710</b>	6%
Maintenance	<b>1,440</b>	1,511	<b>2,921</b>	2,887	<b>34</b>	1%
Amortization of Intangible Assets	<b>151</b>	<b>123</b>	<b>302</b>	<b>246</b>	<b>56</b>	23%
<b>Total Operating Expenses</b>	<b>30,704</b>	37,665	<b>65,341</b>	81,879	<b>(16,538)</b>	-20%

Operating expenses for the Second Quarter 2016 totalled \$30.7 million, a \$7.0 million decrease from \$37.7 million for the Second Quarter 2015. This decrease was due primarily to lower power generation expenses, partially offset by higher general and administration, depreciation and transmission and distribution expenses for the Second Quarter 2016 when compared to the Second Quarter 2015.

Operating expenses for the six months ended June 30, 2016 totalled \$65.3 million, a \$16.6 million decrease from \$81.9 million for the six months ended June 30, 2015. This decrease was due primarily to lower power generation, general and administration costs and

consumer services, partially offset by higher depreciation and transmission and distribution expenses.

### Power Generation

Power generation costs for the Second Quarter 2016 decreased \$7.6 million to \$18.3 million when compared to \$25.9 million for the Second Quarter 2015. This decrease is as a result of lower fuel costs.

Power generation costs for the six months ended June 30, 2016 decreased \$17.4 million to \$41.1 million when compared to \$58.5 million for the six months ended June 30, 2015. This decrease is as a result of lower fuel costs.

Power generation expenses were as follows:

Power Generation (\$ thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Fuel costs (net of deferred fuel charges)	16,646	24,357	37,873	55,401	(17,528)	-32%
Lubricating Oil costs (net of deferred lubricating oil charges)	677	509	1,166	1,129	37	3%
Temporary generation costs	148	196	363	309	54	17%
Other generation expenses	853	856	1,685	1,675	10	1%
<b>Total power generation expenses</b>	<b>18,324</b>	<b>25,918</b>	<b>41,087</b>	<b>58,514</b>	<b>(17,427)</b>	<b>-30%</b>

The Company's average price per IG of fuel for the Second Quarter 2016 decreased 33% to \$2.06, compared to \$3.08 for the Second Quarter 2015.

Net generation was 167.4 million kWh for the Second Quarter 2016, a 7% increase when compared to 156.5 million kWh for the Second Quarter 2015. Net fuel efficiency for the Second Quarter 2016 of 18.71 kWh per IG increased when compared to net fuel efficiency for the Second Quarter 2015 of 17.70 kWh per IG.

Net generation was 312.7 million kWh for the six months ended June 30, 2016 compared to 294.7 million kWh for the six months ended June 30, 2015. Net fuel efficiency for the six months ended June 30, 2016 of 18.49 kWh per IG increased when compared to net fuel efficiency for the six months ended June 30, 2015 of 18.03 kWh per IG. This increase in net fuel efficiency for the three and six months ended June 30, 2016 is due primarily to the new generation units that came on-line in May and June 2016 and the decrease in use of the temporary mobile generation units.

The Company's average price per IG of lubricating oil for the Second Quarter 2016 decreased to \$10.59 when compared to \$11.75 for the Second Quarter 2015. The Company's average price per IG of lubricating oil for the six months ended June 30, 2016 decreased to \$11.04 when compared to \$12.32 for the six months ended June 30, 2015.

The Fuel Tracker Account (see Note 6 of the consolidated financial statements) 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 Program. The objective of the program 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 2015 utilize call options and call spreads to promote transparency in pricing. The monthly hedging costs and returns are also included within the Fuel Tracker Account.

CUC had secured the supply of 10.5 MW of temporary mobile generation following the retirement of 17.5 MW of generation in early 2014 in accordance with the Generation Licence. Temporary generation expenses for the Second Quarter 2016 totalled \$0.1 million, a \$0.1 million decrease when compared to Temporary generation expenses of \$0.2 million for the Second Quarter 2015. Temporary generation expenses for the six months ended June 30, 2016 totalled \$0.4 million, a \$0.1 million increase when compared to temporary generation expenses of \$0.3 for the six months ended June 30, 2015. All temporary generating units had been returned to the supplier by the end of the Second Quarter 2016.

Other generation expenses for the Second Quarter 2016 totalled \$0.9 million, comparable to other generation expenses of \$0.9 million for the Second Quarter 2015. Other generation expenses for the six months ended June 30, 2016 totalled \$1.7 million, comparable to other generation expenses of \$1.7 million for the six months ended June 30, 2015.

#### **General and Administration ("G&A")**

G&A expenses for the Second Quarter 2016 totalled \$2.4 million, a \$0.3 million increase compared to \$2.1 million for the Second Quarter 2015. This increase primarily relates to higher staff welfare costs, public relation expenses, donations, scholarships and legal fees.

G&A expenses for the six months ended June 30, 2016 totalled \$4.5 million comparable to G&A expenses of \$4.5 million for the six months ended June 30, 2015.

General Expenses Capitalised ("GEC") totalled \$2.2 million for the six months ended June 30, 2016, an increase of \$0.1 million when compared to \$2.1 million for the six months ended June 30, 2015.

#### **Consumer Services ("CS")**

CS expenses for the Second Quarter 2016 totalled \$0.7 million, a \$0.1 million decrease compared to \$0.8 million for the Second Quarter 2015. This decrease is primarily attributable to an adjustment in Second Quarter 2015 to the allowance for doubtful accounts which was partially offset by an increase in temporary staff costs.

CS expenses for the six months ended June 30, 2016 totalled \$1.4 million, comparable to \$1.4 million for the six months ended June 30, 2015.

In accordance with its AFDA policy, the Company maintains an accumulated provision for uncollectible customer accounts receivable that is estimated based on known accounts, historical experience and other currently available information, including the economic environment.

Trade and other accounts receivable (\$ thousands)	As at June 30, 2016	As at December 31, 2015
Current	9,689	8,414
Past due 31-60 days	628	1,018
Past due 61-90 days	1,631	240
Past due over 90 days	<u>4,370</u>	<u>4,313</u>
Total Accounts Receivable	16,318	13,985
Less: Allowance for doubtful accounts	(2,297)	(2,218)
Less: Consumer Deposits	<u>(7,344)</u>	<u>(6,823)</u>
Net Exposure	6,677	4,944

Net Exposure as at June 30, 2016 totalled \$6.7 million, an increase of \$1.8 million, or 37% when compared to the Net Exposure of \$4.9 million as at December 31, 2015. This increase was primarily related to an increase in receivables in the current category and the 61-90 day category partially offset by a decrease in the 31-60 day category. The current category of receivables increased by \$1.3 million or 15% due to higher electricity billings. The 61-90 day category of receivables increased by \$1.4 million due to primarily to the aging of Datalink receivables. The 31-60 day category of receivables decreased by \$0.7 million due to improved efficiencies in the disconnection process due to the newly installed Advanced Metering Infrastructure (“AMI”) meters. At the end of June 2016, 23,718 AMI meters were installed. Customers who have had the AMI meters installed are benefiting from the ability to monitor their consumption and manage their usage.

### Transmission and Distribution (“T&D”)

T&D expenses for the Second Quarter 2016 totalled \$0.9 million, an increase of \$0.2 million compared to T&D expenses for the Second Quarter 2015 of \$0.7 million. T&D expenses for the Second Quarter 2016 were impacted by an increase in overtime due to faults, increase in street light maintenance and costs associated with general tree trimming projects.

T&D expenses for the six months ended June 30, 2016 totalled \$1.6 million, an increase of \$0.2 million compared to T&D expenses for the six months ended June 30, 2015 of \$1.4 million. T&D expenses for the six months ended June 30, 2016 were impacted by an increase in overtime due to faults caused by bad weather and after hour outages, increase in street light maintenance and general tree trimming projects when compared to the six months ended June 30, 2015.

### Depreciation of Property, Plant and Equipment (“PP&E”)

Depreciation expenses for the Second Quarter 2016 totalled \$6.8 million, an increase of \$0.2 million, from \$6.6 million for the Second Quarter 2015. Depreciation expenses for the six months ended June 30, 2016 totalled \$13.6 million, an increase of \$0.7 million, from \$12.9 million for the six months ended June 30, 2015.

The increase in depreciation expenses is due to capital projects completed in prior periods.

## Maintenance

Maintenance expenses for the Second Quarter 2016 totalled \$1.4 million, a decrease of \$0.1 million when compared to \$1.5 million for the Second Quarter 2015. This decrease was partially due to a decrease in overtime labour and generator maintenance in Second Quarter 2016. The maintenance has been re-scheduled to be completed later in 2016.

Maintenance expenses for the six months ended June 30, 2016 totalled \$2.9 million, comparable to maintenance expenses for the six months ended June 30, 2015.

## Amortization

Amortization of intangible assets for the Second Quarter 2016 totalled \$0.2 million, an increase of \$0.1 million when compared to \$0.1 million for the Second Quarter 2015. Amortization of intangible assets for the six months ended June 30, 2016 totalled \$0.3 million, an increase of \$0.05 million when compared to \$0.25 million for the six months ended June 30, 2015. The increase in amortization is attributable to software purchases made in prior periods.

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 concluded 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 Income and Expenses experienced a switch from Net Other Expenses for the Second Quarter 2015 of \$0.9 million to Net Other Income of \$0.3 million for the Second Quarter 2016, an increase of \$1.2 million. A similar change was experienced for the six months ended June 30, 2016 as Net Other Income totalled \$0.1 million, an increase of \$2.2 million compared to Net Other Expenses of \$2.1 million for the six months ended June 30, 2015.

