CAPSTONE INFRASTRUCTURE CORPORATION

Financial Report for the Quarter Ended June 30, 2012

FINANCIAL HIGHLIGHTS

PERFORMANCE MEASURES

Earnings Measures ($000s)	Three months ended Jun 30, 2012	Three months ended Jun 30, 2011	Six months ended Jun 30, 2012	Six months ended Jun 30, 2011
Revenue	85,849	37,028	178,005	83,943
Net income (loss)	(609)	(30,370)	15,575	10,962
Basic earnings per share	(0.073)	(0.492)	0.093	0.180

Cash Flow Measures ($000s)	Three months ended Jun 30, 2012	Three months ended Jun 30, 2011	Six months ended Jun 30, 2012	Six months ended Jun 30, 2011
Cash flows from operating activities	23,879	(8,353)	55,100	5,764
Adjusted EBITDA [1]	27,605	(6,570)	64,909	11,299
Adjusted funds from operations ("AFFO") [1]	3,707	(13,888)	18,623	(403)
Payout ratio (before internalization costs)	276.0%	216.3%	121.0%	107.4%

(1) These performance measures are not defined by International Financial Reporting Standards ("IFRS"). Please see page 6 and 7 for a definition of each measure.

Capital Structure – At Fair Value ($000s)	Jun 30, 2012	Dec 31, 2011
Long-term debt – power	312,775	314,196
Long-term debt – utilities – water [1]	252,980	353,135
Long-term debt – corporate	44,031	155,124
Common shares	288,966	270,348
Class B exchangeable units	13,030	12,380
Preferred shares	57,000	52,500
Debt to capitalization	62.9%	71.0%

(1) Calculated as 50% proportionate share based on ownership interest (December 31, 2011 - 70%).

INVESTOR INFORMATION

Quick Facts	
Common shares outstanding	72,061,230
Preferred shares outstanding	3,000,000
Convertible debentures outstanding	42,749
Class B exchangeable units	3,249,390
Securities symbols and exchange	Toronto Stock Exchange: CSE, CSE.PR.A, CSE.DB.A

QUARTERLY TRADING INFORMATION

	High	Low	Closing	Average Daily Trading Volume
Common shares	$4.15	$3.72	$4.01	272,000
Preferred shares	$19.24	$16.66	$19.00	3,054
Convertible debentures	$108.49	$99.51	$103.00	492

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LEGAL NOTICE

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

CAUTION REGARDING FORWARD-LOOKING STATEMENTS

Certain of the statements contained within this document are forward-looking and reflect management's expectations regarding the future growth, results of operations, performance and business of Capstone Infrastructure Corporation (the "Corporation") based on information currently available to the Corporation. Forward-looking statements and financial outlook are provided for the purpose of presenting information about management's current expectations and plans relating to the future and readers are cautioned that such statements and financial outlook may not be appropriate for other purposes. These statements and financial outlook use forward-looking words, such as "anticipate", "continue", "could", "expect", "may", "will", "estimate", "plan", "believe" or other similar words. These statements and financial outlook are subject to known and unknown risks and uncertainties that may cause actual results or events to differ materially from those expressed or implied by such statements and financial outlook and, accordingly, should not be read as guarantees of future performance or results. The forward-looking statements and financial outlook within this document are based on information currently available and what the Corporation currently believes are reasonable assumptions, including the material assumptions set out in the management's discussion and analysis of the results of operations and the financial condition of the Corporation ("MD&A") for the year ended December 31, 2011 under the heading "Results of Operations", as updated in subsequently filed interim MD&A of the Corporation (such documents are available under the Corporation's profile on www.sedar.com).

Other material factors or assumptions that were applied in formulating the forward-looking statements and financial outlook contained herein include or relate to the following: that the business and economic conditions affecting the Corporation's operations will continue substantially in their current state, including, with respect to industry conditions, general levels of economic activity, regulations, weather, taxes and interest rates; the contribution from the UK water utility ("Bristol Water") reflecting the Corporation's reduced ownership interest as at May 10, 2012; a TransCanada Pipelines ("TCPL") gas transportation toll of approximately $2.24 per gigajoule in 2012; no material change in the level of gas mitigation revenue earned by the Cardinal facility; that there will be no unplanned material changes to the Corporation's facilities, equipment or contractual arrangements, no unforeseen changes in the legislative, regulatory and operating framework for the Corporation's businesses, no delays in obtaining required approvals, no unforeseen changes in rate orders or rate structures for the Corporation's power infrastructure facilities, Swedish district heating business ("Värmevärden") or Bristol Water, no unfavourable changes in environmental regulation and no significant event occurring outside the ordinary course of business; the refinancing of the Corporation's Capstone Power Corporation-Cardinal Power credit facility; that there will be no further amendments by the Ontario government to the regulations governing the mechanism for calculating the Global Adjustment (which affects the calculation of the price escalators under each power purchase agreement (a "PPA") for the Cardinal facility and the hydro power facilities located in Ontario); the accounting treatment for Bristol Water's business under International Financial Reporting Standards, particularly with respect to accounting for maintenance capital expenditures; no material change to the amount and timing of capital expenditures by Bristol Water; no material change to the Swedish Krona to Canadian dollar exchange rate; no material change to the UK pound sterling to Canadian dollar exchange rate; and that Bristol Water will operate and perform in a manner consistent with the regulatory assumptions underlying its current asset management plan, including, among others: real and inflationary increases in Bristol Water's revenue, Bristol Water's expenses increasing in line with inflation, and capital investment, leakage, customer service standards and asset serviceability targets being achieved.

Although the Corporation believes that it has a reasonable basis for the expectations reflected in these forward-looking statements and financial outlook, actual results may differ from those suggested by the forward-looking statements and financial outlook for various reasons, including risks related to: variability and payments of dividends on the Corporation's common shares, which are not guaranteed; volatile market price for the Corporation's securities; availability of debt and equity financing; default under credit agreements; credit risk, prior ranking indebtedness and absence of covenant protection for holders of the Corporation's convertible debentures; dependence on subsidiaries and investees; acquisitions; geographic concentration and non-diversification; foreign exchange risk; reliance on key personnel; insurance; shareholder dilution; derivatives risks; changes in legislation and administrative policy; competition; private companies and illiquid securities; operational performance; PPAs; fuel costs and supply; contract performance; Amherstburg Solar Park technology risk; land tenure and related rights; environmental, health and safety regime; regulatory regime and permits; force majeure; influence of the UK water regulator ("Ofwat") price determinations; failure of Bristol Water to deliver capital investment programs; failure of Bristol Water to deliver water leakage target; Ofwat's introduction of the Service Incentive Mechanism and the serviceability assessment; economic environment, inflation and capital market conditions; pension plan obligations; operational risks; competition; default under Bristol Water's artesian loans, bonds, debentures and credit facility; seasonality and climate change; labour relations; special administration; general risks inherent in the district heating sector; industrial and residential contracts; default under Värmevärden's bonds; and minority interest. Further information regarding these risk factors is contained in the Corporation's Annual Information Form (which is available under the Corporation's profile on www.sedar.com).

