TransAlta renewables inc.

TransAlta Renewables Inc.
Third Quarter Report for 2016

Management's Discussion and Analysis

This Management's Discussion and Analysis ("MD&A") contains forward-looking statements. These statements are based on certain estimates and assumptions and involve risks and uncertainties. Actual results may differ materially. See the Forward-Looking Statements section of this MD&A for additional information.

This MD&A should be read in conjunction with the unaudited interim condensed consolidated financial statements of TransAlta Renewables Inc. as at and for the three and nine months ended Sept. 30, 2016 and 2015 and should also be read in conjunction with the annual audited consolidated financial statements and MD&A contained within our Annual Report for the year ended Dec. 31, 2015. In this MD&A, unless the context otherwise requires, 'we', 'our', 'us', 'TransAlta Renewables', and the 'Corporation' refer to TransAlta Renewables Inc. and its subsidiaries and 'TransAlta' refers to TransAlta Corporation and its subsidiaries. Capitalized terms not otherwise defined herein have their respective meanings set forth in the Glossary of Key Terms. All dollar amounts in the tables presented in this MD&A are in millions(1) of Canadian dollars except per share amounts which are presented in whole dollars to the nearest two decimals, unless otherwise noted. The condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standard ("IFRS") International Accounting Standards ("IAS") 34 *Interim Financial Reporting*. This MD&A is dated Oct. 31, 2016. Additional information respecting the Corporation, including its Annual Information Form, is available on SEDAR at www.sedar.com and on our website at www.transaltarenewables.com. Information on or connected to our website is not incorporated by reference herein.

Operations of the Corporation

As at Sept. 30, 2016 TransAlta Renewables owned and operated 12 hydro facilities and 16 wind farms in Western and Eastern Canada, and held economic interests, based on the cash flows of TransAlta's Sarnia cogeneration plant, Le Nordais wind farm, and Ragged Chute hydro facility (the "Canadian Assets") totaling 611 MW of highly contracted power generation assets located in Ontario and Quebec, TransAlta's 425 MW Australian gas-fired generation assets, the 150 MW South Hedland facility currently under construction, and the 270 kilometre gas pipeline (the "Australian Assets"), and in TransAlta's Wyoming wind farm.

In total, we own directly or through economic interests, an aggregate of 2,319 MW of gross generating capacity (2) in operation. TransAlta manages and operates these facilities on our behalf under the terms of a Management, Administrative and Operational Services Agreement.

As we have an economic interest, and not direct ownership, of the Australian Assets, Canadian Assets and the Wyoming Wind farm, the operational results of these assets are not consolidated into our results; however, the finance income we receive on the underlying investments is included in our consolidated net earnings.

---

(1) Refer to the Current Accounting Changes section of this MD&A.
(2) We measure Capacity as Net Maximum Capacity (see Glossary of Key Terms for definition of this and other key terms), which is consistent with industry standards. Capacity figures represent Capacity owned and in operation unless otherwise stated. The gross capacity reflects the basis of consolidation of underlying assets owned, plus those in which we hold an economic interest. Net capacity deducts capacity attributable to non-controlling interest in these assets.

Non-IFRS Measures

We evaluate our performance using a variety of measures. Certain of the measures discussed in this MD&A are not defined under IFRS and, therefore, should not be considered in isolation or as an alternative to or to be more meaningful than measures as determined in accordance with IFRS, when assessing our financial performance or liquidity. These measures may not be comparable to similar measures presented by other issuers and should not be considered in isolation or as a substitute for measures prepared in accordance with IFRS. During the third quarter of 2015, we adjusted the way certain of these measures are calculated. Comparative comparable measures have been restated accordingly.

The Corporation's key non-IFRS measures are Comparable Earnings before Interest, Taxes, Depreciation, and Amortization ("Comparable EBITDA"), Adjusted Funds from Operations ("AFFO") and Comparable Cash Available for Distribution ("Comparable CAFD"). Comparable EBITDA is comprised of our reported EBITDA adjusted to include Comparable EBITDA of the facilities in which we hold an economic interest, which is their reported EBITDA adjusted for: 1) finance lease income and the change in the finance lease receivable amount; and, 2) contractually fixed management costs. Reported EBITDA and Comparable EBITDA are presented to provide management and investors with a proxy for the amount of cash generated from operating activities before net interest expense, non-controlling interest, income taxes, and the impacts of timing on the finance income from subsidiaries of TransAlta in which we have an economic interest. We present Comparable EBITDA along with operational information of the assets in which we own an economic interest so that readers can better understand and evaluate the drivers of those assets in which we have the economic interest. Since the economic interests are designed to provide the Corporation with returns as if we owned the assets themselves, presenting the operational information and Comparable EBITDA provides a more complete picture for readers to understand the underlying nature of the investments and the resultant cash flows that would otherwise only be presented as finance income from the investments. AFFO is calculated as the cash flow from operating activities before changes in working capital, less sustaining capital expenditures, distributions paid to subsidiaries' non-controlling interest and finance income, plus AFFO of the assets owned through economic interests, which is calculated as Comparable EBITDA from the economic interests less the change in long term receivable, sustaining capital expenditures, and current income tax expense. AFFO provides users with a proxy for the amount from operating activities and investments in subsidiaries of TransAlta in which we have an economic interest. Comparable CAFD is calculated as AFFO less scheduled principal repayments of amortizing debt. Comparable CAFD can be used as a proxy for the cash that will be available to shareholders of the Corporation. One of the primary objectives of the Corporation is to provide reliable and stable cash flows and presenting AFFO and Comparable CAFD assists readers in assessing our cash flows in comparison to prior periods.

See the EBITDA on a Comparable Basis and the Adjusted Funds from Operations and Comparable Cash Available for Distribution sections of this MD&A for additional information.

Additional IFRS Measures

An Additional IFRS measure is a line item, heading, or subtotal that is relevant to an understanding of the financial statements but is not a minimum line item mandated under IFRS, or the presentation of a financial measure that is relevant to an understanding of the financial statements, but is not presented elsewhere in the financial statements. We have included line items entitled "gross margin" and "operating income" in our Condensed Consolidated Statements of Earnings. Presenting these line items provides management and investors with a measure of ongoing operating performance that is readily comparable from period to period.

Forward-Looking Statements

This MD&A and other reports and filings made with securities regulatory authorities include forward-looking statements. All forward-looking statements are based on our beliefs as well as assumptions based on information available at the time the assumptions were made and on management's experience and perception of historical trends, current conditions, and expected future developments, as well as other factors deemed appropriate in the circumstances. Forward-looking statements are not facts, but only predictions and generally can be identified by the use of statements that include phrases such as "may", "will", "believe", "expect", "anticipate", "intend", "plan", "foresee", "potential", "enable", "continue", or other comparable terminology. These statements are not guarantees of our future performance and are subject to risks, uncertainties, and other important factors that could cause our actual performance to be materially different from that projected.

In particular, this MD&A contains forward-looking statements pertaining to our business and anticipated financial performance including, but not limited to: spending on growth and sustaining capital and productivity projects, including sustaining capital expenditures of subsidiaries of TransAlta in which we have an economic interest; expectations in terms of the cost of operations, capital spending, and maintenance, including maintenance performed by third parties, and including the variability of those costs; the expected increase to annual energy production at Wolfe Island; expectations related to future earnings and cash flow from operating and contracting activities; incentive levels from government assistance; the payment of future dividends; expectations in respect of generation availability, capacity, and production; the timing and completion and commissioning of projects under development, including the South Hedland facility and the costs thereof and the funding of such costs; the expected conversion rates of the Class B shares into common shares; expected governmental regulatory regimes, legislation and programs, including the Alberta Climate Leadership Plan and procurement process for renewable generation in Alberta and the cap and trade program in Ontario; and the Ontario GHG cap-and-trade program, and their expected impact on us, as well as the cost of complying with resulting regulations and laws and the value of offsets generated by our wind facilities; estimates of future tax rates, future tax expense, and the adequacy of tax provisions; accounting estimates; expectations regarding operations, maintenance and administration costs; anticipated growth rates in our markets; potential legal and contractual claims; expectations for the ability to access capital markets on reasonable terms; the estimated or potential impact of changes in interest rates and expense and changes in the value of the Canadian dollar relative to the US dollar and the Australian dollar; the monitoring of our exposure to liquidity risk; expectations regarding the impact of the Western Canadian, and Australian economies; expectations regarding entering into additional financial instruments; and expectations regarding borrowing rates and our credit practices.

Factors that may adversely impact our forward-looking statements include risks relating to: changes in general economic conditions, including interest rates; operational risks involving our facilities, including Unplanned Outages at such facilities; risks pertaining to the timing and cost of the construction and commissioning of the South Hedland facility; disruptions in the transmission and distribution of electricity; the effects of weather; disruptions in the source of water, wind, or gas required to operate our facilities; natural disasters; the threat of domestic terrorism, cyberattacks, and other man-made disasters; equipment failure and our ability to carry out repairs in a cost-effective or timely manner; industry risk and competition; fluctuations in the value of foreign currencies; the need for additional financing and the ability to access financing at a reasonable cost; structural subordination of securities; counterparty credit risk; insurance coverage; our provision for income taxes; legal and contractual proceedings involving the Corporation; reliance on key personnel; the regulatory and political environments in the jurisdictions in which we operate; increasingly stringent environmental requirements and changes in, or liabilities under, these requirements; and development projects and acquisitions. The foregoing risk factors, among others, are described in further detail in the Risk Factors section of our Annual Information Form and our annual MD&A for the year ended Dec. 31, 2015. All documents are available on SEDAR at www.sedar.com.

Readers are urged to consider these factors carefully in evaluating the forward-looking statements and are cautioned not to place undue reliance on these forward-looking statements. The forward-looking statements included in this document are made only as of the date hereof and we do not undertake to publicly update these forward-looking statements to reflect new information, future events, or otherwise, except as required by applicable laws. In light of these risks, uncertainties, and assumptions, the forward-looking events might occur to a different extent or at a different time than we have described, or might not occur. We cannot assure that projected results or events will be achieved.

Highlights

Consolidated Financial Highlights

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Renewable energy production (GWh)[(1)]	**682**	623	**2,566**	2,279
Revenues	**45**	42	**165**	161
Net earnings (loss) attributable to common shareholders	**23**	61	**(28)**	88
Reported EBITDA	**61**	92	**82**	190
Comparable EBITDA[(2)]	**83**	59	**286**	167
Adjusted funds from operations[(2)]	**55**	40	**193**	122
Cash flow from operating activities	**62**	40	**213**	130
Comparable Cash Available For Distribution[(2)]	**55**	28	**176**	99
Net earnings (loss) per share attributable to common shareholders, basic and diluted	**0.10**	0.32	**(0.13)**	0.56
Adjusted Funds From Operations per share[(2)]	**0.25**	0.21	**0.87**	0.78
Comparable Cash Available For Distribution per share[(2)]	**0.25**	0.15	**0.79**	0.63
Dividends declared per common share	**0.22**	0.21	**0.66**	0.61
Dividends paid per common share	**0.22**	0.21	**0.66**	0.60

As at	Sept. 30, 2016	Dec. 31, 2015
Gas installed capacity (MW)[(3)]	**931**	425
Renewables installed capacity (MW)	**1,388**	1,283
Total assets	**3,878**	3,336
Total long-term liabilities	**1,223**	1,089

- Comparable EBITDA for the three and nine months ended Sept. 30, 2016 increased $24 million and $119 million, compared to the same periods in 2015. The increases are primarily due to the acquisition of the economic interests in the Australian Assets in May 2015 and the Canadian Assets in January 2016, which together contributed EBITDA of $53 million and $164 million, respectively, in the quarter and year-to-date periods, compared to $31 million and $49 million, respectively, from the Australian Assets, for the same periods in 2015.
- AFFO for the three and nine months ended Sept. 30, 2016 increased $15 million and $71 million, respectively, compared to the same periods in 2015, due to the increase in Comparable EBITDA, partially offset by higher sustaining capital expenditures from the Australian Assets and Canadian Assets, current income tax expense of the Canadian Assets, and an increase in a long term receivable resulting from the restructuring of a contract with a counterparty in Australia.
- Reported net earnings (loss) attributable to common shareholders decreased by $38 million and $116 million for the three and nine months ended Sept. 30, 2016, respectively. Losses due to non-cash increases in the fair value of the Class B shares liability were $86 million and $172 million higher in the 2016 periods. The fair value of the Class B shares liability increases when our share price increases. Finance income received on economic interests in assets owned by TransAlta for the quarter and the year-to-date increased by $9 million and $62 million, respectively, due to the acquisition of the economic interests in the Australian Assets and Canadian Assets in May 2015 and January 2016, respectively. Also impacting net income during the quarter are higher foreign exchange gains of $44 million, mainly due to Australian dollar denominated MRPS and economic hedges of committed capital funding, as well as U.S. dollar denominated tracking preferred shares.

---

(1) Includes production from Wyoming Wind, Le Nordais, and Ragged Chute and excludes Australian and Canadian gas-fired generation. Production is not a key revenue driver for gas-fired facilities as most of their revenues are capacity based.
(2) Refer to the Non-IFRS Measures section of this MD&A for further discussion of these Items.
(3) Includes Australian and Canadian gas-fired generation.