	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
<b>Other Income &amp; Expenses (\$ thousands)</b>						
Total interest costs	<b>(3,053)</b>	(3,197)	<b>(6,107)</b>	(6,444)	<b>337</b>	-5%
AFUDC	<b>1,734</b>	1,049	<b>3,646</b>	1,940	<b>1,706</b>	88%
Total finance charges	<b>(1,319)</b>	(2,148)	<b>(2,461)</b>	(4,504)	<b>2,043</b>	-45%
Foreign exchange gain	<b>240</b>	302	<b>546</b>	642	<b>(96)</b>	-15%
Other income	<b>1,412</b>	977	<b>2,083</b>	1,780	<b>303</b>	17%
<b>Total Net Other Income / (Expense)</b>	<b>3</b>	(869)	<b>168</b>	(2,082)	<b>2,250</b>	-108%

Finance charges for the Second Quarter 2016 totalled \$1.3 million, a \$0.8 million decrease from \$2.1 million for the Second Quarter 2015. Finance charges for the six months ended June 30, 2016 totalled \$2.5 million, a \$2.0 million decrease from \$4.5 million for the six months ended June 30, 2015. This decrease is as a result of higher Allowance for Funds Used During Construction (“AFUDC”) partially offset by higher other income for the three and six month periods ended June 30, 2015.

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 2016 was 7.75% (2015:8.25%) as agreed with the ERA, in accordance with the T&D Licence, and is reviewed annually.

The AFUDC amount for the Second Quarter 2016 totalled \$1.7 million, an increase of \$0.7 million from \$1.0 million for the Second Quarter 2015. The AFUDC amount for the six months ended June 30, 2016 totalled \$3.6 million, an increase of \$1.7 million from \$1.9 million for the six months ended June 30, 2015. This increase is due mainly to an increased work in progress assets driven primarily by the generation expansion.

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 Second Quarter 2016 totalled \$0.2 million, a \$0.1 million decrease when compared to \$0.3 million in the Second Quarter 2015. Foreign exchange gains for the six months ended June 30, 2016 totalled \$0.5 million, a \$0.1 million decrease when compared to \$0.6 million for the six months ended June 30, 2015.

Other income is comprised of income from the third party customers of DataLink, income from pipeline operations, sale of meter sockets, sale of recyclable materials, performance rewards as part of the T&D Licence and other miscellaneous income. Performance standards as prescribed by the T&D Licence provide a balanced framework of potential penalties or rewards compared to historical performance in the areas of planning, reliability, operating and overall performance. Standards include “zones of acceptability” where no penalties or rewards would apply.

Other income totalled \$1.4 million for the Second Quarter 2016, a \$0.4 million increase when compared to other income of \$1.0 million for the Second Quarter 2015. Other income totalled \$2.1 million for the six months ended June 30, 2016, a \$0.3 million increase when compared to other income of \$1.8 million for the six months ended June 30, 2015. This increase is due to an increase in the revenue recorded by Datalink in Second Quarter 2016 in the amount of \$0.7 million compared to \$0.3 million for the Second Quarter 2015.



## The Economy

In May 2016, the Cayman Islands Government released the first quarter 2016 Consumer Price Index (“CPI”) Report. The average CPI for March 2016 decreased 2.8% from the average CPI in March 2015. In comparison to the quarter ending December 2015, CPI declined by 0.8%. Of the 12 divisions monitored in the CPI calculation, five divisions saw price declines in the first quarter of 2016 compared to the quarter ending December 2015: Housing & Utilities, Transport, Restaurant & Hotels, Clothing & Footwear and Household Equipment. The divisions with the largest increases were Miscellaneous Good & Services, Food & Non-alcoholic Beverages.

According to the 2015 Annual Economic Report from the Cayman Islands Economics and Statistics office (“ESO”) that was released in July 2016, overall economic activity in the Cayman Islands grew by an estimated 2.0% in 2015 compared to 2014. According to the report, construction led the growth, and growth rates were indicated for a number of other sectors including other services, real estate, renting and business activities, government services, utilities, wholesale and retail and financing and insurance. The ESO is forecasting Annual GDP growth of 2.1% for 2016. The Company’s annual sales growth and resource requirements, including number of employees, have historically been heavily influenced by changes in the level of economic activity in the country as illustrated by the GDP.

Financial services is one of the two main industries of the Cayman Islands. The table below itemises trends in some of the key financial areas:

	As at June 30, 2016	As at December 2015	As at December 2014	As at December 2013	As at December 2012
Bank Licences	176	184	198	213	222
Mutual Funds	11,019	10,940	11,010	11,379	10,841
Mutual Fund Administrators	108	108	115	121	124
Registered Companies	101,430	98,838	99,459	95,530	93,612
Captive insurance companies	738	739	793	788	768

The tourism sector is the second main pillar of the Cayman Islands economy. The Cayman Islands tourism demographic is largely comprised of visitors from the United States of America (“US”). For 2015 76% of air arrivals to the country were citizens of the US. As such the US economy has a large impact on the economy of the Cayman Islands.

Second Quarter 2016 air arrivals were down by 0.1% when compared to 2015 and cruise arrivals saw a decrease of 0.4% when compared to the same period in 2015. Air arrivals have a direct impact on the Company’s sales growth as these visitors are stay-over visitors who occupy local accommodation services. Cruise arrivals have an indirect impact as they affect the opening hours of the establishments operating for that market.

The tourism industry is expected to be positively impacted by the expansion of the Owen Roberts International Airport in Grand Cayman. The expansion is expected to be completed in 2018 and will accommodate the anticipated growth in air arrivals. The expanded airport is expected to provide vital access for long-haul flights and will also provide a vastly improved airlift service for Grand Cayman’s tourists. In addition to the airport expansion, the tourism sector is expected to receive a boost by the completion of the Kimpton Seafire

Resort and Spa. The luxury resort hotel will be completed in November 2016, and will host five restaurants and six beach front bungalows in addition to the 10 storey, 265 room ocean front complex. Both projects are expected to create additional employment opportunities and increase stay over tourism.

The following table presents statistics for tourist arrivals in the Cayman Islands for the three months ending June 30:

Arrivals	2016	2015	2014	2013	2012
By Air	97,712	97,855	101,085	88,382	84,921
By Sea	<u>363,219</u>	<u>364,808</u>	<u>318,500</u>	<u>260,713</u>	<u>325,843</u>
Total	460,931	462,663	419,585	349,095	410,764

All data is sourced from the Cayman Islands Government, Cayman Islands Economics & Statistics Office, Cayman Islands Monetary Authority, Cayman Financial Review, Cayman Islands Department of Tourism and Health City websites; [www.gov.ky](http://www.gov.ky) [www.ESO.ky](http://www.ESO.ky) [www.cimoney.com.ky](http://www.cimoney.com.ky) [www.caymanfinancialreview.com](http://www.caymanfinancialreview.com) [www.caymanislands.ky](http://www.caymanislands.ky) [www.healthcitycaymanislands.com](http://www.healthcitycaymanislands.com).

## Liquidity

The following table outlines the summary of the Company's cash flows:

Cash Flows (\$ thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015	Change	% Change
Beginning cash	3,147	25,164	1,365	21,815	(20,450)	-94%
Cash provided by/(used in):						
Operating activities	10,053	8,768	29,809	24,165	5,644	23%
Investing activities	(15,477)	(14,063)	(28,486)	(21,284)	(7,202)	-34%
Financing activities	<u>11,622</u>	<u>15,259</u>	<u>6,657</u>	<u>10,432</u>	<u>(3,775)</u>	-36%
Ending cash	9,345	35,128	9,345	35,128	(25,783)	-73%

### Operating Activities:

Cash flow provided by operations, after working capital adjustments, for the Second Quarter 2016, was \$10.1 million, a \$1.3 million increase when compared to \$8.8 million for the Second Quarter 2015. This increase is primarily attributable to higher earnings and the movement in regulatory deferrals in the Second Quarter 2016 when compared to the same period last year.

Cash flow provided by operations, after working capital adjustments, for the six months ended June 30, 2016, was \$29.8 million, a \$5.6 million increase when compared to \$24.2 million for the six months ended June 30, 2015. This increase is primarily attributable to higher earnings and the movement in non-cash working capital balances for the six month period ending June 30, 2016 when compared to the same period last year.

*Investing Activities:*

Cash used in investing activities for the Second Quarter 2016 totalled \$15.5 million, an increase of \$1.4 million from \$14.1 million for the Second Quarter 2015. This increase is due mainly to higher expenditures related to property, plant and equipment for the Second Quarter 2016 when compared to the Second Quarter 2015.

Cash used in investing activities for the six months ended June 30, 2016 totalled \$28.5 million, an increase of \$7.2 million from \$21.3 million for the Second Quarter 2015. This increase is due mainly to higher expenditures related to property, plant and equipment for the Second Quarter 2016.

*Financing Activities:*

Cash provided by financing activities for the Second Quarter 2016 totalled \$11.6 million, a decrease of \$3.7 million compared to cash provided by financing activities of \$15.3 million for the Second Quarter 2015. This decrease in cash provided by financing activities is attributable to proceeds from the issuance of Class A Ordinary Shares under the 2015 Rights Offering, and repayment of the bank overdraft in the Second Quarter 2016, partially offset by proceeds from debt financing in the Second Quarter 2016.