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

MESSAGE TO SHAREHOLDERS

I am pleased to report on Capstone Infrastructure's second quarter results and recent activities.

Operationally, our portfolio performed strongly in the second quarter of the year, reflecting contributions from Bristol Water, Värmevärden and Amherstburg Solar Park. Our newest businesses contributed to revenue increases of 131.8% and 112.1% in the second quarter and first six months of the year, respectively, over the same periods in 2011. Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) was also positively affected, with increases of 129.3% and 112.5% in the quarter and year-to-date periods, respectively (excluding internalization costs). These increases were partially offset by lower revenue at Cardinal as a result of a 15-day planned maintenance outage compared with a six-day outage last year and lower revenue at Erie Shores Wind Farm due to poor wind conditions in the quarter.

These factors were also a primary cause of lower Adjusted Funds from Operations (AFFO), which decreased by 21.5% and 1.2% in the quarter and year-to-date periods, respectively. Other significant factors affecting AFFO were higher interest payments and higher scheduled debt repayments at certain of our power facilities and higher corporate costs (excluding internalization costs), including increased administrative expenses due to professional fees. Our operational and financial performance is described in detail on pages 9 to 19 of this report.

During the quarter, we made significant progress on our strategic priorities for 2012, which were to refinance our debt maturing in 2012, set a new dividend policy and obtain a new power purchase agreement (PPA) for Cardinal.

On the first priority, we have now addressed virtually all the debt maturing in 2012 through the recapitalization of Värmevärden and our hydro power facilities, and the sale of a 20% interest in Bristol Water. We have also secured a commitment from our existing lender to refinance the remaining approximately $12 million outstanding under the CPC-Cardinal credit facility, which matures on September 28, 2012. All of the debt at our power facilities and Bristol Water is secured at the asset level and is non-recourse to Capstone.

Notably, our outstanding debt is largely fixed-rate. Virtually all of the debt at our power facilities is fully amortizing over their power purchase agreement (PPA) terms with only Amherstburg requiring refinancing prior to the expiry of its PPA. This represents a significant strengthening of our balance sheet that will allow us to get back to our growth mandate.

Our second priority for 2012 was to establish our new common share dividend policy, which we completed in early June. Our new dividend of 30 cents per share annually, payable quarterly, is based on our expectations for Capstone's cash flow after Cardinal's PPA expires at the end of 2014. The new dividend reflects what we believe are conservative assumptions about possible outcomes at Cardinal. It also provides a buffer in the unlikely event that we receive a worse outcome on Cardinal than we expect, or if we experience unforeseen events in our business. With our new dividend, we are targeting a long-term payout ratio of 70% to 80% of AFFO, which allows us to retain cash that can be reinvested in new growth opportunities. We intend for our new dividend to be a secure foundation from which to grow as we build Capstone's scope, scale and value.

Our third priority is to complete a new contract at Cardinal that recognizes its high quality and importance from electricity, industrial, economic, social and community perspectives. Our dialogue with the Ontario Power Authority, along with other key government ministries, is continuing and we are striving to find the optimal balance between value for our industrial partner, value for Ontario ratepayers and value for our shareholders. While there can be no assurances, we believe that a new contract is achievable in 2012.

Achieving operational excellence across our businesses is an ongoing emphasis for us, including finding improvements and opportunities with the potential to incrementally increase cash flow. These initiatives include the sale of renewable energy credits at Whitecourt, which has delivered approximately $600,000 in revenue in the first six months of 2012. We are exploring similar value-enhancing opportunities across our other renewable power facilities.

Growth is likewise a key imperative for Capstone. We enjoy strong footholds in the contracted power, renewable power, water utility and district heating sectors and are seeking opportunities to build upon these platforms in Canada and internationally, including through acquisitions or development partnerships. The Capstone team has decades of experience in acquiring, financing and managing infrastructure businesses, and our growth strategy is guided by the following principles:

- Building scale with quality assets, including a blend of operating businesses and development-stage projects;

- Seeking to diversify the portfolio by infrastructure category and jurisdiction; and
- Focusing on wholly-owned assets while remaining open to partnering opportunities that are accompanied by strong governance and relationships, such as those we enjoy with AGBAR and ITOCHU Corporation at Bristol Water.

Capstone's mission is to build and responsibly manage a high quality portfolio of infrastructure businesses in Canada and internationally in order to deliver a superior total return to our shareholders by providing reliable income and capital appreciation. We have a solid foundation from which to realize that mission, including a new utilities segment that features perpetual and growing cash flow to complement our power generation facilities, a substantially lower risk profile in terms of our asset mix and balance sheet, and a broader international reach, which is an important point of differentiation from our traditional peer group here in Canada.

We have greatly appreciated the support of our shareholders over the past few months as we addressed our challenges. With your investment in Capstone, you own exceptionally high quality core infrastructure assets that deliver essential services throughout the economic cycle, resulting in reliable, long-term cash flow. You are also poised to benefit from our company's growth as we work to capitalize on the huge infrastructure investment opportunity before us.

We expect a bright future for our company and look forward to updating you on our progress.

Sincerely,

Michael Bernstein
President and Chief Executive Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS

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INTRODUCTION

Management's discussion and analysis ("MD&A") summarizes the Corporation's consolidated operating results for the three and six months ended June 30, 2012 and consolidated cash flows for the six months ended June 30, 2012 with corresponding comparative prior periods and the Corporation's financial position as at June 30, 2012 and December 31, 2011. This MD&A should be read in conjunction with the accompanying unaudited interim consolidated financial statements of the Corporation and notes thereto as at and for the three and six months ended June 30, 2012 and the financial statements and MD&A for the year ended December 31, 2011. Additional information about the Corporation can be found in its other public filings, specifically the Corporation's Annual Information Form dated March 21, 2012 and most recent Annual Report for the year ended December 31, 2011. These filings are available under the Corporation's profile on the Canadian Securities Administrators' System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com. The information contained in this MD&A reflects all material events up to August 13, 2012, the date on which this MD&A was approved by the Corporation's Board of Directors.

BASIS OF PRESENTATION

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

Amounts included in the interim consolidated financial statements of each entity in the Corporation are measured using the currency of the primary economic environment in which the entity operates ("functional currency"). The interim consolidated financial statements are presented in Canadian dollars ("presentation currency"), which is Capstone's functional currency. The exchange rates used in the translation to the presentation currency are as follow:

As at and for the periods ended	Swedish Kronor (SEK)		Pound Sterling (£)	
($000s)	Average	Spot	Average	Spot
December 31, 2011	0.1525 (1)	0.1478	1.6075 (2)	1.5799
Quarter ended March 31, 2012	0.1483	0.1509	1.5732	1.5970
Quarter ended June 30, 2012	0.1454	0.1474	1.5986	1.5984

(1) Nine month period from acquisition on March 31, 2011 to December 31, 2011.

