EPCOR Utilities Inc.
Interim Management's Discussion and Analysis
March 31, 2016

This management's discussion and analysis (MD&A) dated May 6, 2016, should be read in conjunction with the condensed consolidated interim financial statements of EPCOR Utilities Inc. for the three months ended March 31, 2016, and 2015, including significant accounting policies adopted (note 3), the consolidated financial statements and MD&A for the year ended December 31, 2015, including standards and interpretations not yet applied (note 3(w)), related party transactions (note 27) and financial instruments (note 28), and the cautionary statement regarding forward-looking information at the end of this MD&A. In this MD&A, any reference to "the Company", "EPCOR", "it", "its", "we", "our" or "us", except where otherwise noted or the context otherwise indicates, means EPCOR Utilities Inc., together with its subsidiaries. In this MD&A, Capital Power refers to Capital Power Corporation and its directly and indirectly owned subsidiaries including Capital Power L.P., except where otherwise noted or the context otherwise indicates. Financial information in this MD&A is based on the condensed consolidated interim financial statements, which were prepared in accordance with International Financial Reporting Standards (IFRS), and is presented in Canadian dollars unless otherwise specified. In accordance with its terms of reference, the Audit Committee of the Company's Board of Directors reviews the contents of the MD&A and recommends its approval by the Board of Directors. This MD&A was approved and authorized for issue by the Board of Directors on May 6, 2016.

OVERVIEW

EPCOR is wholly owned by The City of Edmonton (the City). EPCOR, through wholly owned subsidiaries, builds, owns and operates electrical transmission and distribution networks, water and wastewater treatment facilities and infrastructure in Canada and the United States (U.S.) and provides Regulated Rate Option (RRO) and default supply electricity related services and also sells electricity and natural gas to Alberta residential consumers under contracts through its Encor brand. EPCOR's water business provides water purification, water distribution, wastewater treatment and related management services within the city of Edmonton and several other communities in Western Canada and the Southwestern U.S. In Western Canada the water business includes design, build, finance, operating and maintenance services for municipal and industrial customers. In Southwestern U.S. the water business includes wastewater collection services.

Net income for the three months ended March 31, 2016, was $78 million compared with net income of $69 million for the comparative period in 2015. The increase of $9 million was due in part to higher approved electricity and water customer rates, gains on sales of surplus lands, higher income related to industrial service contracts, and dividend income from our investment in Capital Power. Partially offsetting these increases was no equity share of income of Capital Power L.P. and lower favorable fair value adjustments related to financial electricity purchase contracts.

EPCOR's core operations performed well in the first quarter without any significant issues or disruptions to customers. Net income from core operations for the three months ended March 31, 2016, was $75 million compared with net income from core operations of $50 million for the comparative period in 2015, as described in the net income table on page 3 of this MD&A. The increase of $25 million was driven in part by higher approved electricity and water customer rates, gains on sales of surplus lands, and higher income related to industrial service contracts. Income from core operations is a non-IFRS financial measure as described in Net Income on page 2 of this MD&A.

CONSOLIDATED RESULTS OF OPERATIONS

Revenues

(Unaudited, $ millions)		
Revenues for the period ended March 31, 2015	**$**	**473**
Higher Water Services segment revenues		4
Higher electricity Distribution and Transmission segment revenues		13
Lower Energy Services segment revenues		(11)
Other		(4)
Increase in revenues from core operations		2
Revenues for the period ended March 31, 2016	**$**	**475**

Consolidated revenues were higher by $2 million for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to the net impact of the following:

- Water Services segment revenues were higher primarily due to higher customer rates and volumes, industrial service contracts revenues, and foreign exchange translation gains, partially offset by lower construction revenues from the Regina wastewater treatment plant project.
- Electricity Distribution and Transmission segment revenues were higher primarily due to higher approved electricity customer rates.
- Energy Services segment revenues were lower primarily due to lower electricity prices and volumes.