Cash provided by financing activities for the six months ended June 30, 2016 totalled \$6.7 million, a decrease of \$3.7 million compared to cash provided by financing activities of \$10.4 million for the six months ended June 30, 2015. This decrease in cash provided by financing activities is attributable to proceeds from the issuance of Class A Ordinary Shares under the 2015 Rights Offering, partially offset by proceeds from debt financing, repayment of the bank overdraft and higher dividend payments in 2016.

*Cash Flow Requirements:*

The Company expects that operating expenses and interest costs will generally be paid from the Company's operating cash flows, with residual cash flows available for capital expenditures and dividend payments. Borrowings under credit facilities may be required from time to time to support seasonal working capital requirements. Cash flows required to complete planned capital expenditures are expected to be financed from a combination of proceeds from operating cash, debt and equity transactions. The Company expects to be able to source the cash required to fund its 2016 capital expenditure programme (see the "Business Risks" section of this MD&A for Liquidity Risk details).

**Transactions with Related Parties**

Miscellaneous receivables were nil at June 30, 2016 (\$300 as at December 31, 2015). Miscellaneous payables to Fortis Turks & Caicos, a subsidiary of Fortis Inc., were nil at June 30, 2016 (\$11,017 as at December 31, 2015 for travel expenses). Miscellaneous payables to Fortis Inc., the Company's majority shareholder, totaling nil were outstanding at June 30, 2016 (\$3,300 as at December 31, 2015 for labor, hurricane preparedness and travel expenses).

## Contractual Obligations

The contractual obligations of the Company over the next five years and periods thereafter, as at June 30, 2016, are outlined in the following table:

<i>(\$ millions)</i>	Total	< 1 year	1 to 3 years	4 to 5 years	> 5 years
Total debt	227.0	11.0	29.4	32.0	154.6
Long-term debt interest	93.9	11.3	20.3	16.7	45.6
MAN/BWSC Generation Expansion Contract	1.1	1.1	-	-	-
Defined benefit pension	<u>0.2</u>	<u>0.2</u>	-	-	-
<b>Total</b>	<b>322.2</b>	<b>23.6</b>	<b>49.7</b>	<b>48.7</b>	<b>200.2</b>

1. Relates to principal payments on long-term debt only.
2. In December 2014, the Company entered into design-build contracts with BWSC and MAN. The contract is valued at approximately \$55 million. A down payment of \$11.1 million was made in 2014 and a progress payment of \$5.5 million was made in the Second Quarter 2015.
3. The defined benefit pension funding contribution is based on an estimate provided under the latest completed actuarial valuation.

### *Power Purchase Obligation*

During 2015, the Company entered into a Power Purchase Agreement (“PPA”) with Entropy Cayman Solar Limited to purchase up to 2.1 MW per year of associated energy for a 25-year term. This 5 MW solar project, scheduled for completion by the end of 2016, is expected to generate energy by December 2016 and will significantly reduce emissions into the atmosphere through the avoidance of diesel fuel consumption. The PPA will also provide renewable energy at a competitive initial price of \$0.17 cents per kWh. The PPA was approved by the ERA during the Fourth Quarter 2015. The PPA qualifies for the Normal Purchase Normal Sale exemption under ASC 815 and does not qualify as a derivative.

### *Fuel Purchase Obligation*

The Company has a primary fuel supply contract with RUBiS Cayman Islands Limited (“RUBiS”). Under the agreement the Company is committed to purchase approximately 60% of its diesel fuel requirements for its generating plant from RUBiS. The Company also has a secondary fuel supply contract with Sol Petroleum Cayman Limited (“Sol”) and is committed to purchase approximately 40% of the Company’s fuel requirements for its generating plant from Sol. Contracts with RUBiS and Sol were executed in September 2012. Both contracts expired on July 31, 2014 with the option to renew for two additional 18 month terms. The Company executed 18 month fuel supply contracts in September 2014 upon the expiration of its previous fuel supply contract with both RUBiS and Sol. The Company is currently negotiating the renewal terms with RUBiS for the final 18 month contract. The contract with Sol was renewed for a final 18 month term on March 1, 2016. The approximate remaining quantities per the fuel contract on an annual basis are, by fiscal year in millions of IGs: 2016 – 7.0 and 2017 – 8.9. Both contracts qualify for the Normal Purchase Normal Sale exemption under ASC 815 and do not qualify as derivatives.

## Financial Position

The following table is a summary of significant changes to the Company's balance sheet from December 31, 2015 to June 30, 2016:

Significant changes in Balance Sheets between December 31, 2015 and June 30, 2016 (\$ millions)	Increase/ (Decrease)	Explanation
Cash and Cash Equivalents	8.0	Increase due to cash provided by operating activities of \$29.7 million, and cash provided by financing activities of \$6.7 million partially offset by cash used in investing activities of \$28.4 million.
Accounts Receivable	2.3	Increase due to higher electricity sales in the Second Quarter 2016.
Regulatory Assets	(1.6)	Change attributable to a decrease in fuel costs.
Prepayments	(0.8)	Decrease due to timing of expense recognition.
Property, Plant and Equipment	15.3	Net increase is comprised of capital expenditures of (1) \$26.1 million (2) depreciation expense of \$13.6 million (3) \$2.8 million in accrued capital expenditure.
Accounts Payable and Accrued Expenses	1.0	Change mainly attributable to increases in capital expenditure accruals, partially offset by a decrease in fuel costs.
Short Term Debt	30.0	Increase due to drawdown of Scotiabank capital expenditure credit facility in May 2016.
Current Portion of Long Term Debt	(3.0)	Decrease due to full repayment of Company's 6.67% Unsecured Note Loan in June 2016.
Long-Term Debt	(7.9)	Decrease due to principal payments made on the Company's Senior Unsecured Notes in the Second Quarter 2016.
Share Premium	1.4	The Company issued 135,365 shares through its share purchase plans.

## 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 Class A Ordinary Share rights offering that occurred in 2015 and 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 60% of the Company's consolidated capital structure, as defined by short-term and long-term debt agreements. As at June 30, 2016, the Company was in compliance with all debt covenants.

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

Capital Structure	June 30, 2016 (\$ millions)	%	December 31, 2015 (\$ millions)	%
Total debt	257.0	54	238.0	53
Shareholder's equity	<u>217.4</u>	<u>46</u>	<u>214.4</u>	<u>47</u>
<b>Total</b>	<b>474.4</b>	<b>100</b>	<b>452.4</b>	<b>100</b>

The change in the Company's capital structure between December 31, 2015 and June 30, 2016 was driven by an increase in equity resulting from the issuance of Class A Ordinary Shares under its share purchase plans and an increase in Short-Term Debt.

The Company's credit ratings under Standard & Poors ("S&P") and the Dominion Bond Rating System ("DBRS") are as follows:

S&P A-/Negative  
DBRS 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.

Following the February 9, 2016 announcement from Fortis Inc. of the proposed \$11.3 billion acquisition of ITC Holdings Corporation, a Michigan based Company that operates electricity transmission facilities in the United States, S&P affirmed the Company's A- rating and revised its outlook on the Company from stable to negative. The negative outlook on CUC reflects the application of S&P's group rating methodology and an expectation of the execution risks associated with the transaction including selling up to 19.9% of ITC to one or more infrastructure-focused minority investors. The A- rating reflects S&P's positive view of the Company's current position as the sole provider of generation services, and the Company's licenced position as the sole provider of T&D services. The rating also reflects S&P's positive view of regulatory support and stable cash flows offset by the economic uncertainty and the limited history of the regulator.

In June 2016, S&P affirmed the Company's "A" with a negative outlook.

In March 2016, 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 the demand for electricity. Impacting the rating were such factors as hurricane event risk and the small size of the Company's customer base.

## Credit Facilities

The Company currently has \$50.0 million of unsecured credit financing facilities with the Scotiabank & Trust (Cayman) Limited ("Scotia") and Royal Bank of Canada ("RBC"). The financing facilities are comprised of:

Credit Facilities	(\$ millions)
<b>Provided by Scotia:</b>	
Letters of Credit	\$1.0
Operating, Revolving Line of Credit	\$10.0
Catastrophe Standby Loan	\$7.5
Demand Loan Facility- Interim Funding of Capital Expenditures	\$31.0
<b>Total</b>	<b>\$49.5</b>
<b>Provided by RBC:</b>	
Corporate Credit Card Line	\$0.5
<b>Total</b>	<b>\$0.5</b>

Of the total above, \$19.0 million was available at June 30, 2016.

## Capital Expenditures

Capital expenditures for the three months ended June 30, 2016 were \$15.5 million, a \$1.5 million, or 10% increase from \$14.0 million in capital expenditures for the three months ended June 30, 2015.

Capital expenditures for the six months ended June 30, 2016 were \$26.1 million, a \$5.0 million, or 20% increase from \$21.1 million in capital expenditures for the six months ended June 30, 2015.

The capital expenditures for the six months ended June 30, 2016 primarily relate to:

- Distribution system extension and upgrades - \$4.0 million
- Generation Replacement Cost – \$5.2 million
- 39.7 MW Generation Project - \$11.7 million
- Facility Asset Replacement & Upgrades Structural & Mechanical- \$0.6 million
- AFUDC of \$3.6 million was capitalized in the six months ended June 30, 2016

Capital expenditures (\$ Millions)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six months Ended June 30, 2016	Six months Ended June 30, 2015
Transmission	0.4	0.1	0.8	0.2
Distribution	4.8	3.2	8.2	5.8
Generation	10.0	10.2	16.1	14.1
Other	0.3	0.5	1.0	1.0
<b>Total</b>	<b>15.5</b>	<b>14.0</b>	<b>26.1</b>	<b>21.1</b>

## **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 June 30, 2016.

## **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 things. 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 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 programmes 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 programme that provides coverage for business interruption, liability and property damage, although the coverage offered by this programme is limited (see the "Insurance" section 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 the "Regulation" section 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 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 by the ERA.