(2) Period from acquisition on October 5, 2011 to December 31, 2011.

CHANGES IN THE BUSINESS

In the first half of 2012, Capstone completed multiple initiatives to address maturing debt and position the company for future growth. As at December 31, 2011, Capstone had $230,899 (including $23,698 at Bristol Water) of debt maturing in 2012, nearly all of which was repaid or refinanced through proceeds from the Värmevärden recapitalization, partial sale of Bristol Water and new financing at the hydro facilities. Following these events, the Corporation set a new dividend policy.

Värmevärden Recapitalization

In March 2012, the district heating business, Värmevärden, was recapitalized by issuing approximately $150,000 (1,000,000 SEK) of senior secured bonds to institutional investors. Värmevärden repaid a portion of the shareholder loans from the bond proceeds. Capstone received $49,400, representing its one-third interest in Värmevärden. Capstone used these proceeds to repay a portion of its senior debt facility. As a result of the return to Capstone of the bond proceeds, Capstone's total investment in Värmevärden was reduced to $52,028, comprising $34,336 in loans receivable and $17,692 in equity accounted investment.

Sale of Partial Interest in Bristol Water

On May 10, 2012, Capstone sold to I-Environment Investments Ltd, a subsidiary of ITOCHU Corporation, a 20% indirect interest in Bristol Water plc. I-Environment Investments Ltd acquired a 2/7ths ownership interest in CSE Water UK Limited, which indirectly owned a 70% interest in Bristol Water plc. Capstone received $69,213 of net proceeds from the sale and used the funds to repay the remaining $28,975 on the senior debt facility and $39,000 on the CPC-Cardinal credit facility, retaining cash of $1,238.

Following this sale, Capstone retained a 50% indirect interest in Bristol Water and continues to consolidate based on retention of control. In accordance with IFRS, Capstone recorded the transaction as a transfer of equity to non-controlling interest holders. The excess net proceeds of $15,955 over the value of the transfer of equity to the non-controlling interest and $850 of taxes were recorded directly to retained earnings.

Financing of Hydro Facilities

On June 6, 2012, MPT Hydro LP, an indirect wholly-owned subsidiary of Capstone, which owns the Dryden. Hluey Lakes, Sechelt and Wawatay hydro facilities (the "Hydro facilities"), completed a $100,621 debt offering to recapitalize the hydro facilities. The debt offering comprised $80,379 of senior secured bonds and $20,242 of subordinated secured bonds.

Proceeds from the offering were first used to repay the $27,239 balance of levelization debt at the Wawatay hydro facility along with $1,785 of transaction costs, which were capitalized to the debt. In addition, Capstone cash funded $3,846 for debt service and maintenance reserve accounts in accordance with the bond indenture and used the $67,700 net proceeds to repay a portion of the CPC-Cardinal credit facility.

New Dividend Policy

On June 1, 2012, the Board of Directors of the Corporation established a new dividend policy whereby the Corporation intends to pay $0.075 per common share quarterly or $0.30 per common share annually.

As negotiations with the Ontario Power Authority have progressed but not yet concluded, the Corporation's new dividend policy reflects management's view on current Ontario power market and fiscal dynamics and its expectation for the cash flow Cardinal will generate following the expiry of its current power purchase agreement at the end of 2014. The Corporation's dividend policy is determined by the Board of Directors of the Corporation and is based on the Corporation's cash flows, earnings, financial requirements, the satisfaction of solvency tests imposed under corporate law for the declaration of dividends and other relevant factors. With the implementation of the new dividend policy, the Corporation expects to retain additional cash that can be reinvested in new growth opportunities.

NON-GAAP AND ADDITIONAL GAAP PERFORMANCE MEASURE DEFINITIONS

While the accompanying interim consolidated financial statements have been prepared in accordance with IFRS, this MD&A also contains figures that are performance measures not defined by IFRS. These non-GAAP and additional GAAP performance measures do not have any standardized meaning prescribed by IFRS and are, therefore, unlikely to be comparable to similar measures presented by other issuers. The Corporation believes that these indicators are useful since they provide additional information about the Corporation's earnings performance and cash generating capabilities and facilitate comparison of results over different periods. The non-GAAP and additional GAAP measures used in this MD&A are defined below.

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

EBITDA is net income (loss), including that net income (loss) related to the non-controlling interest ("NCI") and interest income excluding interest expense, income taxes, depreciation and amortization. EBITDA represents Capstone's continuing capacity to generate income from operations before taking into account management's financing decisions and costs of consuming tangible capital assets and intangible assets, which vary according to their vintage, technological currency, and management's estimate of their useful life. EBITDA is presented on the consolidated statement of income.

Adjusted EBITDA

Adjusted EBITDA is calculated as revenue less operating and administrative expenses plus interest income and dividends or distributions received from equity accounted investments. Amounts attributed to any non-controlling interest are deducted. Adjusted EBITDA for the investment in Bristol Water is included at Capstone's proportionate ownership interest. For the period from October 5, 2011 to May 10, 2012, Capstone's 70% ownership interest was reduced to 50% upon the partial sale of Bristol Water on May 10, 2012. Adjusted EBITDA is reconciled to EBITDA by removing equity accounted income, other gains and losses (net), foreign exchange gains and losses, and adding in dividends or distributions from equity accounted investments.

Adjusted Funds from Operations ("AFFO")

Capstone's definition of AFFO measures cash generated by activities of infrastructure business investments which is available for dividends and general corporate purposes. For wholly owned businesses, AFFO is equal to Adjusted EBITDA less interest paid, repayment of principal on debt income, taxes paid and maintenance capital expenditures. For businesses that are not wholly owned and cash generated by the business is only available to Capstone through periodic dividends, AFFO is equal to dividends received. Also deducted are corporate expenses and dividends on preferred shares.

AFFO is calculated from Adjusted EBITDA by:

Deducting: - Adjusted EBITDA generated from businesses with significant non-controlling interests
Adding: - Dividends received from businesses with significant non-controlling interests
- Scheduled repayments of principal on loans receivable from equity accounted investments

Deducting items, for businesses without significant non-controlling interests:

- Interest paid
- Income taxes paid
- Dividends paid on the preferred shares included in shareholders' equity
- Maintenance capital expenditure payments and
- Scheduled repayments of principal on debt, net of changes to the levelization liability up to repayment on June 6, 2012.

Payout Ratio

Payout ratio measures the proportion of cash generated that is available at corporate that is paid as dividends. The payout ratio is calculated as dividends declared divided by AFFO.