Operational Results

3 months ended Sept. 30, 2016	Long-term average renewable energy production (GWh)(1)	Production (GWh) 2016	Production (GWh) 2015	Comparable EBITDA 2016	Comparable EBITDA 2015
Canadian Wind (2)	**507**	**485**	439	**27**	22
Canadian Hydro(3)	**177**	**127**	126	**6**	7
US Wind	**53**	**70**	58	**2**	2
Total - Renewable energy	**737**	**682**	623	**35**	31
Canadian Gas		**451**	-	**19**	-
Australian Gas		**389**	366	**33**	31
Corporate		**-**	-	**(4)**	(3)
Total		**1,522**	989	**83**	59

9 months ended Sept. 30, 2016	Long-term average renewable energy production (GWh)(1)	Production (GWh) 2016	Production (GWh) 2015	Comparable EBITDA 2016	Comparable EBITDA 2015
Canadian Wind(2)	**1,980**	**1,952**	1,773	**116**	107
Canadian Hydro(3)	**382**	**360**	294	**17**	14
US Wind	**243**	**254**	212	**10**	7
Total - Renewable energy	**2,605**	**2,566**	2,279	**143**	128
Canadian Gas		**1,055**	-	**60**	-
Australian Gas		**1,132**	580	**96**	49
Corporate		-	-	**(13)**	(10)
Total		**4,753**	2,859	**286**	167

- Canadian Wind: Comparable EBITDA increased $5 million and $9 million, respectively, for the three and nine months ended Sept. 30, 2016, compared to the same periods in 2015, primarily due to EBITDA contributed by our economic interest in Le Nordais acquired in January 2016 and a return to more normal and favourable wind resource in Eastern Canada.
- Canadian Hydro: Comparable EBITDA was stable for the quarter with similar production levels compared to the same period in 2015. Year-to-date Comparable EBITDA for the year improved by $3 million, as our production remained in line with our long term average and was higher than the previous period. Performance for the quarter and year-to-date included production and EBITDA from our economic interest in Ragged Chute acquired in January 2016.
- U.S. Wind: Comparable EBITDA remained consistent and increased $3 million, respectively, for the three and nine months ended Sept. 30, 2016, compared to the same periods in 2015. Improved year-to-date production and EBITDA was the result of strong wind resource and performance in the first half of the year.
- Canadian Gas: Comparable EBITDA since our acquisition of the economic interests in the Sarnia cogeneration facility in January 2016 was $19 million and $60 million, respectively, for the three and nine months ended Sept. 30, 2016. Business operations and results have been in line with expectations from when we acquired the interest in the facility.
- Australian Gas: Comparable EBITDA for the three and nine months ended Sept. 30, 2016 was $33 million and $96 million, respectively, and in line with expectations from the business when we acquired the economic interest in the Australian Assets in May 2015.
- Corporate: Corporate costs for the three and nine months ended Sept. 30, 2016 increased $1 million and $3 million, respectively, compared to the same periods in 2015, due to higher fees following our investment in the economic interest in the Canadian Assets.

---

(1) Long-term average is calculated on an annualized basis from the average annual energy yield predicted from our simulation model based on historical resource data performed over a period of typically 15 years for wind and 30 years for hydro.
(2) Includes our economic interest in Le Nordais.
(3) Includes our economic interest in Ragged Chute.

Adjusted Funds from Operations and Comparable Cash Available for Distribution

AFFO and Comparable CAFD provide investors with a proxy for the amount of cash generated from operating activities of our business as well as from investments in subsidiaries of TransAlta in which we own an economic interest before changes in working capital, and provide the ability to evaluate cash flow trends more readily in comparison with results from prior periods.

Beginning in the third quarter of 2015, AFFO is reduced by sustaining capital expenditures and distributions to non-controlling interests, and both AFFO and Comparable CAFD exclude the effects of timing and working capital on distributions from subsidiaries of TransAlta in which we hold an economic interest. The comparative periods have been restated to reflect this methodology.

AFFO per share and Comparable CAFD per share are calculated as follows using the weighted average number of common shares outstanding during the period.

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Cash flow from operating activities	**62**	40	**213**	130
Change in non-cash operating working capital balances	**(8)**	6	**(27)**	4
Adjusted cash flow from operations before changes in working capital	**54**	46	**186**	134
Adjustments:				
Sustaining capital expenditures	**(4)**	(2)	**(7)**	(7)
Distributions paid to subsidiaries' non-controlling interest	**(2)**	(1)	**(5)**	(4)
Finance Income	**(39)**	(30)	**(112)**	(50)
AFFO - economic interests[1]	**46**	27	**131**	49
AFFO	**55**	40	**193**	122
Deduct:				
Principal repayments of amortizing debt	**-**	(12)	**(17)**	(23)
Comparable CAFD	**55**	28	**176**	99
Weighted average number of common shares outstanding in the period (millions)	**224**	191	**223**	156
AFFO per share	**0.25**	0.21	**0.87**	0.78
Comparable CAFD per share	**0.25**	0.15	**0.79**	0.63

Comparable CAFD for the three months ended Sept. 30, 2016 increased $27 million and $77 million for the three and nine months ended Sept. 30, 2016, compared to the same periods in 2015, primarily due to the acquisition of the economic interests in the Canadian Assets in Jan. 2016. The Canadian Assets contributed AFFO of $18 million during the quarter and $55 million year-to-date.

(1) Refer to the Reconciliation of Comparable EBITDA from Economic Interests to Reported Finance Income by Source table in this MD&A.

Reconciliation of Comparable EBITDA to AFFO

3 months ended Sept. 30	2016 Owned Assets	2016 Economic Interests	2016 Total	2015 Owned Assets	2015 Economic Interests	2015 Total
Comparable EBITDA	28	55	83	26	33	59
Interest expense	(12)	-	(12)	(9)	-	(9)
Sustaining capital expenditures	(4)	(9)	(13)	(2)	(5)	(7)
Current income tax expense	(1)	(3)	(4)	(1)	-	(1)
Distributions paid to subsidiaries' non-controlling interest	(2)	-	(2)	(1)	-	(1)
Unrealized risk management gain	-	3	3	-	-	-
Other	-	-	-	-	(1)	(1)
AFFO	9	46	55	13	27	40

9 months ended Sept. 30	2016 Owned Assets	2016 Economic Interests	2016 Total	2015 Owned Assets	2015 Economic Interests	2015 Total
Comparable EBITDA	112	174	286	111	56	167
Interest expense	(36)	-	(36)	(26)	-	(26)
Change in long term receivable	-	(15)	(15)	-	-	-
Sustaining capital expenditures	(7)	(20)	(27)	(7)	(6)	(13)
Current income tax expense	(4)	(9)	(13)	(2)	-	(2)
Distributions paid to subsidiaries' non-controlling interest	(5)	-	(5)	(4)	-	(4)
Unrealized risk management gain	-	2	2	-	-	-
Currency adjustment	-	(1)	(1)	-	-	-
Other	2	-	2	1	(1)	-
AFFO	62	131	193	73	49	122

AFFO for the three and nine months ended Sept. 30, 2016 increased $15 million and $71 million respectively, compared to the same periods in 2015, primarily due to the acquisition of the economic interests in the Canadian Assets in January 2016 and the Australian Assets in May 2015. AFFO from assets owned directly was impacted by higher incremental interest expense relating to additional debt and higher levels of sustaining capital.

Significant and Subsequent Events

Closing of $159 Million Project Financing

On June 3, 2016, our indirect wholly-owned subsidiary, New Richmond Wind L.P. (the "Issuer"), closed a bond offering of approximately $159 million which is secured by a first ranking charge over all assets of the Issuer. The bonds are amortizing and bear interest from their date of issue at a rate of 3.963 per cent, payable semi-annually, and mature on June 30, 2032. Net proceeds of the financing were used to repay debt maturing in one of our subsidiaries, to repay intercompany debt with TransAlta as well as to fund the construction of our South Hedland facility in Australia.

Akolkolex Contract Renewal

In the second quarter, we finalized the recontracting of our 10 MW Akolkolex hydro facility and executed a 30 year contract with BC Hydro, subject to B.C regulatory approval.

Investment in TransAlta's Sarnia Cogeneration Plant, Le Nordais Wind Farm, and Ragged Chute Hydro Facility

On Jan. 6, 2016, we acquired an economic interest in the Canadian Assets for a combined value of approximately $540 million. The Canadian Assets consist of approximately 611 MW of highly contracted power generation assets located in Ontario and Quebec. We invested in CDN Tracking Preferred Shares of a subsidiary of TransAlta that will provide us with an economic interest based on the underlying net distributable profits of the entities that own the Canadian Assets. TransAlta continues to own, manage, and operate the Canadian Assets.

In addition to the cash consideration of $173 million paid to TransAlta, we issued 15,640,583 common shares with a value as of Nov. 23, 2015 of $152 million, and issued a $215 million convertible unsecured subordinated debenture to TransAlta. The debenture is on an interest-only basis at a coupon of 4.5 per cent per annum payable semi-annually in arrears on June 30 and Dec. 31, and matures on Dec. 31, 2020. On the maturity date, TransAlta will have the right, at its sole option, to convert the outstanding principal amount of the debenture, in whole or in part, into common shares of the Corporation at a conversion price of $13.16 per common share. If on the maturity date TransAlta exercises its conversion option in full, we will issue 16.3 million common shares. If TransAlta does not exercise its conversion option, we may satisfy the principal obligation through the issuance of common shares with a unit value corresponding to 95 per cent of the then-current common share value or repay the debenture with cash. The debenture is a direct unsecured obligation of the Corporation ranking subordinate to all liabilities, except liabilities which by their terms rank in right of payment equally with or subordinate to the debenture. The debenture will rank equal with all subordinate debentures issued by us from time to time.

We funded the cash consideration of the purchase price through the issuance of 17,692,750 subscription receipts at a price of $9.75 per subscription receipt. On Jan. 6, 2016, and upon the closing of the transaction, each holder of subscription receipts received one common share of the Corporation and a cash dividend equivalent payment of $0.07 for each subscription receipt held. As a result, we issued 17,692,750 common shares and paid a total dividend equivalent of $1 million.

South Hedland Facility

We continued to advance the construction of the South Hedland facility. The bulk of major equipment has arrived on site. Installation of the new fuel gas interconnection and high voltage works progressed with the connection and energization of the new generator transformer. The first fire on natural gas was achieved and procuring and manufacturing activities are coming to a close. We continue to expect the project to be delivered on schedule and on budget in mid-2017.

Environmental Regulation Updates

Refer to the Environmental Legislation section of our 2015 Annual MD&A for further details that supplement the recent developments discussed below.

Alberta

In March 2016, Alberta began development of its renewable energy procurement process design for the Alberta Electric System Operator to procure a first block of renewable generation projects to be in-service by mid-2019. A decision on the final design parameters is expected by the end of 2016. On Sept. 14, 2016, Alberta re-confirmed its commitment to achieve 30 per cent renewables in Alberta's electricity energy mix by 2030.

Ontario

On May 19, 2016, Ontario put regulations into effect to implement a Greenhouse Gas cap-and-trade program effective Jan. 1, 2017. Gas-fired electricity generation will be regulated at the gas distribution level. Our gas-fired generation facility in Ontario will not be significantly impacted by virtue of change-in-law provisions within existing power purchase agreements.

Discussion of Additional Information

The amounts provided for in this section include operational metrics and financial information related to the investments in the economic interests of TransAlta subsidiaries. Since the investments in these economic interests provide us with returns as if we owned the assets, presenting the operational information provides users with more information to be able to assess the performance of the assets that generate the finance income related to the economic interests. The Canadian Wind discussion includes the results of the Le Nordais facility. The Canadian Hydro discussion includes the results of the Ragged Chute facility. All of the assets in the U.S. Wind, Canadian Gas and Australian Gas discussions are owned through an investment in an economic interest. The Comparable EBITDA of these assets in which we have an economic interest is reconciled to the finance income recognized in our financial statements in the Reconciliation of Comparable EBITDA from Economic Interests to AFFO and Reported Finance Income by Source section of this MD&A.

Canadian Wind

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Production *(GWh)*	**485**	439	**1,952**	1,773
Gross installed capacity *(MW)*	**1,132**	1,034	**1,132**	1,034
Revenues	**40**	33	**154**	141
Royalties and other costs of sales	**2**	2	**7**	7
Comparable gross margin	**38**	31	**147**	134
Operations, maintenance, and administration	**10**	7	**27**	22
Taxes, other than income taxes	**1**	2	**4**	5
Comparable EBITDA	**27**	22	**116**	107

Production for the three and nine months ended Sept. 30, 2016 increased 46 GWh, and 179 GWh, respectively, compared to 2015 due to the addition of an economic interest in the Le Nordais facility and higher wind resources in Eastern Canada. As a result, comparable EBITDA for the three and nine months ended Sept. 30, 2016 increased $5 million and $9 million, respectively, compared to 2015.