Net Income

We use income from core operations to distinguish operating results from the Company's water and electricity businesses from results with respect to its investment in Capital Power and changes in the fair value of financial instruments. This definition has been revised from previous quarters by the addition of the fair value changes of financial instruments. The change in the fair value of financial instruments is the difference between the opening fair value of the derivative instrument for the period and the closing fair value of the derivative instrument. It is a non-IFRS financial measure, which does not have any standardized meaning prescribed by IFRS and is unlikely to be comparable to similar measures published by other entities. It is presented as it provides a useful measure of the Company's core operations and it is referred to by debt holders and other interested parties in evaluating the Company's financial performance and in assessing its creditworthiness.

(Unaudited, $ millions)		
Net income for the period ended March 31, 2015	**$**	**69**
2015 change in the fair value of contracts-for-differences		(10)
2015 change in the fair value of interest rate swaps		5
2015 equity share of income from Capital Power (net of income tax)		(14)
2015 income from core operations		**50**
Higher Water Services segment operating income		16
Higher Distribution and Transmission segment operating income		9
Higher Energy Services segment operating income excluding change in the fair value of contracts-for-differences		3
Other		(3)
Increase in income from core operations		25
2016 income from core operations		**75**
2016 change in the fair value of contracts-for-differences		5
2016 change in the fair value of interest rate swaps		(5)
2016 dividend income from available-for-sale investment in Capital Power		3
Net income for the period ended March 31, 2016	**$**	**78**

Net income was higher for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to the following:

- Changes in each business segment's operating results for the three months ended March 31, 2016, compared with the corresponding period in 2015 as described under Segment Results below.
- Lower favorable change in the fair value of contracts-for-differences.
- EPCOR's equity share of income of Capital Power L.P. was lower due to the Company transitioning from equity accounting to accounting for its investment in Capital Power as an available-for-sale asset following the sale of Capital Power shares in April 2015, when the Company's ownership interest was reduced to below 10%.
- EPCOR's dividend income from Capital Power was higher due to accounting for the investment in Capital Power as an available-for-sale asset commencing in the second quarter of 2015, as described above.

SEGMENT RESULTS

Water Services

(Unaudited, $ millions, including intersegment transactions) **Three months ended March 31,**		**2016**		**2015**
Revenues	$	151	$	147
Expenses		(104)		(116)
Operating income	**$**	**47**	**$**	**31**

Water Services' operating income increased by $16 million for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to the gains on sales of surplus lands, higher approved customer rates, and higher income related to industrial services contracts.

Distribution and Transmission

(Unaudited, $ millions, including intersegment transactions) **Three months ended March 31,**		**2016**		**2015**
Revenues	$	156	$	143
Expenses		(117)		(113)
Operating income	**$**	**39**	**$**	**30**

Distribution and Transmission's operating income increased by $9 million for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to higher net system access collections and transmission revenue.

Energy Services

(Unaudited, $ millions, including intersegment transactions) **Three months ended March 31,**		**2016**		**2015**
Revenues	$	217	$	228
Expenses		(199)		(208)
Operating income		**18**		**20**
Exclude change in the fair value of contracts-for-differences		(5)		(10)
Operating income excluding change in the fair value of contracts-for-differences	**$**	**13**	**$**	**10**

Energy Services' operating income excluding change in the fair value of contracts-for-differences increased by $3 million for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to higher Energy Price Setting Plan margins, partially offset by lower billing charge rates.

Capital Spending and Investment

(Unaudited, $ millions) **Three months ended March 31,**		**2016**		**2015**
Water Services	$	29	$	27
Distribution and Transmission		57		41
Energy Services		-		-
Corporate		2		2
Total capital spending and investment	**$**	**88**	**$**	**70**