Reconciliation of Non-GAAP Performance measures

The following table reconciles Adjusted EBITDA and AFFO to the nearest GAAP measures:

	Three months ended		Six months ended	
($000s)	Jun 30, 2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
EBITDA	32,934	(13,161)	80,002	4,180
Foreign exchange (gain) loss	652	627	(452)	633
Other gains and losses (net)	2,163	4,489	760	2,610
Equity accounted (income) loss	602	1,475	(843)	3,876
Distributions from equity accounted investments	983	-	983	-
NCI portion of Adjusted EBITDA	(9,729)	-	(15,541)	-
Adjusted EBITDA	27,605	(6,570)	64,909	11,299
Cash flow from operating activities	23,879	(8,353)	55,100	5,764
Bristol Water cash flow from operating activities	(15,521)	-	(31,884)	-
Bristol Water dividends paid to Capstone	4,868	-	4,868	-
Värmevärden distributions paid to Capstone	983	-	983	-
Foreign exchange on loans receivable from Värmevärden	(145)	627	(536)	633
Chapais loans receivable principal repayments	243	218	479	430
Power maintenance capital expenditures	(2,857)	(1,883)	(3,326)	(2,684)
Power and corporate scheduled principal repayments	(5,364)	(1,112)	(6,646)	(1,580)
Power and corporate working capital changes	(1,441)	(3,385)	1,461	(2,966)
Dividends on redeemable preferred shares	(938)	-	(1,876)	-
AFFO	3,707	(13,888)	18,623	(403)

RESULTS OF OPERATIONS

Overview

For both the second quarter and the six months ended June 30, 2012, excluding internalization costs, Capstone's results reflect a substantial increase in Adjusted EBITDA and a marginal decline in AFFO from 2011. These results are reflected in the following table.

	Three months ended		Six months ended	
($000s)	**Jun 30, 2012**	**Jun 30, 2011**	**Jun 30, 2012**	**Jun 30, 2011**
Revenue	85,849	37,028	178,005	83,943
Expenses	(50,541)	(45,491)	(101,413)	(74,970)
Interest income	1,043	1,893	2,875	2,326
Distributions from equity accounted investments	983	-	983	-
Less: non-controlling interest ("NCI")	(9,729)	-	(15,541)	-
Adjusted EBITDA	27,605	(6,570)	64,909	11,299
Adjusted EBITDA of consolidated businesses with NCI	(13,712)	-	(27,273)	-
Dividends from businesses with non-controlling interests	4,868	-	4,868	-
Principal from loans receivable	243	218	479	430
Interest paid	(6,045)	(4,533)	(12,083)	(7,860)
Dividends paid on Capstone's preferred shares	(938)	-	(1,876)	-
Income taxes (paid) recovery	(93)	(8)	(429)	(8)
Maintenance capital expenditures	(2,857)	(1,883)	(3,326)	(2,684)
Scheduled repayment of debt principal	(5,364)	(1,112)	(6,646)	(1,580)
AFFO	3,707	(13,888)	18,623	(403)
Internalization costs	-	18,611	-	19,246
AFFO before internalization costs	3,707	4,723	18,623	18,843
Before internalization costs				
AFFO per share	0.049	0.076	0.249	0.309
Payout ratio	276.0%	216.3%	121.0%	107.4%
Dividends declared per share	0.135	0.165	0.300	0.330

Revenue for the second quarter was $48,821, or 132%, higher than in 2011 and $94,062, or 112%, higher on a year-to-date basis. The increases were primarily due to Bristol Water, which contributed $45,717 and $87,230 in the second quarter and year to date, respectively.

Expenses for the second quarter were $5,050, or 11.1%, higher than in 2011 and $26,443, or 35.3%, higher on a year-to-date basis including internalization costs incurred in 2011. Excluding these costs, expenses in the quarter were $23,611, or 88.0%, higher than in 2011 and $45,689, or 82.0%, higher on a year-to-date basis. The increase was primarily attributable to Bristol Water, which added $22,509 and $44,973 in the second quarter and year to date, respectively.

Interest income decreased by $850, or 44.9%, for the quarter and increased by $549, or 23.6%, on a year-to-date basis. The decrease in the second quarter was primarily attributable to Värmevärden, due to a $48,100 reduction in the shareholder loan balance following repayment from the new bond proceeds. In the year-to-date period, this impact was offset by the absence of interest income from Värmevärden during the first quarter of 2011 as the business was acquired on March 31, 2011. The remaining difference was attributable to interest income variances on cash balances at Bristol Water and corporate.

Interest paid increased by $1,512, or 33.4%, for the quarter and $4,223, or 53.7%, on a year-to-date basis. The increases were due to additional interest costs primarily at Amherstburg and at corporate for bridge financing to fund the acquisition of Bristol Water. Interest paid by Bristol Water is excluded from Capstone's definition of AFFO and is the primary difference between interest expense included in consolidated net income (loss) and interest paid in AFFO. The remaining difference between interest expense and interest paid is attributed to timing differences between accrual and payment basis and amortization on financing costs.

Scheduled debt repayments increased by $4,252, or 382%, for the quarter and $5,066, or 321%, on a year-to-date basis. The increases were primarily due to higher debt service payments at Amherstburg since commencement of operations on June 30, 2011 along with debt service payments at the Hydro facilities since the issuance of new debt on June 6, 2012.

Maintenance capital expenditures increased by $974, or 51.7%, for the quarter and $642, or 23.9%, on a year-to-date basis. The increases were primarily due to the outage at Cardinal for major maintenance on the hot gas path, which occurs every three years.

Results by Segment

Capstone's results are segmented into power facilities across Canada, a water utility in Europe, a district heating utility in Europe, and remaining corporate activities. The power segment includes gas cogeneration, hydro, wind, biomass and solar power. In 2011, Capstone made investments in the utilities segment through the acquisition of an interest in Bristol Water, a regulated water utility in the United Kingdom, and a 33.3% interest in Värmevärden, a district heating business in Sweden. The full results of Bristol Water are consolidated with Capstone's other businesses before deducting the portion of Adjusted EBITDA attributable to non-controlling interests. Capstone's non-controlling interest in Värmevärden returns interest income and dividends.