Canadian Hydro

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Production *(GWh)*	**127**	126	**360**	294
Gross installed capacity *(MW)*	**112**	105	**112**	105
Revenues	**8**	9	**23**	20
Royalties and other costs of sales	**-**	1	**2**	2
Comparable gross margin	**8**	8	**21**	18
Operations, maintenance, and administration	**1**	1	**2**	3
Taxes, other than income taxes	**1**	-	**2**	1
Comparable EBITDA	**6**	7	**17**	14

Production for the three months ended Sept. 30, 2016 was consistent with the prior year but remains below the long-term average. The Ragged Chute facility acquired in January 2016 contributed 6 GWh during the quarter. Comparable EBITDA for the three months ended Sept. 30, 2016 was in line with last year.

Production for the nine months ended Sept. 30, 2016 increased 66 GWh compared to 2015 due to the addition of an economic interest in the Ragged Chute facility in January 2016 (31 GWh) and improved hydrological conditions. As a result, Comparable EBITDA for the nine months ended Sept. 30, 2016 increased $3 million compared to 2015. Year-to-date production is now in line with our long-term average after being ahead for the first half of the year.

U.S. Wind

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Production *(GWh)*	**70**	58	**254**	212
Gross installed capacity *(MW)*	**144**	144	**144**	144
Revenues	**4**	3	**15**	11
Royalties and other costs of sales	**-**	-	**1**	-
Comparable gross margin	**4**	3	**14**	11
Operations, maintenance, and administration(1)	**2**	1	**4**	4
Comparable EBITDA	**2**	2	**10**	7

Production at the Wyoming Wind farm for the three and nine months ended Sept. 30, 2016 increased 12 GWh and 42 GWh, respectively, compared to the same periods in 2015, due to better wind resource, resulting in higher revenues of $1 million and $4 million, respectively, for the three and nine months ended. Comparable EBITDA for the three and nine months ended Sept. 30, 2016 was consistent with the same periods last year.

Canadian Gas

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Production *(GWh)*	**451**	-	**1,055**	-
Gross installed capacity *(MW)*	**506**	-	**506**	-
Revenue	**52**	-	**140**	-
Fuel and purchased power	**26**	-	**60**	-
Comparable gross margin	**26**	-	**80**	-
Operations, maintenance, and administration	**7**	-	**20**	-
Comparable EBITDA	**19**	-	**60**	-

We completed the acquisition of an economic interest in the Sarnia cogeneration facility in January 2016. The Sarnia facility performed in line with our expectations during the quarter as the facility is highly contracted.

(1) Includes the effect of contractually fixed management costs.

Australian Gas

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Production *(GWh)*	**389**	366	**1,132**	580
Gross installed capacity *(MW)*	**425**	425	**425**	425
Revenues	**30**	28	**89**	46
Finance lease income(1)	**13**	13	**41**	20
Fuel and purchased power	**(5)**	(5)	**(16)**	(8)
Comparable gross margin	**38**	36	**114**	58
Operations, maintenance, and administration(2)	**5**	5	**18**	9
Comparable EBITDA	**33**	31	**96**	49

The Australian Assets performed in line with expectations, as all facilities are fully contracted. We completed the acquisition of an economic interest in the Australian Assets on May 7, 2015 and, accordingly, 2015 comparative results are for the period from May 7 to Sept. 30.

Other Consolidated Results

Net Interest Expense

The components of net interest expense are shown below:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Interest on debt	**9**	9	**27**	26
Interest on convertible debenture	**3**	-	**8**	-
Loss on redemption of unsecured debenture(3)	**-**	-	**1**	-
Accretion of provisions	**1**	-	**1**	1
Net interest expense	**13**	9	**37**	27

For the three and nine months ended Sept. 30, 2016, net interest expense increased compared to 2015, primarily due to the issuance of the convertible debenture in January 2016 related to the investment in the economic interest in the Canadian Assets.

Class B Shares

As at Sept. 30, 2016, 26.1 million Class B shares were outstanding (Dec. 31, 2015 – 26.1 million). As the Class B shares are convertible into common shares at a variable rate depending on final construction costs of the South Hedland facility, they are classified as liabilities and their change in value is recognized in net earnings. The increase in value of the Class B shares of $129 million is unrealized and relates to the change in value of the underlying common shares during the period (net of the effect of estimated foregone dividends, as discounted using a risk-free rate for the period to conversion). Additional information on Class B shares is presented in Note 11 of our interim condensed consolidated financial statements.

The South Hedland facility is currently expected to be completed on time and on budget and the Corporation expects to convert the Class B shares to common shares on a one to one basis. Once converted to common shares, the Class B Shares will be included in equity and will no longer create the changes in fair value as required by the current accounting treatment.

(1) Finance lease income adjusted for change in finance lease receivable.
(2) Includes the effect of contractually fixed management costs.
(3) Unsecured debentures of principal amount $10 million were redeemed in June 2016 resulting in a net loss on the transaction of $1 million.

Income Taxes

A reconciliation of income taxes and effective tax rates on earnings attributable to common shareholders is presented below:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Earnings (loss) before income taxes	**29**	63	**(10)**	107
Earnings attributable to non-controlling interest	**(1)**	-	**(3)**	(2)
Earnings (loss) attributable to common shareholders	**28**	63	**(13)**	105
(Income) losses not taxable				
Change in fair value of Class B shares	**41**	(45)	**129**	(43)
Finance income	**(35)**	(25)	**(96)**	(42)
Foreign exchange (gains) losses	**(20)**	-	**10**	-
Earnings (loss) attributable to common shareholders subject to tax	**14**	(7)	**30**	20
Income tax expense	**5**	2	**15**	17
Withholding tax - finance income	**(1)**	(1)	**(3)**	(1)
Deferred tax rate adjustment	**-**	-	**(1)**	(4)
Valuation allowance	**-**	(3)	**1**	(5)
Tax expense on investment in subsidiary	**-**	-	**(3)**	-
Income tax expense related to transaction fair value differences at initial recognition	**-**	-	**-**	(4)
Other	**-**	-	**-**	2
Adjusted effective income tax expense (recovery)	**4**	(2)	**9**	5
Adjusted effective tax rate on earnings attributable to common shareholders (%)	**29**	29	**30**	25

The Corporation's expected tax rate ranges between 25% and 30%.

Other Comprehensive Income ("OCI")

As part of the investment in the economic interest in TransAlta's Canadian Assets in the first quarter of 2016, we acquired CDN Tracking Preferred Shares (see the Significant Events and Financial Instruments sections of this MD&A). Under IFRS accounting requirements, we designated these shares as available-for-sale financial assets with the result that changes in the fair value of these shares are recognized in OCI each period.

During the three and nine months ended Sept. 30, 2016, we recognized a $50 million and $17 million, respectively, increase in fair value in OCI. The changes in the fair value of available-for-sale instruments during the periods are primarily attributable to the Australian Tracking Preferred Shares. See Note 4 of our financial statements for additional information.

Sustaining Capital Expenditures

Actual sustaining capital expenditures for assets we directly own, as well as the facilities in which we own economic interests, is noted below for the three and nine months ended Sept. 30, 2016 and 2015:

3 months ended Sept. 30

	Canadian Wind	Canadian Hydro	U.S Wind	Canadian Gas	Australian Gas	Total
2016 Total sustaining expenditures	**3**	**1**	**1**	**1**	**6**	**12**
2015 Total sustaining expenditures	2	-	-	-	5	7

9 months ended Sept. 30

	Canadian Wind	Canadian Hydro	U.S Wind	Canadian Gas	Australian Gas	Total
2016 Total sustaining expenditures	**7**	**2**	**2**	**4**	**12**	**27**
2015 Total sustaining expenditures	7	-	-	-	6	13

Sustaining capital spending for the three and nine months ended Sept. 30, 2016 increased by $5 million and $14 million, respectively, compared to the same periods in 2015, primarily due to the addition of the investments in the economic interests of the Australian Assets and Canadian Assets. While we are not required to fund these expenditures, they reduce the finance income from these investments.

We also incurred $3 million on blade enhancement technology at our Wolfe Island wind project since the beginning of the year. This investment is expected to increase the annual energy production of the Wolfe Island wind project by approximately three per cent.

Growth capital spending on the South Hedland facility for the three and nine months ended Sept. 30, 2016 was $36 million and $83 million, respectively.

Liquidity and Capital Resources

Liquidity risk arises from our ability to meet general funding needs, engage in hedging activities, and manage the assets, liabilities, and capital structure of the Corporation. Liquidity risk is managed by maintaining sufficient liquid financial resources to fund obligations as they come due in the most cost-effective manner.

Our liquidity needs are met through a variety of sources, including cash generated from operations, capital markets, and funding from TransAlta. Our primary uses of funds are operational expenses, capital expenditures, distributions to the non-controlling interest, interest and principal payments on debt and dividends.

Financial Position

The following chart highlights significant changes in the Condensed Consolidated Statements of Financial Position from Dec. 31, 2015 to Sept. 30, 2016:

	Increase/ (decrease)	Primary factors explaining change
Cash and cash equivalents	18	Timing of receipts and payments
Property, plant, and equipment, net	(40)	Depreciation, partially offset by additions
Investments in subsidiaries of TransAlta	575	Increase due to the acquisition of economic interest in the Canadian Assets and additional investments in Australian Assets
Accounts payable and accrued liabilities	13	Timing of payments and accruals
Dividends payable	6	Issuance of common shares as part of the Canadian Assets investment
Long-term debt (including current portion)	17	Issuance of New Richmond bond, partially offset by repayment of credit facilty and unsecured debentures, and redemption of unsecured debenture
Convertible debenture	215	Issuance of convertible debenture as part of the Canadian Assets investment
Class B shares liability (including current portion)	129	Change in value of the Class B shares related to the increased value of the underlying common shares
Deferred income tax liabilities	9	Decrease in tax loss carryforwards
Equity attributable to shareholders	156	Common shares issued, partially offset by the net loss for the period and by dividends declared

Cash Flows

The following chart highlights significant changes in the Consolidated Statements of Cash Flows for the three and nine months ended Sept. 30, 2016 compared to the same periods in 2015:

3 months ended Sept. 30	2016	2015	Primary factors explaining change
Cash and cash equivalents, beginning of period	12	51	
Provided by (used in):			
Operating activities	62	40	Higher cash earnings of $8 million and favourable changes in working capital of $14 million
Investing activities	4	(120)	Decrease in investment in subsidiaries of TransAlta of $110 million
Financing activities	(58)	42	Decrease in borrowings under credit facility of $221 million and higher dividends paid on common shares of $10 million, partially offset by prior year long-term debt repayments of $132 million.
Translation of foreign currency cash	-	1	
Cash and cash equivalents, end of period	20	14	

9 months ended Sept. 30	2016	2015	Primary factors explaining change
Cash and cash equivalents, beginning of period	2	24	
Provided by (used in):			
Operating activities	213	130	Higher cash earnings of $52 million and favourable changes in working capital of $31 million.
Investing activities	(224)	(343)	Decrease in investment in subsidiaries of TransAlta of $106 million, partially offset by higher return on capital on investment in subsidiaries of $17 million.
Financing activities	29	202	Higher repayment of credit facilities and long-term debt of $140 million, lower proceeds on issuance of common shares of $52 million and higher dividends paid of $55 million, partially offset by proceeds on the issuance of a $159 million bond.
Translation of foreign currency cash	-	1	
Cash and cash equivalents, end of period	20	14	

Debt

Debt, including amounts owing to TransAlta, totalled $1,029 million as at Sept. 30, 2016 compared to $797 million as at Dec. 31, 2015. Debt increased from Dec. 31, 2015 primarily due to the issuance in January of the convertible debenture as part of the acquisition of the economic interest in the Canadian Assets and the issuance in June of the New Richmond Wind L.P. (the "Issuer") bond.

In June 2016, the Issuer issued a $159 million bond that bears interest at 3.963 per cent, with principal and interest payable semi-annually in blended payments until maturity on June 30, 2032 and secured by a first ranking charge over all the assets of the Issuer.

In June 2016, the $27 million 5.69 per cent non-recourse unsecured debenture matured and was paid out using existing liquidity. We also redeemed $10 million of non-recourse unsecured debentures that were scheduled to mature in 2018, and made a scheduled semi-annual $17 million principal payment on the Melancthon-Wolfe Wind debenture.

We have a $350 million unsecured credit facility with TransAlta available to us for general corporate purposes, including financing ongoing working capital requirements, construction capital requirements, growth opportunities, and for repayment of outstanding borrowings. For the three and nine months ending Sept. 30, 2016, we repaid $5 million and $86 million, respectively, of the Credit Facility. As at Sept. 30, 2016 there is no amount drawn and outstanding on the Credit Facility (Dec. 31, 2015 – $86 million).

At Sept. 30, 2016, including our Credit Facility and the convertible debenture, $215 million of our debt was due to TransAlta (Dec. 31, 2015 – $86 million).

The Corporation is subject to customary positive and negative covenants related to our debt. We are not in violation of any of these covenants.

Share Capital

On Sept. 30, 2016 and Oct. 31, 2016, we had 224.1 million common shares and 26.1 million Class B shares issued and outstanding. At Dec. 31, 2015 we had 190.8 million common shares and 26.1 million Class B shares issued and outstanding.

During the first quarter, we issued 33.3 million common shares and a $215 million convertible debenture as part of the investment in the economic interest of the Canadian Assets.