Total capital spending and investment was higher for the three months ended March 31, 2016, compared with the corresponding period in 2015 primarily due to increased spending in the Distribution and Transmission segment on growth and lifecycle replacement projects, and increased spending in the Water segment on wastewater and lifecycle projects. This was partially offset by decreased construction activity in the Water Services segment at the Rossdale water treatment plant.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Unaudited, $ millions)	March 31, 2016	December 31, 2015	Increase (decrease)	Explanation of material changes
Cash and cash equivalents	$ 36	$ 36	$ -	Refer to Consolidated Statements of Cash Flows section.
Trade and other receivables	462	620	(158)	Decrease primarily due to payment on the current portion of the Capital Power receivable related to the back-to-back debt and the Regina milestone payment, lower electricity billings and accruals resulting from lower electricity price and volumes, partially offset by an increase in current portion of Regina long-term receivable (see below).
Inventories	16	15	1	
Finance lease receivables	1	1	-	
Other financial assets	275	316	(41)	Decrease due to portions of the Regina long-term receivable reclassified to trade and other receivables, net of construction additions.
Deferred tax assets	79	77	2	Increase due to recognition of tax loss carry-forwards amounts.
Available-for-sale investment in Capital Power	169	167	2	Increase due to fair value adjustments.
Property, plant and equipment	4,570	4,568	2	Increase primarily due to capital expenditures partially offset by foreign currency valuation adjustments, depreciation expense and asset retirements.
Intangible assets and goodwill	274	288	(14)	Decrease primarily due to unfavorable foreign currency valuation adjustments and amortization of assets with finite lives, partially offset by capital expenditures.
Trade and other Payables	234	259	(25)	Decrease primarily due to lower electricity accruals and lower trade payables.
Loans and borrowings (including current portion)	1,913	2,117	(204)	Decrease primarily due to repayment of long-term debt related to Capital Power, repayment of short-term debt and foreign currency valuation adjustments on U.S. dollar denominated debt.
Deferred revenue (including current portion)	952	952	-	
Provisions (including current portion)	159	160	(1)	
Derivative liabilities (including current portion)	16	12	4	Increase primarily due to higher unfavorable fair value adjustments related to the interest rate swaps.
Other liabilities (including current portion)	37	38	(1)	
Deferred tax liabilities	35	35	-	
Equity attributable to the Owner of the Company	2,536	2,515	21	Increase due to increase in net income, partially offset by other comprehensive loss and dividends paid.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited, $ millions)
Cash inflows (outflows)

Three months ended March 31,	2016	2015	Increase (decrease)	Explanation
Operating	$ 136	$ 113	$ 23	Increase primarily reflects higher funds from operations and higher non-cash operating working capital. The higher non-cash operating working capital resulted from a lower decrease in accounts payable and higher decrease in trade and other receivables.
Investing	83	(80)	163	Increase primarily due to higher payments received on financial lease receivables and other assets net of advances including the payment received from Capital Power related to the back-to-back debt, proceeds on disposal of property, plant and equipment, partially offset by higher capital expenditures and lower distributions received from Capital Power.
Financing	(219)	(30)	(189)	Decrease primarily due to higher repayment of long-term debt which includes obligations related to Capital Power, and short-term loans and borrowings.
Opening cash and cash equivalents	36	37	(1)	
Closing cash and cash equivalents	$ 36	$ 40	$ (4)	

Operating Activities and Liquidity

The Company maintains its financial position through rate-regulated utility and contracted operations which generate stable cash flows.

The Company expects to have sufficient liquidity to finance its plans and fund its obligations for the remainder of 2016 with a combination of cash on hand, cash flow from operating activities, interest and principal payments related to long-term loans receivable from Capital Power, the issuance of commercial paper, public or private debt offerings and drawing upon existing credit facilities described below under Financing. EPCOR plans to eventually sell all or a substantial portion of its remaining interest in Capital Power subject to market conditions, to fund its requirements for capital and other circumstances that may arise in the future.

Cash flows from operating activities would be impaired by events that cause severe damage to our facilities and would require unplanned cash outlays for system restoration repairs. Under those circumstances, more reliance would be placed on our credit facilities for working capital requirements until a regulatory approved recovery mechanism was in place or insurance proceeds were received.