### *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 appropriate 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, noise, land use activities, and the handling, storage, processing, use, and disposal of materials and waste products.

CUC's Environmental Management System ("EMS") is registered to the ISO 14001 Environmental Standard. The Company was initially registered in 2004, pursuant to an audit by a third party of the Company's EMS to ensure that the Company was meeting requirements put in place by the Government as well as self-imposed requirements. Under the ISO 14001 standard companies are required to establish, document, implement, maintain and continually improve their environmental performance with an aim of prevention of pollution. In order to maintain the Company's registration to this standard an external surveillance audit is conducted annually, and an external audit is conducted every three years for re-certification. Internal audits of the system must also be conducted on an annual basis. CUC has most recently conducted, and passed its re-certification audit in March 2016.

In May 2002, the United Kingdom ("UK") ratified the Kyoto Protocol, which sets targets and timetables for the reduction of greenhouse gas (GHG) emissions, which was later extended to the Cayman Islands in March 2007. Under the Kyoto Protocol, the UK is legally bound to reduce its GHG emissions, but Cayman has no emissions reduction target. 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 to quantify as best as possible the country's fuel consumption across a variety of sectors, production processes and distribution means. CUC continues to supply the Department of Environment with data for Cayman's GHG inventory.

Through the EMS, CUC has determined that its exposure to environmental risks is not significant and does not have an impact on CUC's 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, 2016 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 its 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, which provides a specified monthly benefit on retirement irrespective of individual investment returns. The assumed long-term rate of return on pension plan assets for the purposes of estimating pension expense for 2016 is 5%. This compares to assumed long-term rates of return of 5% used during 2015. There is no assurance that the pension plan assets will be able to earn the assumed rate of returns. The loss on pension plan assets during 2015 was 2% (2014: gain of 3%).

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 2016 is 4.5% compared to the discount rate assumed during 2015 of 4.0%.

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.

### *Financial Instruments*

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. Financial instruments of the Company consist mainly of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, consumers' deposits and advances for construction and long-term debt.

### *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 a 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 the Company 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. The Company 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 under 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. The Company has also secured committed credit facilities to support short-term financing of capital expenditures and seasonal working capital requirements. The cost of renewed and extended credit facilities

could increase in the future; however, any increase in interest expense and fees is not expected to materially impact the Company's consolidated financial results in 2016.

#### *Interest Rate Risk*

Long-term debt is issued at fixed interest rates, thereby minimizing 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 nil.

### **FUTURE ACCOUNTING POLICIES**

#### *Revenue from Contracts with Customers*

ASU No. 2014-09 was issued in May 2014 and the amendments in this update create ASC Topic 606, Revenue from Contracts with Customers, and supersede the revenue recognition requirements in ASC Topic 605, Revenue Recognition, including most industry specific revenue recognition guidance throughout the codification. This standard completes a joint effort by FASB and the International Accounting Standards Board to improve financial reporting by creating common revenue recognition guidance for US GAAP and International Financial Reporting Standards that clarifies the principles for recognizing revenue and that can be applied consistently across various transactions, industries and capital markets. This standard was originally effective for annual and interim periods beginning after December 15, 2016 and is to be applied on a full retrospective or modified retrospective basis. ASU No. 2015-14 was issued in August 2015 and the amendments in this update defer the effective date of ASU No. 2014-09 by one year to annual and interim periods beginning after December 15, 2017. Early adoption is permitted as of the original effective date. The majority of the Company's revenue is generated from energy sales to customers based on published tariff rates, as approved by the respective regulators, and is considered to be in the scope of ASU No. 2014-09. The Company and its subsidiary, Datalink Ltd., are assessing the impact that the adoption of this standard will have on the consolidated financial statements and plans to have this assessment complete in 2016.

#### *Recognition and Measurement of Financial Assets and Financial Liabilities*

ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, was issued in January 2016 and the amendments in this update address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. Most notably, the amendments require the following: (i) equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) to be measured at fair value through earnings; however, entities will be able to elect to record equity investments without readily determinable fair values at cost, less impairment, and plus or minus subsequent adjustments for observable price changes; and (ii) financial assets and financial liabilities to be presented separately in the notes to the consolidated financial statements, grouped by measurement category and form of financial asset. This update is effective for annual and interim periods beginning after December 15, 2017.

### *Leases*

ASU No. 2016-02 was issued in February 2016 and the amendments in this update create ASC Topic 842, Leases, and supersede lease requirements in ASC Topic 840, Leases. The main provision of Topic 842 is the recognition of lease assets and lease liabilities on the balance sheet by lessees for those leases that were previously classified as operating leases. For operating leases, a lessee is required to do the following: (i) recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, on the balance sheet; (ii) recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term on a generally straight-line basis; and (iii) classify all cash payments within operating activities in the statement of cash flows. These amendments also require qualitative disclosures along with specific quantitative disclosures. This update is effective for annual and interim periods beginning after December 15, 2018 and is to be applied using a modified retrospective approach with practical expedients options. Early adoption is permitted. The Company is assessing the impact that the adoption of this update will have on its consolidated financial statements and related disclosures.

### *Improvements to Employee Share-Based Payment Accounting*

ASU No. 2016-09, Improvements to Employee Share-Based Payment Accounting, was issued in March 2016 as part of FASB's simplification initiative. The areas for simplification in this update involve several aspects of accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This update is effective for annual and interim periods beginning after December 15, 2016. Early adoption is permitted, however, an entity that elects early adoption must adopt all the amendments in the same period. The Company is assessing the impact that the adoption of this update will have on its consolidated financial statements.

### **Changes in Accounting Policies**

#### *Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved After the Requisite Service Period*

Effective January 1, 2015, the Company early adopted ASU No. 2014-12 that resolves diversity in practice for employee share-based payments with performance targets that can entitle an employee to benefit from an award regardless of if they are rendering services at the date the performance target is achieved. The adoption of this update did not have an impact on the Company's consolidated financial statements.

#### *Simplifying the Presentation of Debt Issuance Costs*

Effective December 1, 2015, the Company early adopted ASU No. 2015-03 that requires debt issuance costs to be presented on the consolidated balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The Company early adopted ASU No. 2015-15 that clarifies the presentation and subsequent measurement of debt issuance costs associated with line-of-credit arrangements. The update permits an entity to defer and present debt issuance costs as an asset and subsequently amortize the deferred debt issuance costs ratably over the term of the line-of-

credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The adoption of this update was applied retrospectively and did not have a material impact on the Company's consolidated financial statements.

### **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 June 30, 2016, the amount of unbilled revenue recorded in Electricity Sales was \$2.7 million (June 30, 2015: \$2.7 million).

#### *Kilowatt Hour ("kWh") Sales*

KWh 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 June 30, 2016, the amount of estimated kWh sales was 21.2 million kWh (June 30, 2015: 21.3 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 June 30, 2016, the Company has a long term liability of \$1.3 million (December 31, 2015: \$1.2 million).

### *Property, Plant and Equipment Depreciation*

Depreciation 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 June 30, 2016, the net book value of the Company's PP&E was \$463.2 million compared to \$447.7 million as at December 31, 2015, increasing as a result of the Company's generation and T&D capital expenditures. Depreciation expense for the Second Quarter 2016 was \$6.8 million (\$6.6 million for the Second Quarter 2015). Due to the value of the Company's property, plant and equipment, 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 September 30, 2014 through June 30, 2016. 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.

<b>Quarterly results (\$ thousands, except basic and diluted earnings per ordinary share)</b>	<b>Operating Revenue</b>	<b>Net earnings</b>	<b>Income applicable to ordinary shares</b>	<b>Earnings per ordinary share</b>	<b>Diluted earnings per ordinary share</b>
June 30, 2016	37,915	7,544	7,431	0.23	0.23
March 31, 2016	39,732	4,975	4,862	0.15	0.15
December 31, 2015	45,882	6,151	5,560	0.18	0.18
September 30, 2015	50,242	7,893	7,780	0.25	0.25
June 30, 2015	44,048	5,514	5,401	0.17	0.17
March 31, 2015	48,709	3,284	3,171	0.11	0.11
December 31, 2014	58,192	5,397	4,806	0.16	0.16
September 30, 2014	63,437	6,221	6,108	0.21	0.21

#### *June 2016/June 2015*

Operating income for Second Quarter 2016 totalled \$7.2 million, an increase of \$0.8 million when compared to operating income of \$6.4 million for Second Quarter 2015. The increase is primarily attributable to the 7% increase in kWh sales partially offset by higher depreciation and general and administration costs.

In addition to the factors positively impacting operating income, net earnings increased as a result of higher capitalization of interest expenses through the Allowance for Funds Used During Construction ("AFUDC") of \$1.7 million in Second Quarter 2016 when compared to \$1.0 million in Second Quarter 2015. The increase in AFUDC, and resulting reduction in Finance Charges, is due primarily to the Company's 39.7 MW Generation Project which was completed in June 2016. AFUDC is the capitalisation of Financing Cost which is calculated by multiplying the Company's Cost of Capital rate by the average construction work in progress for each month.

The Company anticipates a reduction in AFUDC and an increase in depreciation costs commencing with the completion of the Generation Project.