The convertible debenture will mature on Dec. 31, 2020. On the maturity date, TransAlta will have the right, at its sole option, to convert the outstanding principal amount of the convertible debenture, in whole or in part, into common shares of the Corporation at a conversion price of $13.16 per common share. If on the maturity date TransAlta exercises its conversion option in full, we will issue 16.3 million common shares. If TransAlta does not exercise its conversion option, we may satisfy the principal obligation through the issuance of common shares with a unit value corresponding to 95 per cent of the then-current common share value or repay the debenture with cash.

Commitments

On July 5, 2016, we renewed the long-term service agreements at two of our wind farms for a period of five years each, commencing August 2016. Total committed expenditures under the extensions are approximately $27 million.

Unconsolidated Structured Entities or Arrangements

Disclosure is required of all unconsolidated structured entities or 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 or the availability of, or requirements for, capital resources. We currently have no such unconsolidated structured entities or arrangements.

2016 Outlook

Business Environment

Economic Environment

Through the use of PPAs, including TransAlta PPAs, substantially all of our owned facilities and the Canadian Assets and Australian Assets are currently contracted, and we therefore expect to see no significant impact on our business from the slowing Western Canadian and Australian economies.

Counterparty credit risk is monitored and we operate in accordance with our established risk management policies. We do not anticipate any material change to our existing credit practices and continue to deal primarily with investment grade counterparties.

A September 2016 meeting of the Wyoming Joint Review Committee voted against the two proposed wind tax bills. It is the Corporation's view that there is unlikely to be a wind tax increase contemplated in the near future.

Environmental Legislation

As noted in the Significant Events section of our 2015 Annual MD&A, Alberta's current GHG program has been renewed and expanded. We expect value realized from our Green Attributes generated in the province in 2016 to be consistent with 2015. Revenue from Green Attributes generated in Alberta amounted to $11 million in 2015 which is expected to be consistent in 2016. The GHG offsets created by our Alberta wind facilities are expected to increase in value through 2017 as the Government of Alberta is increasing compliance costs.

As part of the Climate Leadership Plan, the Government of Alberta has stated its intention to establish a new system of obligations and allowances, benchmarked against highly efficient gas generation, beginning in 2018. The initial compliance price is expected to be set at $30 per tonne of carbon dioxide emissions.

Operations

Production

We expect renewable energy production from our wind and hydro assets in 2016 to be in the range of 3,500 to 3,850 GWh. This includes expected generation from economic interests in the renewable Canadian Assets acquired on Jan. 6, 2016. Contracts from gas-fired generation primarily provide compensation for capacity, and accordingly, production is not a significant performance indicator of that business.

Contracted Cash Flows

Through the use of PPAs, including the TransAlta PPAs, our facilities and those in which we have an economic interest have a weighted average contractual life remaining of approximately 15 years.

Operating Costs

We have established long-term service agreements with suppliers to stabilize operations, maintenance and administration costs. Most of our generation from gas is sold under contracts with pass-through provisions for fuel. For gas generation with no pass-through provision, we purchase natural gas coincident with production, thereby minimizing our exposure to changes in price.

Exposure to Fluctuations in Foreign Currencies

We are exposed to fluctuations in the exchange rate between the Canadian and the Australian and US dollars as a result of our economic interest in the Wyoming Wind Farm and the Australian Assets (including the remaining construction costs for the South Hedland facility). The securities acquired from TransAlta and the related dividends received are denominated in Canadian, Australian and US dollars. TransAlta has agreed to provide us with protection against fluctuations in the exchange rates on the first five years of cash flows from the Australian Assets and for the cost of constructing the South Hedland facility, which is expected to be completed mid-2017. Any changes in foreign investments or foreign-denominated debt may change our exposure. All of our other assets are located in Canada. We may acquire equipment from foreign suppliers in various foreign currencies for future capital projects, which could create exposure to fluctuations in the value of the Canadian dollar related to these currencies.

Our strategy is to mitigate foreign exchange risk on foreign denominated cash flows to ensure our ability to meet dividend requirements. Cash flows relating to the Australian Assets are predominantly hedged under agreements with TransAlta. In addition, we entered into foreign exchange forwards to hedge US dollar cash flows primarily related to the Wyoming Wind assets.

Net Interest Expense

Exposure to interest rate risk is not significant as interest rates on long-term debt are largely fixed. Net interest for 2016 is expected to be higher than 2015, due to a higher volume of debt.

Liquidity and Capital Resources

If there are low wind volumes, low hydro resources, or unexpected maintenance costs, we may need additional liquidity in the future. We expect to maintain adequate available liquidity under our Credit Facility with TransAlta.

The Corporation manages liquidity risk associated with debentures due in 2017 and beyond by preparing and revising long-term external financing plans reflecting business plans and market availability of capital. The Corporation anticipates refinancing its maturing debt based on reasonable commercial terms, primarily through project-level debt.

Income Taxes

The adjusted effective tax rate on earnings attributable to common shareholders excluding non-comparable items for 2016 is expected to be approximately 25 to 30 per cent, compared to the statutory tax rate of 26.7 per cent. Variance from the statutory tax rate is due to certain earnings that are not subject to tax. Finance income earned in relation to our economic interests in subsidiaries of TransAlta is net of certain tax amounts.

Capital Expenditures

Sustaining Capital

Our sustaining capital is comprised of the ongoing capital costs associated with maintaining the existing generating capacity of our facilities. The facilities of TransAlta in which we own economic interests also incur sustaining capital expenditures. While we are not required to fund these expenditures, they reduce the finance income from these investments.

For 2016, our estimate for total sustaining capital expenditures for owned assets and those in which we own an economic interest ranges from $35 million to $41 million.

We reduced our estimate by $9 million compared to the range previously disclosed in our Annual MD&A, due to deferral of a major maintenance project to 2017 and other expected spending reductions.

Construction of South Hedland

In 2016, we anticipate investing $87 million in the construction of the South Hedland facility, with $48 million invested to date in 2016. We have invested $224 million to date. We continue to expect the facility to be delivered on schedule and on budget in mid-2017.

Financing

Financing for these capital expenditures is expected to be provided by cash flow from operating activities, capital markets transactions and the Credit Facility provided by TransAlta.

Financial Instruments

Refer to *Note 12* of our most recent annual consolidated financial statements and Note 7 of our interim condensed consolidated financial statements for the three months and nine months ended Sept. 30, 2016 for details on Financial Instruments. Also refer to the Financial Instruments section of our most recent annual MD&A for additional details. Our risk management profile and practices have not changed materially since Dec. 31, 2015.

As part of our investment in the Canadian Assets, we acquired CDN Tracking Preferred Shares in a subsidiary of TransAlta which have been designated as available-for-sale financial assets and are measured at fair value with changes recognized in OCI.

At Sept. 30, 2016, Level III financial instruments were comprised of financial assets with a carrying value of $1,339 million (Dec. 31, 2015 - $804 million) and financial liabilities with a carrying value of $371 million (Dec. 31, 2015 - $242 million). The changes are attributable, respectively, primarily to the investment in CDN Tracking Preferred Shares, and to changes in value of the Class B shares liability. Refer to the interim condensed consolidated financial statements for the three and nine months ended Sept. 30, 2016 for additional information on these measurements.

Related-Party Transactions and Balances

Related-Party Transactions

Amounts recognized from transactions with TransAlta or subsidiaries of TransAlta, excluding those described in the Significant Events section of this MD&A, are as follows:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Revenue from TransAlta PPAs	**7**	7	**27**	24
Revenue from Green Attributes(1)	**-**	-	**-**	2
Finance income related to subsidiaries of TransAlta	**39**	30	**112**	50
G&A Reimbursement Fee	**4**	3	**12**	8
Interest expense	**2**	3	**8**	9
Realized foreign exchange loss on hedge contribution commitment	**-**	1	**-**	1

(1) The value of Green Attributes was determined by reference to market information for similar instruments, including historical transactions with third parties, with the transaction ultimately reviewed and approved by the Corporation's independent members of the Board of Directors.

Related-Party Balances

Related-party balances include the following:

As at	Sept. 30, 2016	Dec. 31, 2015
Trade and other receivables	34	30
Accounts payable and accrued liabililities (including interest payable)	5	4
Dividends payable	20	17
Investments in subsidiaries of TransAlta	2,140	1,565
Net risk management assets	9	9
Convertible debenture	215	-
Class B shares liability	371	242
Credit Facility	-	86
Letters of credit issued by TransAlta on behalf of the Corporation	59	31
Guarantees provided by TransAlta on behalf of the Corporation	40	226
Indemnification guarantee provided by the Corporation to TransAlta	993	1,013

All of these balances are with TransAlta or subsidiaries of TransAlta.

EBITDA on a Comparable Basis

Presenting Comparable EBITDA from period to period provides management and investors with a proxy for the amount of cash generated from operating activities before net interest expense, non-controlling interest, income taxes, and the impacts of timing and sustaining capital expenditures on finance income from subsidiaries of TransAlta.

Beginning in the third quarter of 2015, Comparable EBITDA also includes the Comparable EBITDA of the facilities in which we hold an economic interest. In prior periods we used to reclassify all the finance income from these sources into Comparable EBITDA. Adjustments for comparative and cumulative periods have been restated to reflect the current methodology.

Reconciliation of Reported EBITDA to Comparable EBITDA

3 months ended Sept. 30, 2016	Reported	Adjustments	Economic interests	Comparable total
Revenues[1]	45	-	102	147
Royalties and other costs of sales	2	-	31	33
Gross margin	43	-	71	114
Operations, maintenance, and administration[2]	13	-	16	29
Taxes, other than income taxes	2	-	-	2
Finance income related to subsidiaries of TransAlta	(39)	39	-	-
Change in fair value of Class B shares	41	(41)	-	-
Foreign exchange gain	(35)	35	-	-
Earnings before interest, taxes, depreciation, and amortization	61	(33)	55	83

(1) Amounts related to economic interests include finance lease income adjusted for change in finance lease receivable amount.

(2) Amounts related to economic interests include the effect of contractually fixed management costs.

9 months ended Sept. 30, 2016

	Reported	Adjustments	Economic interests	Comparable total
Revenues[(1)]	165	-	297	462
Royalties and other costs of sales	8	-	78	86
Gross margin	157	-	219	376
Operations, maintenance, and administration[(2)]	39	-	45	84
Taxes, other than income taxes	6	-	-	6
Finance income related to subsidiaries of TransAlta	(112)	112	-	-
Change in fair value of Class B shares	129	(129)	-	-
Foreign exchange loss	13	(13)	-	-
Earnings before interest, taxes, depreciation, and amortization	82	30	174	286

3 months ended Sept. 30, 2015

	Reported	Adjustments	Economic interests	Comparable total
Revenues[(1)]	42	-	44	86
Royalties and other costs of sales	3		5	8
Gross margin	39	-	39	78
Operations, maintenance, and administration[(2)]	11	-	6	17
Taxes, other than income taxes	2	-	-	2
Finance income related to subsidiaries of TransAlta	(30)	30	-	-
Change in fair value of Class B shares	(45)	45	-	-
Foreign exchange loss	9	(9)	-	-
Earnings before interest, taxes, depreciation, and amortization	92	(66)	33	59

9 months ended Sept. 30, 2015

	Reported	Adjustments	Economic interests	Comparable total
Revenues[(1)]	161	-	77	238
Royalties and other costs of sales	9	-	8	17
Gross margin	152	-	69	221
Operations, maintenance, and administration[(2)]	35	-	13	48
Taxes, other than income taxes	6	-	-	6
Finance income related to subsidiaries of TransAlta	(50)	50	-	-
Change in fair value of Class B shares	(43)	43	-	-
Foreign exchange loss	14	(14)	-	-
Earnings before interest, taxes, depreciation, and amortization	190	(79)	56	167

(1) Amounts related to economic interests include finance lease income adjusted for change in finance lease receivable amount.
(2) Amounts related to economic interests include the effect of contractually fixed management costs.

Reconciliation of Comparable EBITDA from Economic Interests to AFFO and Reported Finance Income by Source

3 months ended Sept. 30	2016						2015		
	Canadian Wind	Canadian Hydro	U.S. Wind	Canadian Gas	Australian Gas	Total	U.S. Wind	Australian Gas	Total
Comparable EBITDA	1	-	2	19	33	55	2	31	33
Sustaining capital	(1)	-	(1)	(1)	(6)	(9)	(1)	(4)	(5)
Current income tax expense	-	-	-	(3)	-	(3)	-	-	-
Unrealized risk management gain	-	-	-	3	-	3	-	-	-
Currency adjustment	-	-	-	-	-	-	-	(1)	(1)
AFFO	-	-	1	18	27	46	1	26	27
Return of capital	-	-	-	(10)	-	(10)	-	-	-
Effects of changes in working capital and other timing on finance income	1	-	5	(3)	-	3	3	-	3
Finance income	1	-	6	5	27	39	4	26	30

9 months ended Sept. 30	2016						2015		
	Canadian Wind	Canadian Hydro	U.S. Wind	Canadian Gas	Australian Gas	Total	U.S. Wind	Australian Gas	Total
Comparable EBITDA	7	1	10	60	96	174	7	49	56
Sustaining capital	(2)	-	(2)	(4)	(12)	(20)	(1)	(5)	(6)
Change in long term receivable	-	-	-	-	(15)	(15)	-	-	-
Current income tax expense	-	-	-	(9)	-	(9)	-	-	-
Unrealized risk management gain	-	-	-	2	-	2	-	-	-
Currency adjustment	-	-	-	-	(1)	(1)	-	(1)	(1)
AFFO	5	1	8	49	68	131	6	43	49
Return of capital	-	-	-	(17)	-	(17)	-	-	-
Effects of changes in working capital and other timing on finance income	-	-	2	(4)	-	(2)	1	-	1
Finance income	5	1	10	28	68	112	7	43	50

Accounting Changes

Critical Accounting Estimates

The critical accounting estimates were made consistent with our most recent annual MD&A for Dec. 31, 2015, and the transaction value in respect of the investment in the economic interests of the Canadian Assets on Jan. 6, 2016, as disclosed in Notes 3, 4 and 10 of the interim condensed consolidated financial statements.