Capital Requirements and Contractual Obligations

During the first quarter of 2016, there were no material changes to the Company's capital requirements or purchase obligations, including payments for the next five years and thereafter as previously disclosed in the 2015 annual MD&A.

Financing

Generally, our external capital is raised at the corporate level and invested in the operating business units. Our external financing has consisted of commercial paper issuance, borrowings under committed syndicated bank credit facilities, debentures payable to the City, publicly issued medium-term notes, U.S. private-debt notes and issuance of preferred shares.

The Company has bank credit facilities, which are used principally for the purpose of backing the Company's commercial paper program and providing letters of credit, as outlined below:

(Unaudited, $ millions) **March 31, 2016**	**Expiry**	**Total facilities**	**Banking commercial paper issued**	**Letters of credit and other facility draws**	**Net amounts available**
Committed					
Syndicated bank credit facility[1]	November 2018	$ 200	$ -	$ 41	$ 159
Syndicated bank credit facility	November 2020	350	47	-	303
Total committed		550	47	41	462
Uncommitted					
Bank line of credit	No expiry	25	-	-	25
Total uncommitted		25	-	-	25
Total credit facilities		**$ 575**	**$ 47**	**$ 41**	**$ 487**

1 Restricted to letters of credit.

(Unaudited, $ millions) **December 31, 2015**	**Expiry**	**Total facilities**	**Banking commercial paper issued**	**Letters of credit and other facility draws**	**Net amounts available**
Committed					
Syndicated bank credit facility[1]	November 2018	$ 200	$ -	$ 48	$ 152
Syndicated bank credit facility	November 2020	350	98	-	252
Total committed		550	98	48	404
Uncommitted					
Bank line of credit	No expiry	25	-	-	25
Total uncommitted		25	-	-	25
Total credit facilities		**$ 575**	**$ 98**	**$ 48**	**$ 429**

1 Restricted to letters of credit.

Letters of credit are issued to meet the credit requirements of energy market participants and conditions of certain service agreements. Letters of credit totaling $41 million (December 31, 2015 - $48 million) were issued and outstanding at March 31, 2016.

The committed syndicated bank credit facilities cannot be withdrawn by the lenders until expiry, provided that the Company operates within the related terms and covenants. The extension feature of EPCOR's committed syndicated bank credit facilities gives the Company the option each year to re-price and extend the terms of the facilities by one or more years subject to agreement with the lending syndicate. The Company regularly monitors market conditions and may elect to enter into negotiations to extend the maturity dates.

The Company has a Canadian base shelf prospectus under which it may raise up to $1 billion of debt with maturities of not less than one year. At March 31, 2016, the available amount remaining under this base shelf prospectus was $1 billion (December 31, 2015 - $1 billion). The base shelf prospectus expires in December 2017.

Commercial paper was issued and outstanding at March 31, 2016, for $47 million (December 31, 2015 - $98 million).

If the economy were to deteriorate in the longer term, particularly in Canada and the U.S., the Company's ability to extend the maturity or revise the terms of bank credit facilities, arrange long-term financing for its capital expenditure programs and acquisitions, or refinance outstanding indebtedness when it matures could be adversely impacted. We believe that these circumstances have a low probability of occurring. We continually monitor our capital programs and operating costs to minimize the risk that the Company becomes short of cash or unable to honor its debt servicing obligations. If required, the Company would look to reduce capital expenditures and operating costs and / or sell a portion of its investment in Capital Power as market conditions permit.

Financial Covenants

EPCOR is currently in compliance with all of its financial covenants in relation to its syndicated bank credit facilities, Canadian public medium-term notes and U.S. private-debt notes. Based on current financial covenant calculations, the Company has sufficient borrowing capacity to fund current and long-term requirements. Although the risk is low, breaching these covenants could potentially result in a revocation of EPCOR's credit facilities causing a significant loss of access to liquidity.

For further information on the Company's contractual obligations, refer to the 2015 annual MD&A.