Net income (loss) and non-GAAP measure results for each business segment were as follows:

	Three months ended		Six months ended	
($000s)	**Jun 30, 2012**	**Jun 30, 2011**	**Jun 30, 2012**	**Jun 30, 2011**
Net Income (loss)				
Power	(3,016)	(6,374)	10,386	5,286
Utilities - Water	9,496	-	18,838	-
Utilities – District Heating	(752)	(510)	3,843	(2,924)
Corporate	(6,337)	(23,486)	(17,492)	8,600
Total	(609)	(30,370)	15,575	10,962
Adjusted EBITDA				
Power	15,927	12,784	40,487	35,170
Utilities - Water	13,712	-	27,273	-
Utilities – District Heating	1,637	1,692	2,988	1,692
Corporate	(3,671)	(2,435)*	(5,839)	(6,317)*
Total	27,605	12,041	64,909	30,545
AFFO				
Power	4,016	7,299	22,809	25,793
Utilities - Water	4,868	-	4,868	-
Utilities – District Heating	1,637	1,692	2,988	1,692
Corporate	(6,814)	(4,268)*	(12,042)	(8,642)*
Total	3,707	4,723	18,623	18,843

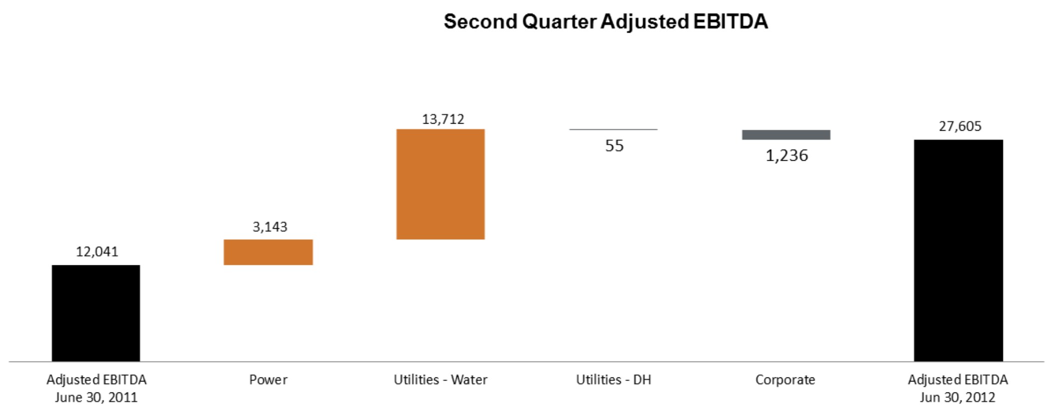
*excludes internalization costs for the second quarter of $18,611 and $19,246 for the year-to-date period

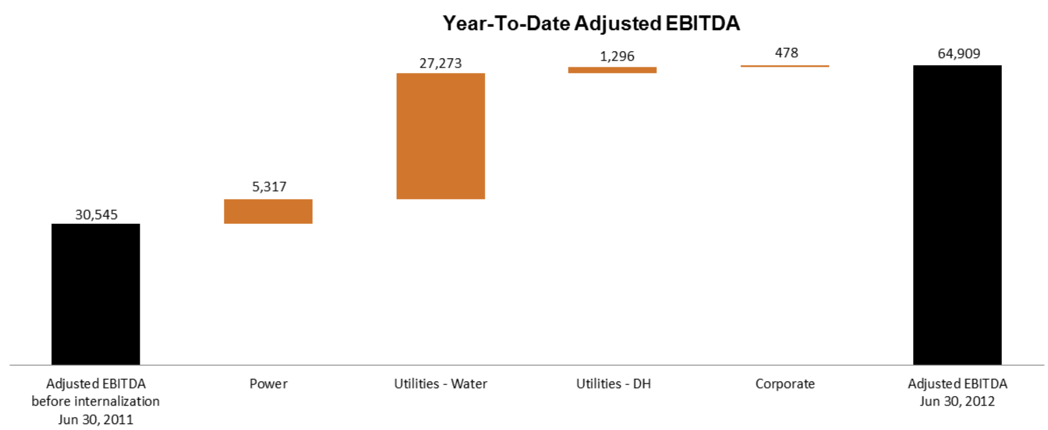
Adjusted EBITDA

Adjusted EBITDA increased by $15,564, or 129%, during the second quarter. The increase was attributable to the addition of Bristol Water and Amherstburg, which contributed a combined $19,366. This was partially offset by a reduction of $2,511 at the other power assets and an increase in corporate administrative expenses of $1,224. Lower Adjusted EBITDA from other power assets was primarily attributable to Cardinal, which declined by $1,787 due to lower revenue resulting from a longer scheduled outage than in previous years. Erie Shores also declined by $743 based on poorer wind conditions than in the comparable period of 2011. Higher administrative expenses were primarily attributable to higher professional fees to support refinancing of long-term debt, higher staff costs based on more paid weeks in 2012 due to internalization of staff on April 15,2011 and other administrative expenses such as rent since moving to new premises at the end of 2011.

Adjusted EBITDA was $34,364, or 113%, higher in the year-to-date period than in the comparable period of 2011.The addition of Bristol Water and Amherstburg contributed a combined $35,480 while Värmevärden contributed $983 in dividends. This was partially offset by a $2,890 decrease at the other power facilities primarily attributable to a $3,480 decline at Cardinal due to the scheduled outage and higher fuel and fuel transportation costs in the first quarter. This was partially offset by higher revenue in the first quarter due to strong wind conditions at Erie Shores. In addition, corporate administrative expenses declined by $698, reflecting lower business development expenses in 2012 as the Corporation focused on refinancing initiatives.

The following charts show the change in Adjusted EBITDA, excluding internalization costs for the second quarter and year to date:



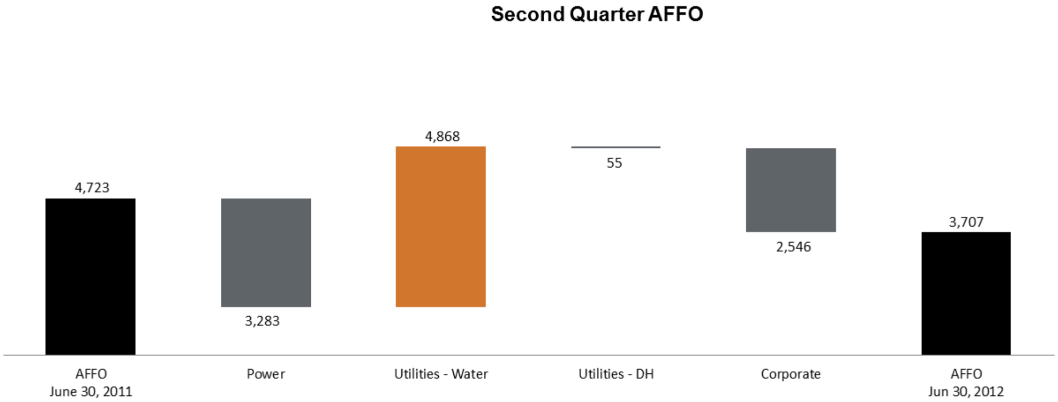


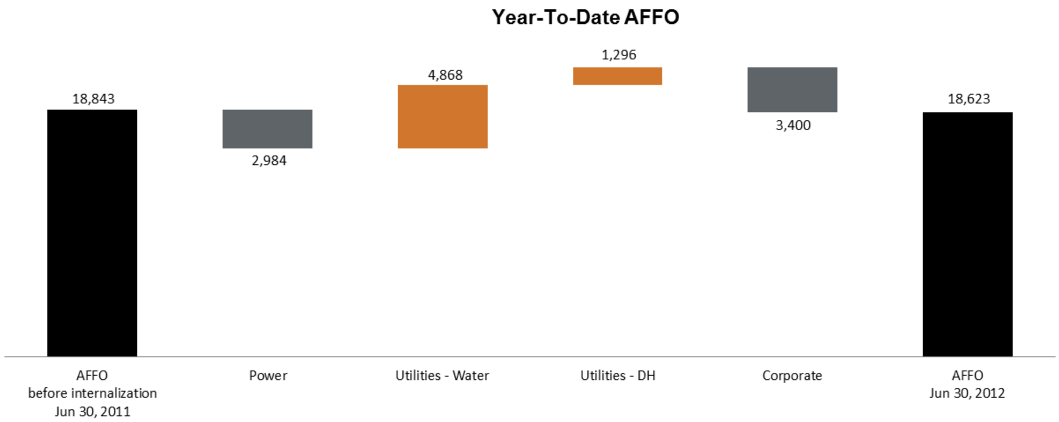
Adjusted Funds from Operations (AFFO)