In the second and third quarter significant judgement was applied in relation to the assessment of whether dividends from investments in subsidiaries of TransAlta were to be recognized as income or as return of capital. See Note 1 (C) of the interim financial statements.

Current Accounting Changes

During the first quarter, we changed the presentation of our financial information from rounding in thousands to rounding in millions. Comparative period information presented has been restated accordingly.

Future Accounting Changes

Accounting standards that have been previously issued by the International Accounting Standards Board but are not yet effective, and have not been applied by the Corporation include IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers,* and *IFRS 16 Leases*. Refer to the Future Accounting Changes section of our most recent annual MD&A for information regarding the requirements of these accounting standards.

In April 2016, the IASB issued an amendment to IFRS 15 to clarify the identification of performance obligations, principal versus agent considerations, licenses of intellectual property, and transition practical expedients. Amendments are effective for annual periods beginning on or after Jan. 1, 2018, consistent with IFRS 15.

We continue to assess the impact of adopting these standards on the consolidated financial statements.

Selected Quarterly Information

	Q4 2015	Q1 2016	Q2 2016	Q3 2016
Revenue	75	68	52	45
Net earnings (loss) attributable to common shareholders	107	(36)	(15)	23
Cash flow from operating activities	59	81	70	62
Comparable AFFO	78	82	55	55
Comparable CAFD	78	82	38	55
Net earnings (loss) per share attributable to common shareholders, basic and diluted	0.56	(0.16)	(0.07)	0.10
Comparable CAFD per share	0.41	0.37	0.17	0.25

	Q4 2014	Q1 2015	Q2 2015	Q3 2015
Revenue	73	68	51	42
Net earnings attributable to common shareholders	22	20	7	61
Cash flow from operating activities	45	41	49	40
Comparable AFFO	45	43	39	40
Comparable CAFD	45	32	39	28
Net earnings per share attributable to common shareholders, basic and diluted	0.19	0.17	0.04	0.32
Comparable CAFD per share	0.39	0.28	0.24	0.15

Our business results fluctuate with seasonal variations, with the first and fourth quarters seeing the largest wind volumes and the second and third quarters recording higher hydro volumes. As wind forms a larger part of our renewable fleet, higher revenues and earnings are expected in the first and fourth quarters. On Jan. 6, 2016, we acquired an economic interest in the Canadian Assets, adding 611 MW to our existing capacity. In May 2015, we acquired an economic interest in the Australian Assets, and approximately doubled our capitalization. The earnings after this investment include various effects arising from financial instruments:

- Unfavourable changes in the fair value of the Class B shares in the third and fourth quarters of 2015, and in the first, second, and third quarters of 2016.
- Foreign exchange gains on Australian-dollar-denominated instruments in the fourth quarter of 2015 and the third quarter of 2016 with losses in the first and second quarters of 2016.

Controls and Procedures

Management has evaluated, with the participation of our designated Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in our report is accumulated and communicated to management, including our designated Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding our required disclosure. In designing and evaluating our disclosure controls and procedures, management is required to apply its judgment in evaluating and implementing possible controls and procedures.

There has been no change in the internal control over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. Based on the foregoing evaluation, our designated Chief Executive Officer and Chief Financial Officer have concluded that, as of Sept. 30, 2016, the end of the period covered by this report, our disclosure controls and procedures and our internal controls over financial reporting were effective.

TransAlta Renewables Inc.
Condensed Consolidated Statements of Earnings (Loss)
(in millions of Canadian dollars, except as otherwise noted)

	3 months ended Sept. 30		9 months ended Sept. 30	
Unaudited	**2016**	2015	**2016**	2015
Revenues	**34**	31	**130**	125
Government incentives	**4**	4	**14**	14
Lease revenue	**7**	7	**21**	22
Total revenue	**45**	42	**165**	161
Royalties and other costs of sales	**2**	3	**8**	9
Gross margin	**43**	39	**157**	152
Operations, maintenance, and administration	**13**	11	**39**	35
Depreciation and amortization	**19**	20	**55**	56
Taxes, other than income taxes	**2**	2	**6**	6
Operating income	**9**	6	**57**	55
Finance income related to subsidiaries of TransAlta *(Note 4)*	**39**	30	**112**	50
Net interest expense *(Note 5)*	**(13)**	(9)	**(37)**	(27)
Change in fair value of Class B shares *(Note 11)*	**(41)**	45	**(129)**	43
Foreign exchange gain (loss)	**35**	(9)	**(13)**	(14)
Earnings (loss) before income taxes	**29**	63	**(10)**	107
Income tax expense *(Note 6)*	**5**	2	**15**	17
Net earnings (loss)	**24**	61	**(25)**	90
Net earnings (loss) attributable to:				
Common shareholders	**23**	61	**(28)**	88
Non-controlling interest	**1**	-	**3**	2
	24	61	**(25)**	90
Weighted average number of common shares outstanding in the period *(millions) (Note 12)*	**224**	191	**223**	156
Net earnings (loss) per share attributable to common shareholders, basic and diluted *(Note 12)*	**0.10**	0.32	**(0.13)**	0.56

See accompanying notes.

TransAlta Renewables Inc.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(in millions of Canadian dollars)

Unaudited	3 months ended Sept. 30 2016	3 months ended Sept. 30 2015	9 months ended Sept. 30 2016	9 months ended Sept. 30 2015
Net earnings (loss)	24	61	(25)	90
Losses on derivatives designated as cash flow hedges, net of tax	-	-	(1)	-
Reclassification of losses on derivatives designated as cash flow hedges to net earnings, net of tax	-	-	1	-
Available-for-sale financial assets - net change in fair value *(Note 4)*	50	(8)	17	7
Total items that will be reclassified subsequently to net earnings	50	(8)	17	7
Other comprehensive income (loss)	50	(8)	17	7
Total comprehensive income (loss)	74	53	(8)	97
Total comprehensive income (loss) attributable to:				
Common shareholders	73	53	(11)	95
Non-controlling interest	1	-	3	2
	74	53	(8)	97

See accompanying notes.

TransAlta Renewables Inc.
Condensed Consolidated Statements of Financial Position

(in millions of Canadian dollars)

Unaudited	Sept. 30, 2016	Dec. 31, 2015
Cash and cash equivalents	20	2
Trade and other receivables	58	62
Prepaid expenses	4	2
Risk management assets *(Note 7)*	9	4
Income taxes receivable	-	1
Inventory	3	3
	94	74
Property, plant, and equipment *(Note 8)*		
Cost	2,021	2,012
Accumulated depreciation	(492)	(443)
	1,529	1,569
Intangible assets	86	92
Risk management assets *(Note 7)*	-	6
Other assets	3	3
Investments in subsidiaries of TransAlta *(Note 4)*	2,140	1,565
Deferred income tax assets	26	27
Total assets	3,878	3,336
Accounts payable and accrued liabilities	27	14
Other provisions	1	-
Dividends payable *(Note 12)*	33	27
Current portion of deferred revenue	-	1
Current portion of Class B shares liability *(Note 11)*	371	-
Current portion of long-term debt *(Note 9)*	43	148
	475	190
Long-term debt *(Note 9)*	771	649
Convertible debenture *(Note 10)*	215	-
Class B shares liability *(Note 11)*	-	242
Decommissioning provisions	7	7
Deferred revenues	6	6
Risk management liabilities *(Note 7)*	-	1
Deferred income tax liabilities	224	215
Total liabilities	1,698	1,310
Equity		
Common shares *(Note 12)*	2,469	2,152
Deficit	(347)	(169)
Accumulated other comprehensive income	23	6
Equity attributable to shareholders	2,145	1,989
Non-controlling interest	35	37
Total equity	2,180	2,026
Total liabilities and equity	3,878	3,336

Commitments and contingencies (Note 13)

See accompanying notes.

TransAlta Renewables Inc.
Condensed Consolidated Statements of Changes in Equity
(in millions of Canadian dollars)

Unaudited	Common shares	Deficit	Accumulated other comprehensive income	Equity attributable to shareholders	Non-controlling interest	Total
Balance, Dec. 31, 2015	2,152	(169)	6	1,989	37	2,026
Net earnings (loss)	-	(28)	-	(28)	3	**(25)**
Other comprehensive loss:						
Net change in fair value of available-for-sale financial assets *(Note 4)*	-	-	17	17	-	**17**
Total comprehensive income (loss)	-	(28)	17	(11)	3	**(8)**
Common shares issued to TransAlta *(Note 3)*	152	-	-	152	-	**152**
Public offering *(Note 3)*	165	-	-	165	-	**165**
Common share dividends	-	(150)	-	(150)	-	**(150)**
Distributions to non-controlling interest	-	-	-	-	(5)	**(5)**
Balance, Sept. 30, 2016	**2,469**	**(347)**	**23**	**2,145**	**35**	**2,180**

Unaudited	Common Shares	Deficit	Accumulated other comprehensive income	Equity attributable to shareholders	Non-controlling interest	Total
Balance, Dec. 31, 2014	1,224	(221)	-	1,003	38	1,041
Net earnings	-	88	-	88	2	90
Other comprehensive income:						
Net change in fair value available-for-sale financial assets	-	-	7	7	-	7
Total comprehensive income	-	88	7	95	2	97
Completion of share offering to parent	711	-	-	711	-	711
Completion of public share offering	217	-	-	217	-	217
Common share dividends	-	(102)	-	(102)	-	(102)
Distributions to non-controlling interest	-	-	-	-	(4)	(4)
Balance, Sept. 30, 2015	2,152	(235)	7	1,924	36	1,960

See accompanying notes.

TransAlta Renewables Inc.
Condensed Consolidated Statements of Cash Flows
(in millions of Canadian dollars)

	3 months ended Sept. 30		9 months ended Sept. 30	
Unaudited	**2016**	2015	**2016**	2015
Operating activities				
Net earnings (loss)	**24**	61	**(25)**	90
Depreciation and amortization	**19**	20	**55**	56
Accretion of provisions *(Note 5)*	**1**	-	**1**	1
Deferred income tax expense *(Note 6)*	**4**	1	**11**	15
Change in fair value of Class B shares *(Note 11)*	**42**	(45)	**130**	(43)
Unrealized foreign exchange loss (gain)	**(34)**	8	**13**	14
Other non-cash items	**(2)**	1	**1**	1
Cash flow from operations before changes in working capital	**54**	46	**186**	134
Change in non-cash operating working capital balances	**8**	(6)	**27**	(4)
Cash flow from operating activities	**62**	40	**213**	130
Investing activities				
Additions to property, plant, and equipment *(Note 8)*	**(3)**	-	**(10)**	(5)
Investment in subsidiaries of TransAlta *(Notes 3 and 4)*	**-**	(110)	**(221)**	(327)
Realized risk management and foreign exchange losses		(2)		(2)
Return of capital on investment in subsidiaries of TransAlta *(Note 4)*	**10**	-	**17**	-
Change in non-cash investing working capital balances	**(3)**	(8)	**(10)**	(9)
Cash flow used in (from) investing activities	**4**	(120)	**(224)**	(343)
Financing activities				
Net (increase) decrease in borrowings under credit facility *(Note 9)*	**(5)**	216	**(86)**	216
Issuance of long-term debt *(Note 9)*	**-**	-	**159**	45
Long-term debt repayments *(Note 9)*	**-**	(132)	**(54)**	(178)
Net proceeds on issuance of common shares *(Note 3)*	**-**	-	**162**	214
Dividends paid on common shares *(Note 12)*	**(50)**	(40)	**(145)**	(90)
Distributions to non-controlling interest	**(2)**	(1)	**(5)**	(4)
Other	**(1)**	(1)	**(2)**	(1)
Cash flow from (used in) financing activities	**(58)**	42	**29**	202
Cash flow from (used in) operating, investing, and financing activities	**8**	(38)	**18**	(11)
Effect of translation on foreign currency cash	**-**	1	**-**	1
Increase (decrease) in cash and cash equivalents	**8**	(37)	**18**	(10)
Cash and cash equivalents, beginning of period	**12**	51	**2**	24
Cash and cash equivalents, end of period	**20**	14	**20**	14
Cash income taxes paid	**1**	1	**4**	2
Cash interest paid	**-**	8	**22**	25

Notes to Condensed Consolidated Financial Statements

(Unaudited)

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

1. Background and Accounting Policies

A. The Corporation

TransAlta Renewables Inc. ("TransAlta Renewables" or the "Corporation"), a subsidiary of TransAlta Corporation ("TransAlta"), owns and operates 12 hydro facilities and 16 wind farms in Western and Eastern Canada with a total installed capacity of 1,139 megawatts ("MW") and holds economic interests in TransAlta's 144 MW Wyoming wind farm and 425 MW Australian gas-fired generation assets, as well as a 270 kilometre gas pipeline. These assets are substantially all contracted. On Jan. 6, 2016, the Corporation also acquired economic interests in TransAlta's Sarnia cogeneration plant, Le Nordais wind farm and Ragged Chute hydro facility totalling 611 MW of highly contracted power generation assets located in Ontario and Quebec. The Corporation's head office is located in Calgary, Alberta.