RISK MANAGEMENT

This section should be read in conjunction with the Risk Management section of the 2015 annual MD&A. EPCOR faces a number of risks including strategy execution risk, regulatory risk, political and legislative risk, health and safety risk, risk related to investment in Capital Power, information technology related security risks, water scarcity risk, environment risk, operational risks, electricity price and volume risk, project risk, weather risk, financial liquidity risk, counterparty credit risk, availability of people, foreign exchange risk, conflicts of interest, and general economic conditions, business environment and other risks. The Company employs active programs to manage these risks.

As part of ongoing risk management practices, the Company reviews current and proposed transactions to consider their impact on the risk profile of the Company. There have been no material changes to the risk profile or risk management strategies of EPCOR as described in the 2015 annual MD&A that have affected the condensed consolidated interim financial statements for the three months ended March 31, 2016.

CRITICAL ACCOUNTING ESTIMATES

In preparing the condensed consolidated interim financial statements, management necessarily made judgments and estimates in determining transaction amounts and financial statement balances. The following are the items for which significant estimates were made in the condensed consolidated interim financial statements: electricity revenues and costs, unbilled consumption of electricity and water, fair values and income taxes. Although the current condition of the economy has not impacted our methods of estimating accounting values, it has impacted the inputs in those determinations and the resulting values. Interim results will fluctuate due to the seasonal demands for electricity and water, changes in electricity prices, and the timing and recognition of regulatory decisions. Consequently, interim results are not necessarily indicative of annual results.

For further information on the Company's other critical accounting estimates, refer to the 2015 annual consolidated financial statements and 2015 annual MD&A.

OUTLOOK

In 2016, we intend to continue to focus on growth in rate-regulated water and electricity infrastructure. We expect this growth to come from new infrastructure to accommodate customer growth and lifecycle replacement of existing infrastructure primarily related to the Edmonton and U.S. based operations. We also intend to expand our water and electricity commercial services activity.

Demand for water is expected to continue to increase and we anticipate increased requirements for better water management practices including watershed management and conservation. We will pursue expansion of our portfolio of commercial water contracts.

In the quarter, the Company commenced discussions with the City of Lloydminster related to the creation of a municipal utility corporation, potentially partnering with EPCOR. Negotiations have ended with the Town of Innisfil to purchase a 50% share of its electrical distribution company.

EPCOR's Water segment will be filing their 2017 – 2021 Edmonton water and wastewater performance-based rate application in the second quarter of 2016. A decision on the application is expected in the fourth quarter of 2016.

EPCOR's Distribution and Transmission segment received a $9 million refund from the Alberta Electricity System Operator for the 2013 and 2014 Deferral Account Reconciliation in the first quarter of 2016. This amount will be refunded to customers in the third quarter of 2016.

The Energy Services segment received approval of their 2016 – 2018 Energy Price Setting Plan in the first quarter of 2016. The Company is approved to implement the new plan in the third quarter of 2016. The plan will adapt more quickly to changes in wholesale market conditions thereby reducing EPCOR's risk.

QUARTERLY RESULTS

(Unaudited, $ millions) **Quarters ended**	**Revenues**	**Net income**
March 31, 2016	$ 475	$ 78
December 31, 2015	523	65
September 30, 2015	511	(13)
June 30, 2015	489	139
March 31, 2015	473	69
December 31, 2014	499	75
September 30, 2014	506	23
June 30, 2014	435	55

Events for the past eight quarters compared to the same quarters of the prior year that have significantly impacted net income included:

- March 31, 2016, first quarter results included higher approved electricity and water customer rates, gains on sales of surplus lands, higher income related to industrial services contracts, and higher dividend income from Capital Power. This was partially offset by no equity share of income of Capital Power, and lower favorable fair value adjustments on financial electricity purchase contracts.
- December 31, 2015, fourth quarter results included the impairment of the available-for-sale investment in Capital Power, no equity share of income of Capital Power and lower deferred income tax recovery. This was partially offset by higher approved water and electricity customer rates, higher billing charge rates, higher customer water consumption, and higher favorable fair value adjustments on financial electricity purchase contracts.