Net earnings for the three months ended June 30, 2016 totalled \$7.5 million, an increase of \$2.0 million when compared to net earnings of \$5.5 million for the three months ended June 30, 2015 ("Second Quarter 2015").

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Second Quarter 2016 were \$7.4 million, or \$0.23 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$5.4 million or \$0.17 per Class A Ordinary Share for Second Quarter 2015.

#### *March 2016/March 2015*

Operating income for First Quarter 2016 totalled \$5.1 million, an increase of \$0.6 million when compared to operating income of \$4.5 million for First Quarter 2015. The increase is attributable to the 5% increase in kWh sales and lower general and administration costs. These items were partially offset by higher depreciation, maintenance and amortization costs.

In addition to the factors positively impacting Operating income, net earnings increased as a result of higher capitalization of interest expenses through the Allowance for Funds Used During Construction ("AFUDC") of \$1.9 million in First Quarter 2016 when compared to \$0.9 million in First Quarter 2015. The increase in AFUDC, and resulting reduction in Finance Charges, is due primarily to the Company's ongoing 39.7 MW Generation Project. AFUDC is the capitalisation of Financing Cost which is calculated by multiplying the Company's Cost of Capital rate by the average work in progress for each month.

Net Earnings for the First Quarter 2016 totalled \$5.0 million, an increase of \$1.7 million when compared to net earnings of \$3.3 million for the First Quarter 2015.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the First Quarter 2016 were \$4.9 million, or \$0.15 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$3.2 million or \$0.11 per Class A Ordinary Share for the First Quarter 2015.

#### *December 2015/December 2014*

Operating income for the three months ended December 31, 2015 ("Fourth Quarter 2015") totalled \$6.0 million, a decrease of \$0.3 million when compared to operating income of \$6.3 million for the three months ended December 31, 2014 ("Fourth Quarter 2014"). The decrease was due primarily to higher depreciation, consumer services, general and administration, and maintenance costs. These items were partially offset by an 8% increase in kWh sales

Net earnings for Fourth Quarter 2015 were \$6.2 million, a \$0.8 million increase when compared to \$5.4 million for Fourth Quarter 2014.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Fourth Quarter 2015 were \$5.6 million, or \$0.18 per Class A



Ordinary Share, as compared to \$4.8 million, or \$0.16 per Class A Ordinary Share for the Fourth Quarter 2014.

#### *September 2015/September 2014*

Operating income for the three months ended September 30, 2015 (“Third Quarter 2015”) totalled \$8.4 million, an increase of \$1.3 million when compared to operating income of \$7.1 million for the three months ended September 30, 2014 (“Third Quarter 2014”). This increase was due mainly to higher electricity sales revenues, and lower consumer services and transmission and distribution costs. These items were partially offset by higher depreciation and maintenance costs.

Net earnings for Third Quarter 2015 totalled \$7.9 million, an increase of \$1.7 million when compared to net earnings of \$6.2 million for Third Quarter 2014.

After the adjustment for dividends on the preference shares of the Company, earnings on Class A Ordinary Shares for the Third Quarter 2015 were \$7.8 million, or \$0.25 per Class A Ordinary Share, compared to earnings on Class A Ordinary Shares of \$6.1 million or \$0.21 per Class A Ordinary Share for the Third Quarter 2014.

#### **Disclosure Controls and Procedures**

The President and Chief Executive Officer (“CEO”) and the VP Finance and Chief Financial Officer (“CFO”), together with Management, have established and maintained the Company’s disclosure controls and procedures (DC&P), to provide reasonable assurance that material information relating to the Company is made known to them by others, particularly during the year ending December 31, 2015; 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. Based on the evaluation performed over disclosure controls and procedures, it was concluded that the DC&P of CUC is adequately designed and operating effectively as of June 30, 2016.

#### **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). Based on the assessment, it was concluded that CUC’s internal controls over financial reporting are adequately designed and operating effectively as of June 30, 2016.

## Outlook

The 39.7 MW generation project was successfully completed and the units were commissioned in May and June 2016. The project was estimated at \$85 million and the actual costs amounted to \$79.0 million.

In December 2015 the ERA approved CUC's 2016-2020 Capital Investment Plan in the amount of \$204 million. Approved projects for the upcoming period include completion of the generation project and ongoing generation and T&D system replacements and upgrades.

The Company continues to facilitate the connecting of renewable energy sources to the grid. During the Fourth Quarter 2015, the ERA approved a Power Purchase Agreement (PPA) for a 5 MW plant to be built by Entropy Cayman Solar Limited in the district of Bodden Town.

This 5 MW Solar project, scheduled for completion by the end of 2016, will provide energy to power approximately 800 homes with clean renewable solar energy and will significantly reduce emissions into the atmosphere through the avoidance of diesel fuel consumption.

## Outstanding Share Data

At July 29, 2016 the Company had issued and outstanding 32,516,996 Ordinary Shares and 250,000 9% cumulative Participating Class B Preference Shares.

The number of common shares of the Company that would be issued if all outstanding stock options were converted as at July 29, 2016 is as follows.

Conversion of Securities into Common Shares As at July 29, 2016 (Unaudited)	Number of Common Shares
Stock Options	237,120

Additional information, including CUC's Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com) and on the Company's website at [www.cuc-cayman.com](http://www.cuc-cayman.com).

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

Unaudited	Note	As at June 30, 2016	As at December 31, 2015
<b>Assets</b>			
<i>Current Assets</i>			
Cash and Cash Equivalents		9,345	1,365
Accounts Receivable	5	14,021	11,767
Regulatory Assets	6	12,689	14,346
Inventories	7	2,253	2,237
Prepayments		<u>1,347</u>	<u>2,096</u>
		39,655	31,811
Property, Plant and Equipment	8	463,037	447,700
Other Assets	9	24	24
Intangible Assets	10	<u>3,180</u>	<u>3,271</u>
		<u>505,896</u>	<u>482,806</u>
<b>Total Assets</b>			
<b>Liabilities and Shareholders' Equity</b>			
<i>Current Liabilities</i>			
Bank Overdraft		-	1,735
Accounts Payable and Accrued Expenses	11	21,430	20,410
Related Party Payables	22	-	14
Regulatory Liabilities	6	2,367	863
Short-Term Debt	12	30,000	-
Current Portion of Long-Term Debt		11,000	14,000
Consumers' Deposits and Advances for Construction		<u>7,344</u>	<u>6,823</u>
		72,141	43,845
Defined Benefit Pension Liability	18	1,252	1,242
Long-Term Debt	15	214,679	222,594
Other Long Term Liabilities	13	<u>394</u>	<u>636</u>
<b>Total Liabilities</b>		288,466	268,317
<b>Shareholders' Equity</b>			
Share Capital		2,186	2,177
Share Premium		117,630	116,201
Additional Paid in Capital	13	467	467
Retained Earnings		98,213	96,822
Accumulated Other Comprehensive Loss		<u>(1,066)</u>	<u>(1,178)</u>
<b>Total Shareholders' Equity</b>		217,430	214,489
<b>Total Liabilities and Shareholders' Equity</b>		<u>505,896</u>	<u>482,806</u>

*See accompanying Notes to Unaudited Interim Consolidated Financial Statements*

**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 June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
<b>Operating Revenues</b>					
Electricity Sales		20,592	19,182	38,609	36,226
Fuel Factor		<u>17,323</u>	<u>24,866</u>	<u>39,039</u>	<u>56,530</u>
<i>Total Operating Revenues</i>		<b>37,915</b>	<b>44,048</b>	<b>77,648</b>	<b>92,756</b>
<b>Operating Expenses</b>					
Power Generation		18,324	25,918	41,087	58,514
General and Administration		2,373	2,068	4,460	4,510
Consumer Services		722	760	1,352	1,401
Transmission and Distribution		864	707	1,621	1,433
Depreciation		6,830	6,578	13,598	12,888
Maintenance		1,440	1,511	2,921	2,887
Amortization of Intangible Assets		<u>151</u>	<u>123</u>	<u>302</u>	<u>246</u>
<i>Total Operating Expenses</i>		<b>30,704</b>	<b>37,665</b>	<b>65,341</b>	<b>81,879</b>
<b>Operating Income</b>		<b>7,211</b>	<b>6,383</b>	<b>12,307</b>	<b>10,877</b>
<b>Other Income /(Expenses):</b>					
Finance Charges	17	(1,319)	(2,148)	(2,461)	(4,504)
Foreign Exchange Gain	19	240	302	546	642
Other Income		<u>1,412</u>	<u>977</u>	<u>2,083</u>	<u>1,780</u>
<i>Total Net Other (Expenses)/Income</i>		333	(869)	168	(2,082)
<b>Earnings for the Period</b>		<b>7,544</b>	<b>5,514</b>	<b>12,475</b>	<b>8,795</b>
<i>Preference Dividends Paid- Class B</i>		<u>(113)</u>	<u>(113)</u>	<u>(225)</u>	<u>(226)</u>
<i>Earnings on Class A Ordinary Shares</i>		<b>7,431</b>	<b>5,401</b>	<b>12,250</b>	<b>8,569</b>
Weighted-Average Number of Class A Ordinary Shares Issued and Fully Paid (in thousands)	14	32,431	30,284	32,462	31,030
<i>Earnings per Class A Ordinary Share</i>	14	0.23	0.17	0.38	0.28
Diluted Earnings per Class A Ordinary Share	14	0.23	0.17	0.38	0.28
Dividends Declared per Class A Ordinary Share		0.170	0.165	0.335	0.330