B. Basis of Preparation

These unaudited interim condensed consolidated financial statements have been prepared by management in compliance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting* using the same accounting policies as those used in the Corporation's most recent annual consolidated financial statements. These unaudited interim condensed consolidated financial statements do not include all of the disclosures included in the Corporation's annual consolidated financial statements. Accordingly, these condensed consolidated financial statements should be read in conjunction with the Corporation's most recent annual consolidated financial statements which are available on SEDAR at www.sedar.com.

The unaudited interim condensed consolidated financial statements include the accounts of the Corporation and the subsidiaries that it controls.

The unaudited interim condensed consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments, which are stated at fair value.

The condensed consolidated financial statements are presented in Canadian dollars, which is the Corporation's functional and presentation currency.

The unaudited interim condensed consolidated financial statements reflect all adjustments that consist of normal recurring adjustments and accruals that are, in the opinion of management, necessary for a fair presentation of results. The Corporation's results are partly seasonal due to the nature of electricity, which is generally consumed as it is generated and the nature of wind and run-of-river hydro resources, which fluctuate based on both seasonal patterns and annual weather variation. Typically, run-of-river hydro facilities generate most of their electricity and revenues during the spring and summer months when melting snow starts feeding watersheds and rivers. Inversely, wind speeds are historically greater during the cold winter months and lower in the warm summer months.

These unaudited interim condensed consolidated financial statements were authorized for issue by the Audit Committee on behalf of the Board of Directors on Oct. 31, 2016.

C. Use of Estimates and Significant Judgments

The preparation of these unaudited interim condensed consolidated financial statements in accordance with IAS 34 requires management to use judgment and make estimates and assumptions that could affect the reported amounts of assets, liabilities, revenues, and expenses, and disclosures of contingent assets and liabilities. These estimates are subject to uncertainty. Actual results could differ from these estimates due to factors such as fluctuations in interest rates, foreign exchange rates, inflation and commodity prices, and changes in economic conditions, legislation, and regulations. Refer to Note 2(Q) of the Corporation's most recent annual consolidated financial statements for a more detailed discussion of the significant accounting judgments and key sources of estimation uncertainty.

Significant judgment was applied during 2016 in relation to the assessment of dividends as income or return of capital, as follows:

The Corporation receives dividends from its investment in the preferred shares tracking adjusted TransAlta Energy (Australia) Pty Ltd ("TEA") amounts, the TEA preferred shares, and the preferred shares tracking adjusted Canadian Assets amounts. Determining whether a dividend represents in substance a return of capital requires significant judgment. The Corporation determines the amount of dividends that represents a return of capital based on the lower of: i) the difference, if positive, between the cost base of the shares and their fair value, at the end of the reporting period; and ii) the actual dividend declared on the shares during the reporting period. When it is determined that a dividend represents a return of capital, the carrying amount of the related investment is reduced. During the second and third quarters, the Corporation determined that a portion of the dividend earned on the preferred shares tracking adjusted Canadian Assets amounts constituted a return of capital.

2. Accounting Changes

A. Current Accounting Changes

During the first quarter of 2016, the Corporation changed the presentation of its financial information from rounding in thousands to rounding in millions. Comparative period information presented has been restated accordingly.

B. Future Accounting Changes

Accounting standards that have been previously issued by the International Accounting Standards Board ("IASB") but are not yet effective, and have not been applied by the Corporation, include International Financial Reporting Standards ("IFRS") 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers,* and IFRS 16 *Leases*. Refer to Note 3 of the Corporation's most recent annual consolidated financial statements for information regarding the requirements of these accounting standards.

In April 2016, the IASB issued an amendment to IFRS 15 to clarify the identification of performance obligations, principal versus agent considerations, licenses of intellectual property, and transition practical expedients. Amendments are effective for annual periods beginning on or after Jan. 1, 2018, consistent with IFRS 15.

The Corporation continues to assess the impact of adopting these standards on its consolidated financial statements.

3. Significant Events

Closing of $159 Million Project Financing

On June 3, 2016, the Corporation's indirect wholly-owned subsidiary, New Richmond Wind L.P. (the "Issuer"), closed a bond offering of approximately $159 million which is secured by a first ranking charge over all assets of the Issuer. The bonds are amortizing and bear interest from their date of issue at a rate of 3.963 per cent, payable semi-annually, and mature on June 30, 2032. Net proceeds of the financing were used to repay debt maturing in a subsidiary and intercompany debt with TransAlta as well as to fund the construction of the South Hedland facility in Australia.

Akolkolex Contract Renewal

In the second quarter we finalized the recontracting of our 10 MW Akolkolex hydro facility and executed a 30 year contract with BC Hydro, subject to B.C. regulatory approval.

Investment in TransAlta's Sarnia Cogeneration Plant, Le Nordais Wind Farm, and Ragged Chute Hydro Facility
On Jan. 6, 2016, the Corporation invested in an economic interest based on the cash flows of TransAlta's Sarnia cogeneration plant, Le Nordais wind farm, and Ragged Chute hydro facility (the "Canadian Assets") for a combined value of approximately $540 million. The Canadian Assets consist of approximately 611 MW of highly contracted power generation assets located in Ontario and Quebec. The Corporation's investment consists of the acquisition of tracking preferred shares of a subsidiary of TransAlta that will provide the Corporation with an economic interest based on cash flows broadly equal to the underlying net distributable profits of the entities that own the Canadian Assets. The transaction was originally announced on Nov. 23, 2015. TransAlta will continue to own, manage, and operate the Canadian Assets.

As consideration, the Corporation provided to TransAlta, $173 million in cash, issued 15,640,583 common shares with a value of $152 million, and issued a $215 million convertible unsecured subordinated debenture as discussed in Note 10.

The Corporation funded the cash consideration of the purchase price primarily through the issuance of 17,692,750 subscription receipts at a price of $9.75 per subscription receipt. Upon the closing of the transaction, each holder of subscription receipts received one common share of the Corporation and a cash dividend equivalent payment of $0.07 for each subscription receipt held. As a result, the Corporation issued 17,692,750 common shares and paid a total dividend equivalent of $1 million. Share issuance costs amounted to $8 million, net of a $2 million income tax recovery.

4. Finance Income Related to Subsidiaries of TransAlta

Finance income related to subsidiaries of TransAlta is comprised of income from various interests that in aggregate and over time indirectly provide the Corporation with cash flows based on those of TEA, the Canadian Assets and TransAlta Wyoming Wind LLC, respectively.

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Interest income from investment in mandatory redeemable preferred shares of TEA ("MRPS")	**11**	8	**31**	13
Dividend income from investment in preferred shares	**1**	-	**2**	-
Fee income from indirect guarantee of TEA obligations	**6**	5	**18**	8
Dividend income from investment in preferred shares tracking adjusted TEA amounts	**9**	12	**17**	21
Total finance income related to TEA	**27**	25	**68**	42
Dividend income from investment in preferred shares tracking adjusted Canadian Assets amounts	**6**	-	**34**	-
Dividend income from investment in preferred shares tracking earnings and distributions of TransAlta Wyoming Wind LLC	**6**	5	**10**	8
Total	**39**	30	**112**	50

A summary of investments in subsidiaries of TransAlta is as follows:

As at	Sept. 30, 2016	Dec. 31, 2015
Investment in MRPS	**617**	589
Investment in preferred shares tracking adjusted TEA amounts	**816**	804
Investment in preferred shares of TEA	**48**	29
Total investments in subsidiaries related to TEA	**1,481**	1,422
Investment in preferred shares tracking adjusted Canadian Assets amounts	**523**	-
Investment in preferred shares tracking earnings and distributions of TransAlta Wyoming Wind LLC	**136**	143
Total investment in subsidiaries of TransAlta	**2,140**	1,565

Investment in subsidiaries of TransAlta related to TEA

The Corporation estimated the fair value of the preferred shares tracking adjusted TEA amounts utilizing significant unobservable inputs such as TEA's long-range forecast as part of a discounted cash flow model, as outlined in Note 7(B)(I)(c).

Key assumptions in respect of significant unobservable inputs used in the fair value measurement include the discount rate and the quarterly cash flows from the instrument and guarantee fees. The model extends over 32 years. The table below summarizes quantitative data regarding these unobservable inputs:

Unobservable input	Sept. 30, 2016	Dec. 31, 2015
Discount rate	7.2 per cent	7.6 per cent
Quarterly cash flows	Average of $15.1	Average of $15.6

The following table summarizes the impact on the fair value measurement of a change in the above unobservable inputs to reflect reasonably possible alternative assumptions:

Unobservable input	Alternative assumption	Change in fair value as at Sept. 30, 2016	Change in fair value as at Dec. 31, 2015
Basis point change in discount rates	-10 basis points decrease	7.1	7.3
	+10 basis points increase	(7.0)	(7.1)
Quarterly cash flows	+1% increase	8.2	8.0
	- 1% decrease	(8.2)	(8.0)

Changes in the investments in subsidiaries of TransAlta that relate to TEA are detailed as follows:

	MRPS(1)	Preferred shares tracking adjusted TEA amounts	Preferred shares of TEA(2)	Total
Investment balance at Dec. 31, 2015	589	804	29	1,422
Additional investment	34	-	14	48
Unrealized foreign exchange losses recognized in earnings	(6)	-	-	(6)
Net change in fair value recognized in OCI	-	12	5	17
Investment balance at Sept. 30, 2016	**617**	**816**	**48**	**1,481**

(1) Principal amount as at Dec. 31, 2015 and Sept. 30, 2016 was AUD$592 million and AUD$627 million, respectively.

(2) Principal amount as at Dec. 31, 2015 and Sept. 30, 2016 was AUD$32 million and AUD$47 million, respectively.

During the third quarter the preferred shares tracking adjusted TEA amounts increased by $47 million. The change in fair value in the quarter is the result of foreign exchange gains, a decrease in the discount rate, and changes in the coupon rate on the preferred shares.

Investment in a Subsidiary of TransAlta Related to Canadian Assets

Changes in the investment in a subsidiary of TransAlta that relate to the Canadian Assets are detailed as follows:

	Preferred shares tracking adjusted Canadian Assets amounts
Issuance on initial investment - Jan. 6, 2016	540
Return of capital[(1)(2)]	(17)
Investment balance at Sept. 30, 2016	523

(1) See Note 1 (C).

(2) Includes a return of capital of $7 million as at June 30, 2016.

The investment in the preferred shares tracking adjusted Canadian Assets amounts has been classified as an available-for-sale financial asset. The investment is measured at fair value on an ongoing basis, with changes in fair value recognized in OCI.

The Corporation estimated the fair value of the preferred shares tracking adjusted Canadian Assets amounts utilizing significant unobservable inputs such as the long-range forecasts of the Canadian Assets as part of discounted cash flow models, as outlined in Note 7(B)(I)(c).

Key assumptions in respect of significant unobservable inputs used in the fair value measurements include the discount rates and the quarterly cash flows. The models extend over 28 years. The table below summarizes quantitative data regarding the material unobservable inputs:

Unobservable input	Sept. 30, 2016
Discount rate	7.5 per cent
Quarterly cash flows	Average of $10.3

The following table summarizes the impact on the fair vale measurement of a change in the above unobservable inputs to reflect reasonably possible alternative assumptions:

Unobservable input	Alternative assumption	Change in fair value as at Sept. 30, 2016
Basis point change in discount rates	-10 basis points decrease	3.7
	+10 basis points increase	(3.7)
Quarterly cash flows	+1% increase	5.2
	- 1% decrease	(5.2)

5. Net Interest Expense

The components of net interest expense are as follows:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Interest on long-term debt	**9**	9	**27**	26
Interest on convertible debenture	**3**	-	**8**	-
Loss on redemption of unsecured debenture (see Note 9)	**-**	-	**1**	-
Accretion of provisions	**1**	-	**1**	1
Net interest expense	**13**	9	**37**	27

6. Income Taxes

The components of income tax expense are as follows:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Current income tax expense	**1**	1	**4**	2
Adjustments in respect of deferred income tax of previous years	**-**	-	**-**	(1)
Deferred income tax expense (recovery) arising from the writedown of deferred tax assets(1)	**-**	3	**(1)**	4
Deferred income tax expense (recovery) related to the origination and reversal of temporary differences	**4**	(2)	**8**	8
Deferred income tax expense related to investment in subsidiary	**-**	-	**3**	
Deferred income tax expense resulting from changes in tax rates(2)	**-**	-	**1**	4
Income tax expense	**5**	2	**15**	17

(1) Relates to the writedown (recovery) of the deferred tax assets on realized and unrealized foreign exchange capital losses as the Corporation does not expect to realize capital gains in the foreseeable future.