Second quarter AFFO was $1,016, or 21.5%, lower than in the comparable period of 2011. A $6,939 increase in AFFO, attributable to the addition of Bristol Water and Amherstburg, was offset by a $5,354 decline across the other power facilities and various corporate factors, which reduced AFFO by $2,546. In the balance of the power portfolio, Cardinal and the Hydro facilities declined $2,573 and $1,445, respectively. Lower AFFO at Cardinal was due to higher maintenance capital expenditures and lower revenue as a result of the longer outage. Lower AFFO at the Hydro facilities was attributable to debt servicing expenses since the placement of new financing. The reduction at corporate was primarily due to $938 of dividends on preferred shares, a $1,224 increase in administrative expenses and $286 of additional interest paid primarily on the senior debt facility, which was fully repaid in April 2012.

AFFO in the year-to-date period was $220, or 1.2%, lower than in the comparable period of 2011. AFFO increased by $7,473 from the addition of Bristol Water and Amherstburg, which did not contribute in 2011. Värmevärden contributed an additional $983 in the form of a dividend. These factors were offset by a $5,589 decline across the other power facilities along with various corporate factors totaling $3,400. In the balance of the power portfolio, Cardinal and the Hydro facilities declined $3,956 and $1,505, respectively. Lower AFFO at Cardinal was due to higher major maintenance expenses combined with the factors impacting Adjusted EBITDA. Lower AFFO at the Hydro facilities was primarily due to debt servicing attributable to the new debt.

The following charts show the change in AFFO, excluding internalization costs for the second quarter and year to date:





Net income (loss)

Capstone's net income (loss) comprises cash measures included in Adjusted EBITDA and non-cash measures required by IFRS. The major items are summarized below:

	Three months ended		Six months ended	
($000s)	Jun 30, 2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
Adjusted EBITDA	27,605	(6,570)*	64,909	11,299*
Adjustment to distributions from Värmevärden to get to equity accounted income	(1,585)	(1,475)	(140)	(3,876)
NCI portion of Adjusted EBITDA	9,729	-	15,541	-
Other gains and (losses), net	(2,163)	(4,489)	(760)	(2,610)
Foreign exchange gain (loss)	(652)	(627)	452	(633)
Interest expense	(13,007)	(5,004)	(27,863)	(10,111)
Depreciation and amortization	(14,065)	(7,908)	(28,088)	(15,800)
Income tax recovery (expense)	(6,471)	(4,297)	(8,476)	32,693
Net Income (loss)	(609)	(30,370)	15,575	10,962

*includes internalization costs for the second quarter of $18,611 and $19,246 for the year-to-date period

Infrastructure - Power

Capstone's power facilities produce electricity from gas cogeneration, wind, biomass, hydro and solar and are located in Ontario, Alberta, British Columbia and Quebec. Results from these facilities were:

Three months ended Jun 30, 2012 ($000s)	Gas	Wind	Biomass[1]	Hydro	Solar	Total
Power generated (GWh)	251.4	47.5	47.8	63.8	13.7	424.2
Capacity factor	78.7%	22.0%	93.2%	81.8%	31.3%	n.m.f
Availability	83.1%	98.1%	93.6%	99.8%	97.9%	n.m.f
Revenue	21,441	4,651	3,398	4,945	5,697	40,132
Operating expenses	(19,564)	(1,009)	(2,585)	(843)	(352)	(24,353)
Interest income	14	9	117	3	5	148
Adjusted EBITDA	1,891	3,651	930	4,105	5,350	15,927
Principal from loans receivable	-	-	243	-	-	243
Interest paid	(90)	(1,546)	(2)	(542)	(1,753)	(3,933)
Income taxes (paid) recovery	-	-	-	-	-	-
Maintenance capital expenditures	(2,032)	(129)	(464)	(232)	-	(2,857)
Scheduled repayment of debt principal	-	(1,298)	(32)	(2,204)	(1,830)	(5,364)
AFFO	(231)	678	675	1,127	1,767	4,016

Three months ended Jun 30, 2011 ($000s)	Gas	Wind	Biomass[1]	Hydro	Solar	Total
Power generated (GWh)	281.0	52.6	45.9	61.4	-	440.9
Capacity factor	87.8%	24.4%	90.7%	78.6%	-	n.m.f
Availability	92.3%	92.3%	92.2%	99.5%	-	n.m.f
Revenue	24,009	5,119	3,187	4,713	-	37,028
Operating expenses	(20,336)	(727)	(2,160)	(864)	(338)	(24,425)
Interest income	5	2	140	-	34	181
Adjusted EBITDA	3,678	4,394	1,167	3,849	(304)	12,784
Principal from loans receivable	-	-	218	-	-	218
Interest paid	(262)	(1,508)	(4)	(933)	-	(2,707)
Income taxes (paid) recovery	(1)	-	-	-	-	(1)
Maintenance capital expenditures	(1,073)	(228)	(531)	(51)	-	(1,883)
Scheduled repayment of debt principal	-	(819)	-	(293)	-	(1,112)
AFFO	2,342	1,839	850	2,572	(304)	7,299

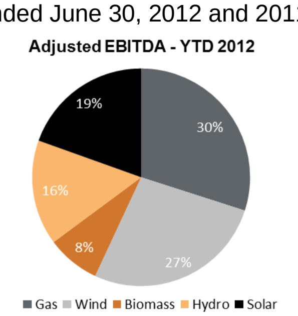
(1) Includes interest and loan receivable receipts from Capstone's 31.3% equity interest in the Chapais facility. Statistics for power generated, capacity factors and availability do not include the Chapais facility.