*See accompanying Notes to Unaudited Interim Consolidated Financial Statements*

**Consolidated Statements of Comprehensive Income**  
*(expressed in thousands of United States Dollars)*

Unaudited	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
<b>Earnings for the Period</b>	<b>7,544</b>	<b>5,514</b>	<b>12,475</b>	<b>8,795</b>
Defined Benefit Pension plans:				
Amortization of net actuarial loss	<u>56</u>	<u>52</u>	<u>112</u>	<u>103</u>
Total Other Comprehensive Income	56	52	112	103
<b>Comprehensive Income</b>	<b>7,600</b>	<b>5,566</b>	<b>12,587</b>	<b>8,898</b>

*See accompanying Notes to Unaudited Interim Consolidated Financial Statements*

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

Unaudited	Class A Ordinary Shares (in thousands )	Class A Ordinary Shares Value (\$)	Preferenc e Shares (\$)	Share Premium (\$)	Additional Paid-in Capital (\$)	Accumulat ed Other Comprehe nsive Loss (\$)	Retained Earnings (\$)	Total Equity (\$)
<b>As at January 1, 2016</b>	<b>32,382</b>	<b>1,927</b>	<b>250</b>	<b>116,201</b>	<b>467</b>	<b>(1,178)</b>	<b>96,822</b>	<b>214,489</b>
Net earnings	-	-	-	-	-	-	12,475	12,475
Common share issuance and stock options plans	135	9	-	1,429	-	-	-	1,438
Defined benefit plans	-	-	-	-	-	112	-	112
Dividends on common shares	-	-	-	-	-	-	(10,859)	(10,859)
Dividends on preference shares	-	-	-	-	-	-	(225)	(225)
<b>As at June 30, 2016</b>	<b>32,517</b>	<b>1,936</b>	<b>250</b>	<b>117,630</b>	<b>467</b>	<b>(1,066)</b>	<b>98,213</b>	<b>217,430</b>
<b>As at January 1, 2015</b>	<b>29,260</b>	<b>1,742</b>	<b>250</b>	<b>83,044</b>	<b>463</b>	<b>(1,386)</b>	<b>95,722</b>	<b>179,835</b>
Net earnings	-	-	-	-	-	-	8,795	8,795
Common share issuance and stock options plans	3,029	180	-	32,197	2	-	-	32,379
Defined benefit plans	-	-	-	-	-	103	-	103
Dividends on common shares	-	-	-	-	-	-	(10,146)	(10,146)
Dividends on preference shares	-	-	-	-	-	-	(226)	(226)
<b>As at June 30, 2015</b>	<b>32,289</b>	<b>1,922</b>	<b>250</b>	<b>115,241</b>	<b>465</b>	<b>(1,283)</b>	<b>94,145</b>	<b>210,740</b>

*See accompanying Notes to Unaudited Interim Consolidated Financial Statements*

**Consolidated Statements of Cash Flows**  
(expressed in thousands of United States Dollars)

Unaudited	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
<i>Operating Activities</i>				
Earnings for the period	7,544	5,514	12,475	8,795
Items not affecting cash:				
Depreciation	6,830	6,578	13,598	12,888
Amortization of Intangible Assets	151	123	302	246
Non-cash Pension Expenses	61	-	122	-
Amortization of Deferred Financing Costs	40	40	80	79
Stock-based compensation	-	<u>1</u>	<u>1</u>	<u>2</u>
	<b>14,626</b>	<b>12,256</b>	<b>26,578</b>	<b>22,010</b>
Net change in non-cash working capital balances related to operations	(4,457)	(1,896)	70	(1,003)
Net Change in Regulatory Deferrals	<u>(116)</u>	<u>(1,592)</u>	<u>3,161</u>	<u>3,158</u>
<i>Cash flow related to operating activities</i>	<b>10,053</b>	<b>8,768</b>	<b>29,809</b>	<b>24,165</b>
<i>Investing Activities</i>				
Purchase of property, plant and equipment	(15,355)	(13,967)	(28,304)	(21,074)
Costs related to intangible assets	<u>(122)</u>	<u>(96)</u>	<u>(182)</u>	<u>(210)</u>
<i>Cash flow related to investing activities</i>	<b>(15,477)</b>	<b>(14,063)</b>	<b>(28,486)</b>	<b>(21,284)</b>
<i>Financing Activities</i>				
Short-term borrowings	30,000	-	30,000	-
Repayment of debt	(11,000)	(11,000)	(11,000)	(11,000)
Decrease in bank overdraft	(2,662)	-	(1,735)	-
Dividends paid	(5,628)	(5,528)	(12,043)	(10,945)
Net proceeds from share issues	<u>912</u>	<u>31,787</u>	<u>1,435</u>	<u>32,377</u>
<i>Cash flow related to financing activities</i>	<b>11,622</b>	<b>15,259</b>	<b>6,657</b>	<b>10,432</b>
Increase in net cash and cash equivalents	6,198	9,964	7,980	13,313
Cash and cash equivalents - Beginning of period	<u>3,147</u>	<u>25,164</u>	<u>1,365</u>	<u>21,815</u>
Cash and cash equivalents - End of period	<b>9,345</b>	<b>35,128</b>	<b>9,345</b>	<b>35,128</b>
Supplemental disclosure of cash flow information:				
Interest paid during the period	6,067	5,990	6,081	6,413

***See Accompanying Notes to Unaudited Interim Consolidated Financial Statements***

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## **Notes to Interim Consolidated Financial Statements**

*Unaudited – June 30, 2016 (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 25 year non-exclusive Generation Licence (collectively the “Licences”) with the Cayman Islands Government (the “Government”), which expire in April 2028 and November 2039 respectively.

In 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 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 Rate Cap and Adjustment Mechanism (“RCAM”). In June 2016, following review and approval by the Electricity Regulatory Authority (“ERA”), the Company increased its base rates by 0.1%. This increase was a result of the 2015 Return on Rate Base (“RORB”) and the increase in the applicable United States (“US”) and Cayman Islands consumer price indices, adjusted to exclude food and fuel, for calendar year 2015. The change in the base rates as a percentage of the US and Cayman Islands consumer price indices was 80% based on the range of the RORB values. The required rate adjustment of 0.1% can be calculated by applying 80% to the total price level index (60% of the Cayman Islands CPI and 40% of the US CPI) of 0.12%. All fuel and lubricating oil costs are passed through to customers without mark-up 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 includes 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. Summary of Significant Accounting Policies**

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. Future Accounting Policies**

### *Revenue from Contracts with Customers*

ASU No. 2014-09 was issued in May 2014 and the amendments in this update create ASC Topic 606, *Revenue from Contracts with Customers*, and supersede the revenue recognition requirements in ASC Topic 605, *Revenue Recognition*, including most industry-specific revenue recognition guidance throughout the codification. This standard completes a joint effort by FASB and the International Accounting Standards Board to improve financial reporting by creating common revenue recognition guidance for US GAAP and International Financial Reporting Standards that clarifies the principles for recognizing revenue and that can be applied consistently across various transactions, industries and capital markets. This standard was originally effective for annual and interim periods beginning after December 15, 2016 and is to be applied on a full retrospective or modified retrospective basis. ASU No. 2015-14 was issued in August 2015 and the amendments in this update defer the effective date of ASU No. 2014-09 by one year to annual and interim periods beginning after December 15, 2017. Early adoption is permitted as of the original effective date. The majority of the Company’s revenue is generated from energy sales to customers based on published tariff rates, as approved by the respective regulators, and is considered to be in the scope of ASU No. 2014-09. The Company and its subsidiary, DataLink Ltd., are assessing the impact that the adoption of this standard will have on the consolidated financial statements and plan to have this assessment complete in 2016.

### *Recognition and Measurement of Financial Assets and Financial Liabilities*

ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, was issued in January 2016 and the amendments in this update address certain aspects of recognition, measurement, presentation and disclosure of financial instruments. Most notably, the amendments require the following: (i) equity investments in unconsolidated entities (other than those accounted for using the equity method of accounting) to be measured at fair value through earnings; however, entities will be able to elect to record equity investments without readily determinable fair values at cost, less impairment, and plus or minus subsequent adjustments for observable price changes; and (ii) financial assets and financial liabilities to be presented separately in the notes to the consolidated financial statements, grouped by measurement category and form of financial asset. This update is effective for annual and interim periods beginning after December 15, 2017.

### *Leases*

ASU No. 2016-02 was issued in February 2016 and the amendments in this update create ASC Topic 842, Leases, and supersede lease requirements in ASC Topic 840, Leases. The main provision of Topic 842 is the recognition of lease assets and lease liabilities on the balance sheet by lessees for those leases that were previously classified as operating leases. For operating leases, a lessee is required to do the following: (i) recognize a right-of-use asset and a lease liability, initially measured at the present value of the lease payments, on the balance sheet; (ii) recognize a single lease cost, calculated so that the cost of the lease is allocated over the lease term on a generally straight-line basis; and (iii) classify all cash payments within operating activities in the statement of cash flows. These amendments also require qualitative disclosures along with specific quantitative disclosures. This update is effective for annual and interim periods beginning after December 15, 2018 and is to be applied using a modified retrospective approach with practical expedients options. Early adoption is permitted. The Company is assessing the impact that the adoption of this update will have on its consolidated financial statements and related disclosures.

### *Improvements to Employee Share-Based Payment Accounting*

ASU No. 2016-09, Improvements to Employee Share-Based Payment Accounting, was issued in March 2016 as part of FASB's simplification initiative. The areas for simplification in this update involve several aspects of accounting for share-based payment transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This update is effective for annual and interim periods beginning after December 15, 2016. Early adoption is permitted, however, an entity that elects early adoption must adopt all the amendments in the same period. The Company is assessing the impact that the adoption of this update will have on its consolidated financial statements.