(2) 2016 is the impact of increase in New Brunswick corporate income tax rate from 12 per cent to 14 per cent and 2015 is the impact of increase in Alberta income tax rate from 10 per cent to 12 per cent.

Presented in the Condensed Consolidated Statements of Earnings (Loss) as follows:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Current income tax expense	**1**	1	**4**	2
Deferred income tax expense	**4**	1	**11**	15
Income tax expense	**5**	2	**15**	17

7. Financial Instruments and Risk Management

A. Financial Assets and Liabilities – Measurement

Financial assets and financial liabilities are measured on an ongoing basis at fair value or amortized cost.

Following the close of the investment in the Canadian Assets described in Note 3, the Corporation is party to new financial instruments. The preferred shares tracking adjusted Canadian Assets amounts have been classified as available-for-sale, and the liability component of the convertible debenture issued has been classified as an other financial liability measured at amortized cost.

B. Fair Value of Financial Instruments

I. Level I, II, and III Fair Value Measurements

The Level I, II, and III classifications in the fair value hierarchy utilized by the Corporation are defined below. The fair value measurement of a financial instrument is included in only one of the three levels, the determination of which is based on the lowest level input that is significant to the derivation of the fair value.

a. Level I

Fair values are determined using inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Corporation has the ability to access at the measurement date.

b. Level II

Fair values are determined, directly or indirectly, using inputs that are observable for the asset or liability, either directly or indirectly.

Fair values within the Level II category are determined through the use of quoted prices in active markets, which in some cases are adjusted for factors specific to the asset or liability, such as basis, credit valuation, and location differentials.

The Corporation's commodity risk management Level II financial instruments include over-the-counter derivatives with values based on observable commodity futures curves and derivatives with inputs validated by broker quotes or other publicly available market data providers. Level II fair values are also determined using valuation techniques, such as option pricing models and regression or extrapolation formulas, where the inputs are readily observable, including commodity prices for similar assets or liabilities in active markets, and implied volatilities for options.

In determining Level II fair values of other risk management assets and liabilities and the preferred shares of TEA measured and carried at fair value, the Corporation uses observable inputs other than unadjusted quoted prices that are observable for the asset or liability, such as interest rate yield curves and currency rates. For certain financial instruments where insufficient trading volume or lack of recent trades exists, the Corporation relies on similar interest or currency rate inputs and other third-party information such as credit spreads. The fair value of the preferred shares of TEA is determined by calculating an implied price based on a current assessment of the yield to maturity.

c. Level III

Fair values are determined using inputs for the asset or liability that are not readily observable.

In estimating the fair value of the preferred shares tracking adjusted TEA amounts and the preferred shares tracking adjusted Canadian Assets amounts, the Corporation uses a discounted cash flow method, and makes estimates and assumptions about sales prices, production, capital expenditures, asset retirement costs, and other related cash inflows and outflows over the life of the facilities, as well as the remaining life of the facilities. In developing these assumptions, management uses estimates of contracted and merchant prices, anticipated production levels, planned and unplanned outages, changes to regulations, and transmission capacity or constraints for the estimated remaining life of the facilities. Appropriate discount rates reflecting the risks specific to TEA and the Canadian Assets are used in the valuations. Management also develops assumptions in respect of ongoing financing and tax positions of TEA and the Canadian Assets. These estimates and assumptions are susceptible to change from period to period and actual results can, and often do, differ from the estimates, and can have either a positive or negative impact on the estimate of the fair value of the instrument, and such differences may be material. Additional disclosures on these measurements are presented in Note 4.

Estimates of the fair value of the Class B shares liability can vary based on the estimated cost of construction and commissioning of the South Hedland facility by TEA, which could vary based on emergent or unforeseen capital needs of the project, or release of uncommitted planned contingency funds. Additional disclosures on this measurement are presented in Note 11.

II. Commodity and Other Risk Management Assets and Liabilities

The Corporation's commodity-based risk management assets and liabilities relate to trading activities and certain contracting activities. Other risk management assets and liabilities include risk management assets and liabilities that are used in hedging foreign currency exposures, including those related to the Contribution Agreement described in Note 13.

The following table summarizes the net risk management assets as at Sept. 30, 2016 and Dec. 31, 2015:

	Cash flow hedges	Non-hedges	
	Level II	Level II	Total
Net risk management assets at Sept. 30, 2016	**-**	**9**	**9**
Net risk management assets at Dec. 31, 2015	1	8	9

The change in non-hedge assets is primarily attributable to the hedge on contribution commitments, and is reflected in foreign exchange losses.

III. Financial Instruments – Not Measured at Fair Value

The fair value of financial instruments not measured and carried at fair value is as follows:

As at	Sept. 30, 2016		Dec . 31, 2015	
	Fair value Level II	Carrying value	Fair value Level II	Carrying value
MRPS	**610**	**617**	570	589
Convertible debenture (liability component)	**220**	**215**	-	-
Long-term debt(1)	**854**	**814**	803	797

(1) Includes current portion.

The fair value of the Corporation's unsecured debentures is determined using prices observed in secondary markets. The fair value of the MRPS, the liability component of the convertible debenture and other long-term debt is determined by calculating an implied price based on a current assessment of the yield to maturity.

The book value of other short-term financial assets and liabilities (cash and cash equivalents, trade and other receivables, accounts payable and accrued liabilities, and dividends payable) approximates fair value due to the liquid nature of the asset or liability.

The Corporation's investment in the preferred shares tracking earnings and distributions of TransAlta Wyoming Wind LLC continues to be measured at cost under similar conditions as described in Note 12(B)(IV) of the Corporation's most recent annual consolidated financial statements.

C. Nature and Extent of Risks Arising from Financial Instruments and Derivatives

The following discussion is limited to specific risk measures, which are more fully discussed in Note 12(C) of the Corporation's most recent annual consolidated financial statements.

I. Foreign Currency Rate Risk

The foreign currency risk sensitivities outlined below are limited to the risks that arise on financial instruments denominated in currencies other than the functional currency.

The possible effect on net earnings and OCI, due to changes in foreign exchange rates associated with financial instruments denominated in currencies other than the Corporation's functional currency, is outlined below. The sensitivity analysis has been prepared using management's assessment that an average four cent (2015 – four cent) increase or decrease in these currencies relative to the Canadian dollar is a reasonable potential change over the next quarter.

As at Sept. 30	2016		2015	
Currency	Net earnings increase(1)	OCI gain(1)	Net earnings increase(1)	OCI gain(1)
USD	3	17	-	15
AUD	23	29	23	33
Total	26	46	23	48

(1) These calculations assume an increase in the value of this currency relative to the Canadian dollar. A decrease would have the opposite effect.

II. Credit Risk

The Corporation's maximum exposure to credit risk at Sept. 30, 2016, without taking into account collateral held or right of set-off, and including indirect exposures arising from the Corporation's investment in preferred shares tracking adjusted TEA amounts and its investment in preferred shares tracking adjusted Canadian Assets amounts, is detailed as follows:

Component	Amount	Key risk assessment factors
Direct exposure		
Trade accounts receivable	32	The Corporation's counterparties were primarily investment grade. As at Sept. 30, 2016, TransAlta maintains investment grade ratings from three of four credit rating agencies. At Sept. 30, 2016, the Corporation had four unrelated customers whose outstanding balances each accounted for greater than 10 per cent of the total third-party trade accounts receivable outstanding. The Corporation has evaluated the risk of default related to these customers to be minimal.
Distributions receivable from subsidiaries of TransAlta	25	As the distribution declarations were made by paying entities and having regard to the sufficiency of funds available, the risk of default has been assessed as minimal.
MRPS	617	The MRPS form TEA's least subordinate significant form of long-term financing, which benefits from TEA's contract and counterparty profile.
Total - Direct exposure	674	
Indirect exposure		
Accounts receivable and finance lease receivable of TEA	482	TEA had one unrelated below investment grade customer whose outstanding balances accounted for 93% of total trade accounts receivable and finance lease receivable outstanding. Risk of significant loss arising from this counterparty has been assessed as low in the near term, but could increase to moderate in an environment of sustained low commodity prices over the mid- to long-term. Our assessment takes into consideration the counterparty's financial position, external rating assessments, and how TEA provides its services in an area of the counterparty's lower-cost operations, and TransAlta's other credit risk management practices.
Accounts receivable of the Canadian Assets	21	The Canadian Assets had one unrelated below investment grade customer whose outstanding balance accounted for 46% of trade accounts receivable outstanding. Risk of significant loss arising from this counterparty has been assessed as minimal.
Total	1,177	

The Corporation uses external credit ratings, as well as internal ratings in circumstances where external ratings are not available, to establish credit limits for counterparties. In certain cases, the Corporation will require security instruments such as parental guarantees, letters of credit, cash collateral or third party credit insurance to reduce overall credit risk. As at Sept. 30, 2016, no significant component of the amounts forming part of the Corporation's exposure to credit risk was either past due or impaired.

III. Other Market Risks

The Corporation is exposed to market risks based on changes in the fair value of the Class B shares, the preferred shares of TEA, and the preferred shares tracking adjusted TEA and Canadian Assets amounts. A one per cent increase (decrease) in the value of these securities would result in a $4 million decrease (increase) in net income, and a $14 million increase (decrease) in OCI.

IV. Liquidity Risk

The following table presents the contractual maturities of the Corporation's financial liabilities as at Sept. 30, 2016, including committed contributions under the terms of the Contribution Agreement:

	2016	2017	2018	2019	2020	2021 and thereafter	Total
Accounts payable and accrued liabilities	27	-	-	-	-	-	**27**
Long-term debt	22	42	235	40	40	443	**822**
Convertible debenture[(1)]	-	-	-	-	215	-	**215**
Net risk management assets	(1)	(8)	-	-	-	-	**(9)**
Interest on long-term debt[(2)]	15	35	27	19	18	81	**195**
Interest on convertible debenture[(2)]	2	10	10	10	9	-	**41**
Dividends payable	33	-	-	-	-	-	**33**
Contribution commitment[(2)]	19	231	-	-	-	-	**250**
Total	**117**	**310**	**272**	**69**	**282**	**524**	**1,574**

(1) The Corporation may settle the obligation in common shares if the holder's conversion option is not exercised.

(2) Not recognized as a financial liability on the Consolidated Statements of Financial Position.

The Corporation manages liquidity risk associated with its long-term debt and committed contributions through preparing and revising long-term external financing plans reflecting business plans and market availability of capital.

The Class B shares liability will be settled by the issuance of common shares, and accordingly, does not give rise to liquidity risk.

8. Property, Plant, and Equipment

A reconciliation of the changes in the carrying amount of property, plant & equipment ("PP&E") is as follows:

	Hydro generation	Wind generation	Capital spares and other	Total
As at Dec. 31, 2015	180	1,384	5	**1,569**
Additions	2	8	-	10
Depreciation	(5)	(44)	-	(49)
Retirements	-	(1)	-	(1)
As at Sept. 30, 2016	**177**	**1,347**	**5**	**1,529**

9. Long-Term Debt

A. Amounts Outstanding

As at	Sept. 30, 2016			Dec. 31, 2015		
	Carrying value	Face value	Interest[1]	Carrying value	Face value	Interest[1]
Credit facility[2]	-	-	-	86	86	2.84%
Unsecured debentures[3]	192	193	6.31%	230	231	6.25%
Pingston debenture	45	45	2.95%	45	45	2.95%
Melancthon-Wolfe Wind debenture	420	425	3.83%	436	442	3.83%
New Richmond debenture	157	159	3.96%	-	-	-
	814	822		797	804	
Less: current portion	(43)	(43)		(148)	(148)	
Total long-term debt	771	779		649	656	

(1) Interest rate reflects the stipulated rate or the average rate weighted by principal amounts outstanding.

(2) The Corporation has a $350 million credit facility with TransAlta (Dec. 31, 2015 - $350 million) which is available for general corporate purposes, including financing ongoing working capital requirements.

(3) Includes US$20.0 million (2015 - US$20.0 million).

In June 2016, the Corporation issued a $159 million bond ("New Richmond bond") that bears interest at 3.963 per cent, with principal and interest payable semi-annually in blended payments until maturity on June 30, 2032. The New Richmond bond is secured by a first ranking charge over all the assets of the issuer, the New Richmond Wind L.P.

Unsecured debentures of $10 million were redeemed in June 2016, resulting in a net loss on the transaction of $1 million, which is included in net interest expense (See Note 5).

In June 2016, the $27 million 5.69 per cent non-recourse unsecured debenture matured and was paid out using existing liquidity.

In June 2016, the Corporation made a scheduled semi-annual $17 million principal payment on the Melancthon-Wolfe Wind debenture.

B. Restrictions

Unsecured debentures include restrictive covenants requiring the cash proceeds received from the sale of certain assets to be reinvested into similar renewable assets or in the repayment of the non-recourse debentures.