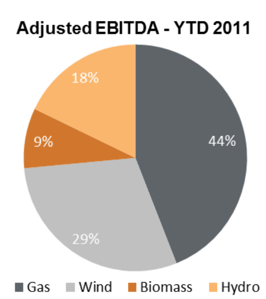
Six months ended Jun 30, 2012 ($000s)	Gas	Wind	Biomass[(1)]	Hydro	Solar	Total
Power generated (GWh)	593.3	131.4	100.9	94.5	20.4	940.5
Capacity factor	87.9%	30.4%	96.3%	60.6%	23.4%	n.m.f
Availability	91.5%	98.5%	96.6%	99.8%	95.2%	n.m.f
Revenue	53,853	12,877	7,552	7,911	8,582	90,775
Operating expenses	(41,757)	(1,968)	(4,588)	(1,588)	(688)	(50,589)
Interest income	29	16	241	3	12	301
Adjusted EBITDA	12,125	10,925	3,205	6,326	7,906	40,487
Principal from loans receivable	-	-	479	-	-	479
Interest paid	(293)	(3,109)	(4)	(1,275)	(3,504)	(8,185)
Income taxes (paid) recovery	-	-	-	-	-	-
Maintenance capital expenditures	(2,272)	(129)	(631)	(294)	-	(3,326)
Scheduled repayment of debt principal	-	(2,577)	(63)	(1,908)	(2,098)	(6,646)
AFFO	9,560	5,110	2,986	2,849	2,304	22,809

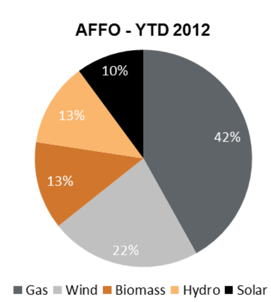
Six months ended Jun 30, 2011 ($000s)	Gas	Wind	Biomass[(1)]	Hydro	Solar	Total
Power generated (GWh)	622.0	123.2	97.1	96.8	-	939.1
Capacity factor	92.9%	28.6%	94.9%	62.4%	-	n.m.f
Availability	96.1%	95.4%	96.1%	99.2%	-	n.m.f
Revenue	57,086	12,004	6,838	8,015	-	83,943
Operating expenses	(41,558)	(1,527)	(4,083)	(1,669)	(338)	(49,175)
Interest income	77	2	286	-	37	402
Adjusted EBITDA	15,605	10,479	3,041	6,346	(301)	35,170
Principal from loans receivable	-	-	430	-	-	430
Interest paid	(523)	(3,131)	(8)	(1,880)	-	(5,542)
Income taxes (paid) recovery	(1)	-	-	-	-	(1)
Maintenance capital expenditures	(1,565)	(238)	(722)	(159)	-	(2,684)
Scheduled repayment of debt principal	-	(1,627)	-	47	-	(1,580)
AFFO	13,516	5,483	2,741	4,354	(301)	25,793

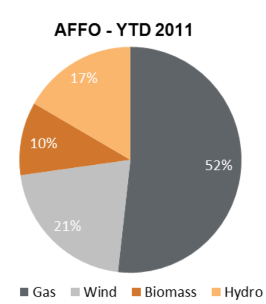
(1) Includes interest and loan receivable receipts from Capstone's 31.3% equity interest in the Chapais facility. Statistics for power generated, capacity factors and availability do not include the Chapais facility.

The following charts show the composition of the power segment's Adjusted EBITDA and AFFO for the six months ended June 30, 2012 and 2011:









Revenue

Revenue for the second quarter was $3,104, or 8.3%, higher than in 2011 and $6,832, or 8.1%, on a year-to-date basis. Revenue growth for the three and six months ended June 30, 2012 was primarily attributable to Amherstburg, which contributed $5,697 and $8,582, respectively.

Cardinal's lower production partially offset the second quarter and year-to-date increases by $2,568 and $3,233, respectively. The decline at Cardinal was primarily due to lower power generation arising from maintenance outages and higher ambient temperatures. Cardinal's power generation for the second quarter was 29.6 GWh, or 10.5%, lower than in 2011 and 28.7 GWh, or 4.6%, lower in the year-to-date period. The 2012 second quarter scheduled outage was for a hot gas path inspection, which occurs every three years and requires more time than other annual outages. In addition, power production is reduced when ambient temperatures are higher.

In addition, year-to-date, Erie Shores revenue was $873, or 7.3%, higher based on a power generation increase of 8.2 GWh, or 6.7%, due to favourable wind conditions in the first quarter of 2012. Whitecourt was $714, or 10.4%, higher year-to-date primarily due to the sale of $592 of renewable energy credits ("RECs").

Operating expenses

Operating expenses were $72, or 0.3%, lower in the second quarter and $1,414, or 2.9%, higher on a year-to-date basis. Excluding the addition from Amherstburg, the increase was primarily attributable to repairs and maintenance expenditures at Erie Shores and Whitecourt, which contributed a combined increase of $707 and $946 in the second quarter and year-to-date, respectively. Cardinal partially offset the increase in the second quarter, with a decrease of $772 in operating expenses due to lower fuel costs during the maintenance outage.

Interest paid

Interest paid in the second quarter was $1,226, or 45.3%, higher than in 2011 and $2,643, or 47.7%, higher on a year-to-date basis, primarily due to Amherstburg, which paid $1,753 and $3,504 of interest in the second quarter and first six months of 2012, respectively. Higher interest paid during 2012 was partially offset by less interest on the CPC-Cardinal credit facility, which had a lower average balance in 2012.

Maintenance capital expenditures

Maintenance capital expenditures in the second quarter increased by $974 over 2011, primarily due to the hot gas path inspection at Cardinal.

Scheduled repayment of debt principal

Scheduled repayments of debt principal for the second quarter were $4,252, or 382%, higher and $5,066, or 321%, higher on a year-to-date basis. The increase is primarily due to repayments on the Hydro facilities debt and Amherstburg project debt. The Hydro facilities added $1,786 since origination in June 2012 to both periods and Amherstburg added $1,830 higher in the second quarter and $2,098 in the year to date as repayments did not start until the third quarter of 2011. Finally, Erie Shores was $479 and $950 higher in the second quarter and year-to-date periods, respectively, because its Tranche C debt became fully amortizing on April 1, 2011.

Seasonality

Results for Capstone's power segment fluctuate during the year due to seasonal factors that affect quarterly production at each facility. These factors include scheduled major maintenance, seasonal electricity demands and environmental factors such as water flows, sunlight, wind speeds, ambient temperature and humidity, which affect the amount of electricity generated. In aggregate, these factors have historically resulted in higher electricity production during the first and fourth quarters as shown in the following table:

			Actual	Average long-term production (GWh) [1]				
Type	Facility	PPA Expiry	Q2	Q1	Q2	Q3	Q4	Annual
Gas	Cardinal	2014	251.4	342.9	278.1	304.0	332.6	1,257.6
Wind	Erie Shores	2026	47.5	76.3	52.5	34.2	78.1	241.1
Biomass	Whitecourt	2014	47.8	50.3	45.3	50.3	49.5	195.4
Hydro	Various	2017 - 2042	63.8	32.2	57.1	29.7	41.2	160.2
Solar	Amherstburg	2031	13.7	6.8	13.7	11.5	6.1	38.1
Total			424.2	508.5	446.7	429.7	507.5	1,892.4

(1) Average long-term production is from March 2005 to June 30, 2012, except for Erie Shores, which is from June 2006, and Amherstburg, which is from July 2011.