## **4. Changes in Accounting Policies**

*Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved After the Requisite Service Period*

Effective January 1, 2015, the Company early adopted ASU No. 2014-12 that resolves diversity in practice for employee share-based payments with performance targets that can entitle an employee to benefit from an award regardless of if they are rendering services at the date the performance target is achieved. The adoption of this update did not have an impact on the Company's consolidated financial statements.

#### *Simplifying the Presentation of Debt Issuance Costs*

Effective December 1, 2015, the Company early adopted ASU No. 2015-03 that requires debt issuance costs to be presented on the consolidated balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The Company early adopted ASU No. 2015-15 that clarifies the presentation and subsequent measurement of debt issuance costs associated with line-of-credit arrangements. The update permits an entity to defer and present debt issuance costs as an asset and subsequently amortize the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The adoption of this update was applied retrospectively and did not have a material impact on the Company's consolidated financial statements.

## **5. Accounts Receivable**

Accounts Receivable (\$ thousands)	As at June 30, 2016	As at December 31, 2015
Billings to consumers	12,512	10,593
Unbilled revenues	2,719	2,160
Other receivables	1,087	1,232
Allowance for doubtful accounts	<u>(2,297)</u>	<u>(2,218)</u>
Total accounts receivable	<b>14,021</b>	<b>11,767</b>

#### *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 and machine break-down costs covered by warranties. Other receivables at June 30, 2016 also include billing adjustments for commercial customers.

## 6. Regulatory Assets and Liabilities

Asset/Liability (\$ thousands)	Description	As at June 30, 2016	As at December 31, 2015
Regulatory Assets	Fuel Tracker Account (a)	12,430	13,866
Regulatory Assets	Derivative contract (b)	-	208
Regulatory Assets	Miscellaneous Regulatory Assets (c)	259	272
<b>Total Regulatory Assets</b>		<b>12,689</b>	<b>14,346</b>
Regulatory Liabilities	Derivative contract (b)	(65)	-
Regulatory Liabilities	Government & Regulatory Tracker Account (d)	(2,301)	(812)
Regulatory Liabilities	Miscellaneous Regulatory Liabilities (e)	(1)	(51)
<b>Total Regulatory Liabilities</b>		<b>(2,367)</b>	<b>(863)</b>

- 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 current call option contracts will expire by June 2017.
- 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.
- 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 (\$ thousands)	As at June 30, 2016	As at December 31, 2015
Fuel	1,774	1,392
Lubricating Oil	190	547
Line spares	77	76
Datalink, Ltd.	211	211
Other	<u>1</u>	<u>11</u>
<b>Total</b>	<b>2,253</b>	<b>2,237</b>

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

Property, plant and equipment (\$ thousands)	Cost	Accumulated Depreciation	Net Book Value June 30, 2016
Transmission & Distribution (T&D)	321,114	116,508	204,606
Generation	396,748	158,895	237,853
Other:			
Land	5,304	-	5,304
Buildings	20,167	11,319	8,848
Equipment, motor vehicles and computers	<u>23,277</u>	<u>17,326</u>	<u>5,951</u>
<i>Total of T&amp;D, Generation and Other</i>	766,610	304,048	462,562
Datalink, Ltd.	<u>541</u>	<u>66</u>	<u>475</u>
<b>Property, plant and equipment</b>	<b><u>767,151</u></b>	<b><u>304,114</u></b>	<b><u>463,037</u></b>
Property, plant and equipment	Cost	Accumulated Depreciation	Net Book Value December 31, 2015
Transmission & Distribution (T&D)	310,299	111,750	198,549
Generation	379,354	151,065	228,289
Other:			
Land	5,304	-	5,304
Buildings	20,167	11,081	9,086
Equipment, motor vehicles and computers	<u>22,676</u>	<u>16,692</u>	<u>5,985</u>
<i>Total of T&amp;D, Generation and Other</i>	737,800	290,588	447,212
Datalink, Ltd.	<u>541</u>	<u>53</u>	<u>488</u>
<b>Property, plant and equipment</b>	<b><u>738,341</u></b>	<b><u>290,641</u></b>	<b><u>447,700</u></b>

Included in PP&E are a number of capital projects in progress with a total cost to date of \$32.7 million (December 31, 2015: \$83.1 million). These projects primarily relate to various improvements to the Distribution System. The total cost incurred to date for the 39.7MW Generation Project is \$73.3 million. Included in the total cost is an amount of \$0.07 million that relates to fibre optic assets for DataLink.

Also included in Generation and T&D is freehold land with a cost of \$5.0 million (December 31, 2015: \$5.0 million). In addition, line inventory with a cost of \$4.3 million (December 31, 2015: \$4.3 million) is included in T&D. Engine spares with a net book value of \$13.2 million (December 31, 2015: \$13.7 million) are included in Generation.

The capitalisation of AFUDC 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 2016 is 7.75% (2015: 8.25%) and will be adjusted annually. As a result, during the Second Quarter 2016, the Company recognised \$1.7 million in AFUDC (Second Quarter 2015: \$1.0 million). The increase in AFUDC during Second Quarter 2016 is due to mainly to an increased work in progress assets driven primarily by the generation expansion. AFUDC totalled \$3.6 million for the six months ended June 30, 2016, compared to AFUDC of \$1.9 million for the six months ended June 30, 2015.

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 \$1.2 million for the Second Quarter 2016, an increase of \$0.2 million when compared to \$1.0 million for the Second Quarter 2015. GEC totalled \$2.2 million for the six months ended June 30, 2016, compared to GEC of \$2.1 million for the six months ended June 30, 2015.

Depreciation on DataLink's assets is provided on the cost of PP&E on a straight-line basis over the estimated useful lives ranging from 3 to 30 years. 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 take into consideration the anticipated physical life of the assets.

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 regulation 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.

## 9. Other Assets

Other Assets (\$ thousands)	As at June 30, 2016	As at December 31, 2015
Miscellaneous other assets	24	24
<b>Total</b>	<b>24</b>	<b>24</b>

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**

<b>Intangible Assets (\$ thousands)</b>	<b>Cost</b>	<b>Accumulated Amortisation</b>	<b>Net Book Value June 30, 2016</b>
Deferred licence renewal costs	1,890	773	1,117
Datalink Ltd. deferred licence renewal costs	200	57	143
Computer Software	6,411	4,693	1,718
Other Intangible Assets in progress	127	-	127
Trademark Costs	75	-	75
<b>Total</b>	<b>8,703</b>	<b>5,523</b>	<b>3,180</b>

<b>Intangible Assets (\$ thousands)</b>	<b>Cost</b>	<b>Accumulated Amortisation</b>	<b>Net Book Value December 31, 2015</b>
Deferred licence renewal costs	1,890	725	1,165
Datalink Ltd. deferred licence renewal costs	200	50	150
Computer Software	6,200	4,446	1,754
Other Intangible Assets in progress	127	-	127
Trademark Costs	75	-	75
<b>Total</b>	<b>8,492</b>	<b>5,221</b>	<b>3,271</b>

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**

<b>Accounts Payable (\$ thousands)</b>	<b>As at June 30, 2016</b>	<b>As at December 31, 2015</b>
Fuel Cost Payable	12,941	13,556
Trade Accounts Payable & Accrued expenses	5,006	3,252
Accrued Interest	938	991
Dividends Payable	112	592
Other Accounts Payable	2,433	2,019
<b>Total Accounts Payable</b>	<b>21,430</b>	<b>20,410</b>

Included in Other Accounts Payable is an amount related to the fuel option contracts (see Note 15) of \$0.1 million at June 30, 2016 (\$0.2 million at December 31, 2015).

## 12. Short-Term Financing

The Company has \$50.0 million of unsecured credit financing facilities with the Scotiabank & Trust (Cayman) Limited (“Scotia”) and Royal Bank of Canada (“RBC”). The total available amount was \$19.0 million at June 30, 2016 (\$44.3 million at December 31, 2015).

(\$ thousands)	Total Credit Financing Facilities June 30, 2016	Total Utilized June 30, 2016	Total Available June 30, 2016
<b>Provided by Scotia:</b>			
Letter of Credit	1,000	500	500
Operating, Revolving Line of Credit	10,000	-	10,000
Catastrophe Standby Loan	7,500	-	7,500
Demand Loan Facility- Interim Funding of Capital Expenditures	<u>31,000</u>	<u>30,000</u>	<u>1,000</u>
<b>Total</b>	<b>49,500</b>	<b>30,500</b>	<b>19,000</b>
<b>Provided by RBC:</b>			
Corporate Credit Card Line*	<u>500</u>	<u>500</u>	-
<b>Total</b>	<b>500</b>	<b>500</b>	<b>-</b>

\*. Included in Accounts payable and accrued expenses

A stand-by fee of 0.10% per annum is applied to the daily unused portion of the Standby Loan and Demand Loan facilities. An annual review fee of 0.05% of the total credit facilities is payable upon confirmation that the Facility has been renewed for a further period, being the earlier of 12 months or the next annual review date.