The Melancthon-Wolfe Wind, Pingston, and New Richmond bonds are subject to customary financing conditions and covenants that restrict the Corporation's ability to access funds generated by the facilities' operations. Upon meeting certain distribution tests, typically performed once per quarter, the funds are able to be distributed by the subsidiary entities to their respective parent entity.

C. Security

The Melancthon-Wolfe Wind, Pingston, and New Richmond bonds are secured by a first ranking charge over all of the respective assets, including PP&E with a total carrying amount of $877 million, of the Corporation's subsidiaries that issued the bonds, being Melancthon-Wolfe Wind L.P., Pingston Power Inc., and New Richmond Wind L.P., respectively.

10. Convertible Debenture

As part of the Canadian Assets investment, the Corporation issued a $215 million convertible unsecured subordinated debenture to TransAlta. The debenture is on an interest-only basis at a coupon rate of 4.5 per cent per annum, payable semi-annually in arrears on June 30 and Dec. 31, and will mature on Dec. 31, 2020. On the maturity date, TransAlta will have the right, at its sole option, to convert the outstanding principal amount of the debenture, in whole or in part, into common shares of the Corporation at a conversion price of $13.16 per common share. If TransAlta does not exercise its conversion option, the Corporation may satisfy the principal obligation through issuance of common shares with a unit value corresponding to 95 per cent of the then-current share value. The debenture is a direct unsecured obligation of the Corporation ranking subordinate to all liabilities, except liabilities which by their terms rank in rights of payment equally with or subordinate to the debenture. The debenture ranks equal with all subordinate debentures issued by the Corporation from time to time. The equity component of the debenture was estimated to have a value of nil upon issuance.

At the issue date, the fair value of the liability component of the convertible debenture was assessed in order to determine the residual value, if any, to assign to the holder conversion right, being an equity component of the debenture. Based on an assessment of the yield to maturity of similar debt instruments with no conversion feature, a Level II measurement, the Corporation evaluated that the fair value of the liability component of the debenture approximated $215 million. Accordingly, no value was assigned to the equity conversion feature.

11. Class B Shares

As at Sept. 30, 2016, there were 26 million Class B shares outstanding (Dec. 31, 2015 – 26 million). The Class B shares provide voting rights equivalent to the common shares, are non-dividend paying, and will convert to common shares when the South Hedland facility is fully commissioned. The number of common shares that TransAlta will receive on the conversion of the Class B shares will be adjusted based on the actual amount that the Corporation funds for the construction and commissioning of the South Hedland facility relative to the budgeted costs. In the event that the construction amount funded by the Corporation exceeds the budgeted costs, TransAlta will receive fewer common shares upon conversion and, comparably, TransAlta will receive more common shares in the event that the Corporation funds less than the budgeted costs.

As the Class B shares are convertible into common shares at a variable rate, they are classified as liabilities and their change in value is recognized in net earnings. Changes in the value of the Class B shares are unrealized and relate to the change in value of underlying common shares during the period, net of the effect of estimated foregone dividends, as discounted using a risk-free rate for the period to conversion.

The estimated commissioning date and total costs for the construction of the South Hedland facility are based on significant assumptions relating to unobservable inputs, any one of which may materially affect the estimates. As at Sept. 30, 2016, commissioning is anticipated as scheduled and costs were estimated to be at target. A one per cent increase or decrease in costs would result in a $5 million corresponding decrease or increase in fair value, respectively. A one-month delay or acceleration in achieving commissioning would result in a corresponding $2 million decrease or increase in fair value, respectively.

12. Common Shares

A. Authorized and Outstanding

The Corporation is authorized to issue an unlimited number of common shares without nominal or par value and an unlimited number of preferred shares. The common shares entitle the holders thereof to one vote per share at meetings of shareholders. The preferred shares are issuable in series and have such rights, restrictions, conditions, and limitations as the Board of Directors (the “Board”) may from time to time determine. No preferred shares have been issued.

The change in issued and outstanding common shares during the nine months ended Sept. 30, 2016 and 2015 are as follows:

	9 months ended Sept. 30			
	2016		2015	
	Common shares *(millions)*	Amount *(millions)*	Common shares *(millions)*	Amount *(millions)*
Issued and outstanding, beginning of period	**191**	**2,152**	115	1,224
Issued to TransAlta	**15**	**152**	58	711
Public offering(1)	**18**	**165**	18	217
Issued and outstanding, end of period	**224**	**2,469**	191	2,152

(1) 2016 is net of issuance costs of $8 million ($10 million issuance costs, less tax effects of $2 million) and 2015 is net of issuance costs of $8 million ($11 million issuance costs, less tax effects of $3 million).

B. Dividends

The declaration of dividends on the Corporation's common shares is at the discretion of the Board.

The following table summarizes the common share dividends declared within the nine months ended Sept. 30, 2016 and 2015, excluding dividend equivalent payments described in Note 3.

Dividends declared	Total dividends per share	Total dividends	TransAlta	Other shareholders
Period ended September 30, 2016	**0.66330**	**150**	**89**	**61**
Period ended September 30, 2015	0.61248	102	74	28

C. Diluted Earnings per Share

The Corporation's potentially dilutive instruments include the 26 million Class B shares, which are convertible into common shares as outlined in Note 11, and the $215 million debenture, which is convertible at TransAlta's option into 16.3 million common shares on the maturity date. As at Sept. 30, 2016, the conditions related to the potential conversion of Class B shares into the Corporation's common shares have not been met. The potential shares associated with the convertible debenture are antidilutive on a year-to-date basis due to the loss position. For the quarter, there is no dilutive effect on earnings per share from the convertible debenture.

13. Commitments and Contingencies

A. Litigation

In the normal course of business, the Corporation may become party to litigation claims. There are currently no known claims that the Corporation has determined as significant enough to require disclosure.

B. Guarantees

As part of the Transaction, the Corporation entered into a Guarantee and Indemnification Agreement in favour of TransAlta related to certain guarantees TransAlta has provided to third parties in respect of certain obligations of TEA (the "TEA Guarantees"). The Corporation has agreed to indemnify TransAlta from and against all claims, actions, proceedings, liabilities, losses, costs, expenses, or damages against or incurred by TransAlta arising out of or in connection with the TEA Guarantees and to reimburse TransAlta in full for the amount of any payment made by TransAlta under and in accordance with the TEA Guarantees, relating to actions, omissions, events, and circumstances that occur. As at Sept. 30, 2016, the total amounts guaranteed by the Corporation were $993 million (Dec. 31, 2015 - $1,013 million).

C. Commitments

As at Sept. 30, 2016, the remaining costs under the South Hedland contribution agreement are estimated to be approximately $267 million (AUD$276 million). Refer to Note 4 of the Corporation's most recent annual consolidated financial statements for additional information on the contribution agreement.

On July 5, 2016, the Corporation renewed the long-term service agreements at two of our wind farms for a period of five years each, commencing August 2016. Total committed expenditures under the extensions are approximately $27 million.

14. Related Party Transactions and Balances

The Corporation has entered into certain agreements and transactions with TransAlta which are discussed in more detail in Note 24 of the Corporation's most recent annual consolidated financial statements.

A. Related Party Transactions

Related party transactions include the finance income related to subsidiaries of TransAlta (Note 4). Also, all financial instruments and derivatives that relate to the Corporation are entered into on behalf of the Corporation by a subsidiary of TransAlta.

Significant related party transactions that are not otherwise presented elsewhere consist of the following:

	3 months ended Sept. 30		9 months ended Sept. 30	
	2016	2015	**2016**	2015
Revenue from TransAlta PPAs	**7**	7	**27**	24
Revenue from green attributes[1]	**-**	-	**-**	2
G&A Reimbursement Fee[2]	**4**	3	**12**	8
Interest expense	**2**	3	**8**	9
Realized foreign exchange loss on hedge contribution commitment	**-**	1	-	1

(1) The value of the green attributes was determined by reference to market information for similar instruments, including historical transactions with third parties, with the transaction ultimately reviewed and approved by the Corporation's independent members of the Board of Directors.

(2) Includes portion charged directly to the Wyoming wind farm and a 2016 increase due to the investment in the Canadian Assets.

All of these transactions are with TransAlta or subsidiaries of TransAlta.

B. Related Party Balances

Related party balances include the investments in subsidiaries of TransAlta disclosed in Note 4, the risk management assets and liabilities disclosed in Note 7, the credit facility disclosed in Note 9, the convertible debenture disclosed in Note 10, the Class B shares liability disclosed in Note 11, and the guarantees provided by the Corporation on behalf of TransAlta and TEA disclosed in Note 13.

Significant related party balances that are not otherwise presented elsewhere consist of the following:

As at	Sept. 30, 2016	Dec. 31, 2015
Trade and other receivables	**34**	30
Accounts payable and accrued liabililities (including interest payable)	**5**	4
Dividends payable	**20**	17
Letters of credit issued by TransAlta on behalf of the Corporation	**59**	31
Guarantees provided by TransAlta on behalf of the Corporation	**40**	226

All of these balances are with TransAlta or subsidiaries of TransAlta.

Glossary of Key Terms

Australian Assets – TransAlta's 425 MW Australian gas-fired generation assets that are fully operational and contracted under long-term contracts, and the 150 MW South Hedland facility, currently under construction, as well as the 270 kilometre Fortescue River Gas Pipeline.

Australian Mandatory Redeemable Preferred Shares ("MRPS") – Non-voting and rank subordinate to all present and future secured and unsecured indebtedness but senior to all other classes of issued and outstanding shares in the capital of the Australian subsidiary. The MRPS have a stated dividend rate of 7.4%.

Australian Tracking Preferred Shares – Preferred shares of a TransAlta subsidiary, which provide cumulative variable dividends broadly equal to the underlying net distributable profits of TEA.

Canadian Assets – TransAlta's 506 MW Sarnia cogeneration plant, 97 MW Le Nordais wind farm, and 8 MW Ragged Chute hydro facility that are fully operational and contracted under long-term contracts. The assets are located in Ontario and Quebec.

Capacity - The rated continuous load-carrying ability, expressed in megawatts, of generation equipment.

CDN Tracking Preferred Shares - Preferred shares of a TransAlta subsidiary, which provide cumulative variable dividends broadly equal to the underlying net distributable profits of the Canadian Assets.

Credit Facility - A $350 million unsecured credit facility with TransAlta. The facility is available for general corporate purposes, including financing ongoing working capital requirements.

G&A Reimbursement Fee - The fee payable to TransAlta under the Management, Administrative and Operational Services Agreement to compensate TransAlta for the provision of all the general administrative services as may be required or advisable for the management of the affairs of the Corporation.

Gigawatt - A measure of electric power equal to 1,000 megawatts.

Gigawatt Hour (GWh) - A measure of electricity consumption equivalent to the use of 1,000 megawatts of power over a period of one hour.

Greenhouse Gas (GHG) - Gases having potential to retain heat in the atmosphere, including water vapour, carbon dioxide, methane, nitrous oxide, hydrofluorocarbons, and perfluorocarbons.

Green Attributes – Renewable Energy Certificates and Carbon Offsets, or other tradable or saleable instruments that represent the property rights to the environmental, social, and other nonpower qualities of renewable electricity generation that can be sold separately from the underlying physical electricity.

Megawatt (MW) - A measure of electric power equal to 1,000,000 watts.

Megawatt Hour (MWh) - A measure of electricity consumption equivalent to the use of 1,000,000 watts of power over a period of one hour.

Net Maximum Capacity - The maximum capacity or effective rating, modified for ambient limitations, that a generating unit or power plant can sustain over a specific period, less the capacity used to supply the demand of station service or auxiliary needs.

PPA – A power purchase and sale agreement between a power generator and a third party acquirer of electricity.

TransAlta Energy (Australia) Pty Ltd (TEA) – An Australian subsidiary of TransAlta.

TransAlta PPAs - PPAs between TransAlta and the Corporation providing for the purchase by TransAlta, for a fixed price, all of the power produced by certain wind and hydro facilities. The initial price payable in 2013 by TransAlta for output was $30.00/MWh for wind facilities and $45.00/MWh for hydro facilities, which amounts are adjusted annually for changes in the Consumer Price Index.

Unplanned Outage - The shutdown of a generating unit due to an unanticipated breakdown.

Wyoming Wind – TransAlta's 144 MW wind farm in Wyoming.

TransAlta renewables inc.

TransAlta Renewables Inc.
110 - 12th Avenue S.W.
Box 1900, Station "M"
Calgary, Alberta Canada T2P 2M1
Phone
403.267.7110

Website
www.transaltarenewables.com

CST Trust Company
P.O. Box 700 Station "B"
Montreal, Québec
H3B 3K3
Phone
Toll-free in North America: 1.800.387.0825
Toronto/outside North America: 416.682.3860
E-mail
inquiries@canstockta.com

Fax
514.985.8843
Website
www.canstockta.com

Additional Information
Requests can be directed to:

Investor Inquiries

Phone
1.800.387.3598 in Canada and United States
or 403.267.2520
E-mail
investor_relations@transalta.com

Media Inquiries
Toll-free 1.855.255.9184
or 403.267.2540