- September 30, 2015, third quarter results included the impairment of the available-for-sale investment in Capital Power and unfavorable fair value adjustments related to the financial electricity purchase contracts, partially offset by higher approved water and electricity customer rates, higher billing charge rates, and higher Energy Price Setting Plan margins.
- June 30, 2015, second quarter results included gain on sale of a portion of investment in Capital Power and gain on reclassification of investment in Capital Power to an available-for-sale asset. It also included higher approved water and electricity customer rates, higher fair value adjustments on financial electricity purchase contracts, lower income tax expense due to the re-organization of Energy Services, and favorable fair value adjustments related to the interest rate swap.
- March 31, 2015, first quarter results included higher approved water and electricity customer rates, higher fair value adjustments on financial electricity purchase contracts, higher equity share of income of Capital Power, and lower income tax expense due to the re-organization of Energy Services. This was partially offset by a loss on fair value adjustments related to the interest rate swap.
- December 31, 2014, fourth quarter results included higher approved water and electricity customer rates, recovery of deferred income taxes due to the recognition of loss carry forwards as a result from an increase in forecasted taxable income in Energy Services, gain on dilution of interest in Capital Power and higher income from our equity share of Capital Power, partially offset by higher depreciation on capital assets in service, lower fair value adjustments on interest rate swap and financial electricity purchase contracts, and lower capitalized interest due to lower capital spend during the period.
- September 30, 2014, third quarter results included higher favorable fair value adjustments on financial electricity purchase contracts and higher approved water and electricity customer rates, partially offset by lower income from our equity share of Capital Power.
- June 30, 2014, second quarter results included higher favorable fair value adjustments on financial electricity purchase contracts and higher approved water and electricity customer rates, partially offset by lower income from our equity share of Capital Power.

FORWARD - LOOKING INFORMATION

Certain information in this MD&A is forward-looking within the meaning of Canadian securities laws as it relates to anticipated financial performance, events or strategies. When used in this context, words such as “will”, “anticipate”, “believe”, “plan”, “intend”, “target”, and “expect” or similar words suggest future outcomes.

The purpose of forward-looking information is to provide investors with management’s assessment of future plans and possible outcomes and may not be appropriate for other purposes.

Material forward-looking information within this MD&A, including related material factors or assumptions and risk factors, are noted in the table below:

Forward-looking Information	Material Factors or Assumptions	Risk Factors
The Company expects to have sufficient liquidity to finance its plans and fund its obligations in 2016.	EPCOR is able to generate the expected cash flow from operations and various means of funding remain available to the Company.	EPCOR’s operations do not generate the expected level of cash flow and / or circumstances arise limiting or restricting the Company’s ability to access funds through the various means otherwise available.
EPCOR plans to eventually sell all or a substantial portion of its remaining interest in Capital Power.	EPCOR is able to find suitable lower-risk businesses and / or assets in which to invest the sell-down proceeds. Market conditions permit the sale of Capital Power shares at a price suitable to EPCOR.	EPCOR is unsuccessful in finding suitable businesses and / or assets to invest in, therefore negating further sell downs to raise funds. The market price of Capital Power shares declines to an amount that EPCOR no longer deems it feasible to sell all or substantially all of its interest in Capital Power.

Whether actual results, performance or achievements will conform to the Company’s expectations and predictions is subject to a number of known and unknown risks and uncertainties which could cause actual results to differ from expectations and are identified in the Risk Management section above.

Readers are cautioned not to place undue reliance on forward-looking statements as actual results could differ materially from the plans, expectations, estimates or intentions expressed in the forward-looking statements. Except as required by law, EPCOR disclaims any intention and assumes no obligation to update any forward-looking statement even if new information becomes available, as a result of future events or for any other reason.

ADDITIONAL INFORMATION

Additional information relating to EPCOR including the Company’s 2015 Annual Information Form is available on SEDAR at www.sedar.com.