## 13. Share Based Compensation Plans

### Share Options:

The shareholders of the Company approved an Executive Stock Option Plan (“ESOP”) 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	Six Months Ended June 30, 2016 Number of options	Six Months Ended June 30, 2016 Weighted average exercise price per share	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (\$ millions)
Outstanding at beginning of period	282,720	10.53	-	-
Granted	-	-	-	-
Exercised	(40,350)	9.64	-	-
Forefeited/Cancelled	(5,250)	11.61	-	-
Expired	-	-	-	-
Outstanding, end of period	<u>237,120</u>	<u>237,120</u>	<u>3.59</u>	
Vested, end of the period	237,120	237,120	3.59	

Under the fair value method, the compensation expense was \$0.01 million for the six month period ended June 30, 2016 (June 30, 2015: \$0.01 million), resulting in a corresponding increase of Additional Paid in Capital.

**Performance Share Unit (“PSU”) Plan:**

In September 2013, the Board of Directors approved a PSU plan under which officers and certain employees of the Company would receive PSUs. Each PSU represents a unit with an underlying value which is based on the value of one common share relative to the S&P/TSX Utilities Index.

In September 2013, 21,500 PSUs were granted, with additional grants occurring in March 2014 of 26,000, March 2015 of 27,500 and March 2016 of 25,000. The vesting period of the grant is three years, at which time a cash payment may be made to plan participants after evaluation by the Board of Directors of the achievement of certain payment criteria.

PSU Compensation expense was \$0.1 million for the three month period ended June 30, 2016 (June 30, 2015: \$0.01 million), resulting in a corresponding increase to Other Long-Term Liabilities.

**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 32,431,017 and 30,283,909 for the three month periods ended June 30, 2016 and June 30, 2015 respectively. The weighted average Class A Ordinary Shares outstanding were 32,461,660 and 31,029,896 for the six month periods ended June 30, 2016 and June 30, 2015 respectively.

The weighted average of Class A Ordinary Shares used for determining diluted earnings were 32,450,643 and 30,297,402 for the three month periods ended June 30, 2016 and June 30, 2015 respectively. The weighted average of Class A Ordinary Shares used for determining diluted earnings were 32,400,151 and 31,044,679 for the six month periods ended June 30, 2016 and June 30, 2015 respectively. Diluted earnings per Class A Ordinary Share was calculated using the treasury stock method.

As at June 30, 2016 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)	Weighted average shares (in thousands)	Earnings per common shares for the three months ended June 30, 2016
Net earnings applicable to common shares	7,353		
Weighted Average share outstanding		32,431	
<b>Basic Earnings Per Common Share</b>			<b>0.23</b>
Effect of potential dilutive securities:			
Stock Options	-	19	-
Diluted Earnings per Common Share	7,353	32,450	0.23

  

	Earnings (in thousands)	Weighted average shares (in thousands)	Earnings per common shares for the three months ended June 30, 2015
Net earnings applicable to common shares	5,401		
Weighted Average share outstanding		30,284	
Rights Offering Adjustment Factor			
<b>Basic Earnings Per Common Share</b>			<b>0.17</b>
Effect of potential dilutive securities:			
Stock Options	-	13	-
Diluted Earnings per Common Share	5,401	30,297	0.17

## 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:

(\$ thousands)	As at June 30, 2016		As at December 31, 2015	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Long term debt, including current portion	225,679	256,532	236,594	251,723
Fuel Option Contracts <sup>1</sup>	65	65	208	208

<sup>1</sup> 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 current option contracts will expire by June 2017.

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 (\$ thousands)	June 30, 2016 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	256,532	-	256,532	-
Fuel Option Contracts <sup>1</sup>	65	-	65	-

<sup>1</sup> Carrying value of fuel option contracts included in Accounts Payable and Accrued expenses

## 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.

<i>(\$millions)</i>	<b>Total</b>	<b>2016</b>	<b>2017- 2018</b>	<b>2019- 2020</b>	<b>2021 Onward</b>
Accounts payable and accrued expenses	21.4	21.4	-	-	-
Consumer's deposits and advances for construction	7.3	7.3	-	-	-
Letter of credit	0.5	0.5	-	-	-
Short term debt	30.0	30.0			
Long term debt	227	11.0	29.4	32.0	154.6
Long term debt interest	<u>93.9</u>	<u>11.3</u>	<u>20.3</u>	<u>16.7</u>	<u>45.6</u>
Total	380.1	81.5	49.7	48.7	200.2

*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 nil (nil: December 31, 2015).

**17. Finance Charges**

The composition of finance charges were as follows:

Financing costs (\$ thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Interest costs - long-term debt	2,989	3,152	5,951	6,355
Other interest costs	64	45	156	89
AFUDC *	(1,734)	(1,049)	(3,646)	(1,940)
<b>Total</b>	<b>1,319</b>	<b>2,148</b>	<b>2,461</b>	<b>4,504</b>

\*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 \$0.1 million was recognised for the six months ended June 30, 2016 (\$0.1 million: six months ended June 30, 2015).

The composition of the expense was as follows:

(\$ thousands)	Three Months Ended June 30, 2016	Three Months Ended June 30, 2015	Six Months Ended June 30, 2016	Six Months Ended June 30, 2015
Interest cost	82	77	164	154
Expected return on plan assets	(77)	(80)	(154)	(160)
Amortisation of actuarial losses	<u>56</u>	<u>51</u>	<u>112</u>	<u>102</u>
<b>Total</b>	<b>61</b>	<b>48</b>	<b>122</b>	<b>96</b>

This expense has been recorded in general and administrative expenses.

**19. Foreign Exchange**

The closing rate of exchange on June 30, 2016 as reported by the Bank of Canada for the conversion of U.S. dollars into Canadian dollars was Cdn \$1.2917 per US\$1.00. The official exchange rate for the conversion of Cayman Islands dollars into U.S. 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 June 30, 2016 for conversion of Cayman Islands dollars into Canadian dollars was Cdn \$1.5500 per CI\$1.00 (December 31, 2015: Cdn \$1.6608).

## **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 \$0.30 per IG of diesel fuel it imports. In addition, the Company pays customs duties of 15% on all other imports.

## **21. Commitments**

The Company has a primary fuel supply contract with RUBiS Cayman Islands Limited ("RUBiS"). Under the agreement the Company is committed to purchase approximately 60% of its diesel fuel requirements for its generating plant from RUBiS. The Company also has a secondary fuel supply contract with Sol Petroleum Cayman Limited ("Sol") and is committed to purchase approximately 40% of the Company's fuel requirements for its generating plant from Sol. Contracts with RUBiS and Sol were executed in September 2012. Both contracts expired on July 31, 2014 with the option to renew for two additional 18 month terms. The Company executed 18 month fuel supply contracts in September 2014 upon the expiration of its previous fuel supply contracts with both RUBiS and Sol. The Company is currently negotiating the renewal terms with RUBiS for the final 18 month contract. The contract with Sol was renewed for a final 18 month term on March 1, 2016. The approximate remaining quantities per the fuel contract on an annual basis are, by fiscal year in millions of IGs: 2016 – 7.0 and 2017 – 8.9. Both contracts qualify for the Normal Purchase Normal Sale exemption under ASC 815 and do not qualify as derivatives.

The point of delivery for fuel billing purposes remains at the Company's North Sound Plant compound. The Company is also responsible for the management of the fuel pipeline and ownership of bulk fuel inventory at the North Sound Plant.

As a result of the Company's bulk fuel inventory, the value of CUC's closing stock of fuel at June 30, 2016 was \$1.5 million (December 31, 2015: \$1.4 million). This amount includes all fuel held in CUC's bulk fuel storage tanks, service tanks and day tanks located at the North Sound Plant.

In December 2015 the ERA approved CUC's 2016-2020 Capital Investment Plan in the amount of \$204 million. Costs related to the competitive bid award to install 39.7 megawatts ("MW") of generation capacity are included in the approved CIP in the amount of CUC's competitive bid.

As a result of CUC's successful bid, the Company entered into a design-build contract agreement for the generation project with the consortium of Burmeister & Wain Scandinavian Contractor A/S ("BWSC") of Denmark and MAN Diesel & Turbo SE ("MAN") of Germany. The agreement covers the purchase and turnkey installation of a new 39.7 MW power plant which is comprised of two 18.5 MW V48/60 medium-speed diesel generating units, one 2.7 MW waste heat recovery steam turbine, and associated auxiliary equipment. This contract with variation orders is now valued at approximately \$56.1 million, previously \$55.4 million. On this contract a total of \$11.1 million was spent in 2014, an additional \$38.8 million was spent during the year ended December 31, 2015, an additional \$5.1 million was spent during the six months ended June 30, 2016 and the remaining amount of \$1.1 million is expected to be spent during 2016.

**22. Transactions with Related Parties**

Miscellaneous receivables were nil at June 30, 2016 (nil as at December 31, 2015). Miscellaneous payables to Fortis Turks & Caicos, a subsidiary of Fortis Inc., were nil at June 30, 2016 (\$11,017 as at December 31, 2015 for travel expenses). Miscellaneous payables to Fortis Inc., the Company's majority shareholder, totaling nil were outstanding at June 30, 2016 (\$3,300 as at December 31, 2015 for labor, hurricane preparedness and travel expenses).

**23. 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.

#### 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:

#### **CST Trust Company**

P.O. Box 700, Station B

Montreal, QC

H3B 3K3

North America toll free – 1-800-387-0825

Direct – 416-682-3860

Fax – 1-888-249-6189

E-mail: [inquiries@canstockta.com](mailto:inquiries@canstockta.com)

#### **Caribbean Utilities Company, Ltd.**

Company Secretary

P.O. Box 38

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CAYMAN ISLANDS

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Website: [www.cuc-cayman.com](http://www.cuc-cayman.com)

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

#### **Caribbean Utilities Company, Ltd.**

Assistant to the Company Secretary

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