Outlook

In 2012, Capstone's power infrastructure businesses are expected to perform in line with long-term average production, subject to variations in wind, water flows, ambient temperatures and sunlight. Overall steady production from the facilities, including a full year contribution from Amherstburg, is expected to be partially offset by lower production and revenue and higher costs at Cardinal in 2012 due to:

- Lower gas mitigation revenues, primarily reflecting a lower spot gas price.
- The implementation of Government of Ontario amendments to the allocation of the Global Adjustment Mechanism ("GAM"). The GAM represents a key component of the price escalators contained in the power purchase agreements ("PPAs") for Cardinal and the Hydro facilities located in Ontario. The amended GAM is expected to result in lower growth in revenue at Cardinal as well as the Hydro facilities located in Ontario in 2012.
- An interim gas transportation rate of $2.24 per GJ, which is currently expected to remain in effect for the duration of 2012.
- Total maintenance capital expenditures across the power businesses are expected to be higher than in 2011.

Management is continuing to seek incremental growth opportunities to enhance the contribution of its power businesses, including the sale of RECs generated by the Whitecourt facility.

Overall, Capstone expects the net impact of these factors to result in a slightly higher Adjusted EBITDA for the power segment in 2012 compared to 2011.

Infrastructure - Utilities

Water

Capstone's water utilities segment includes a 50% investment in Bristol Water, which is located in the United Kingdom. Capstone initially acquired a 70% interest in October 2011, prior to which no results were reported in Capstone's comparative figures. On May 10, 2012, Capstone sold a 20% indirect interest in Bristol Water to ITOCHU Corporation while retaining the remaining 50%.

	Three months ended		Six months ended	
($000s)	**Jun 30, 2012**	**Jun 30, 2011**	**Jun 30, 2012**	**Jun 30, 2011**
Water supplied (megalitres)	21,359	-	41,122	-
Revenue	45,717	-	87,230	-
Operating expenses	(22,509)	-	(44,973)	-
Interest income	233	-	557	-
Less: non-controlling interest[(1)]	(9,729)	-	(15,541)	-
Adjusted EBITDA	13,712	-	27,273	-
Adjusted EBITDA of consolidated businesses with non-controlling interests	(13,712)	-	(27,273)	-
Dividends from businesses with non-controlling interests[(2)]	4,868	-	4,868	-
AFFO	4,868	-	4,868	-

(1) Starting from May 10, 2012, the NCI increased to 50% from 30%.
(2) Bristol Water pays semi-annual dividends in the second and fourth quarters each year.

Revenue

Bristol Water is a regulated business subject to supervision by the Water Services Regulation Authority ("Ofwat"). Bristol Water completed the second year of its five-year Ofwat approved asset management plan ("AMP5") as at March 31, 2012. Revenue in the first six months of 2012 was over 96.7% derived from water sales.

Operating expenses

Operating expenses primarily comprised raw materials, consumables, bad debts and other charges less recoveries totaling $18,315 for the second quarter and $37,139 on a year-to-date basis. Labour costs to maintain the network and deliver water services to retail and commercial customers comprised an additional $4,194 for the second quarter and $7,834 on a year-to-date basis.

Non-controlling interest

On May 10, 2012, the non-controlling interest was increased to reflect the partial sale of Bristol Water. Capstone's Adjusted EBITDA was reduced for Agbar's 30% interest over the entire period and ITOCHU's 20% interest beginning from May 10.

Capital expenditures

The total capital expenditure planned for AMP5 is approximately $441,000, or £276,000 (Base price of £261,000 has primarily been adjusted for inflation for new regulatory fiscal year). As at June 30, 2012, the cumulative capital expenditure incurred for AMP5 was $155,000, which was $59,000 less than planned. The shortfall was primarily the result of delays at the start of AMP5 as commencement of expenditures was dependent on a competition commission ruling. Bristol Water expects its expenditures over the remainder of AMP5 to achieve the cumulative approved capital expenditure. Bristol Water made $31,066 in capital expenditures in the second quarter and $73,491 on a year-to-date basis as detailed on page 25 of this MD&A.

Seasonality

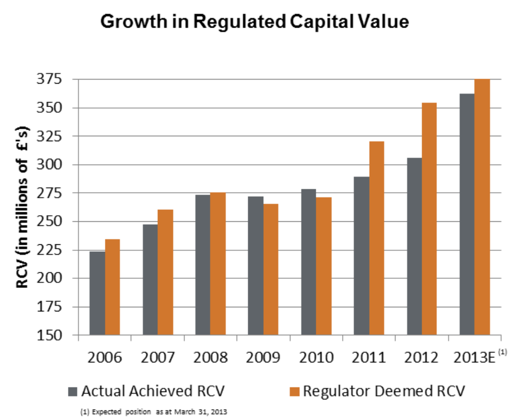
Bristol Water experiences little seasonal variation in demand resulting in stable revenues throughout the year. Operating expenses vary during the year depending on the availability of water from Bristol Water's various sources, the quantity of water requiring treatment as a result of dry weather and pipe bursts, which are more common in periods when freezing and thawing occur. Additionally, the level of capital expenditure activity fluctuates with weather, which impacts the infrastructure renewals expenditure.

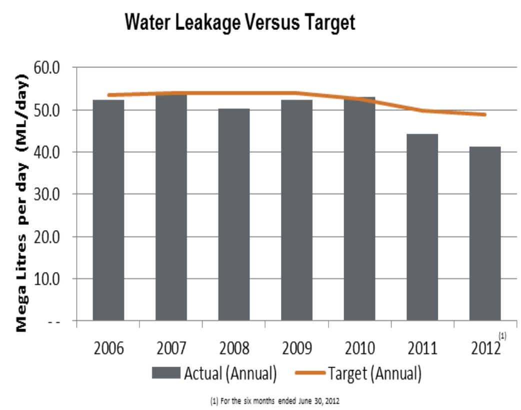
Outlook

In 2012, Bristol Water will contribute a full year of results to Capstone. Following the sale in May 2012 of an indirect 20% of Capstone's interest in Bristol Water, the business is expected to deliver over $7,500 in dividends to Capstone in 2012, reflecting Bristol Water's continuing stable performance. For 2012/2013, Bristol Water is benefiting from an increase of approximately 9.1% (3.9% real increase and a 5.2% inflationary increase) in its regulated water tariffs, positively impacting revenue.

In 2012, Bristol Water expects to complete capital expenditures of approximately $120,000 to $130,000 (£75,000 to £80,000). Capstone expects between 9 to 10% growth in Ofwat's deemed regulated capital value ("RCV") by March 31, 2013, which is expected to lead to future revenue growth. Bristol Water's capital program is aimed at improving and expanding Bristol Water's network of reservoirs, treatment facilities, water mains and pipes in order to continue providing high quality water to customers, reducing the amount of water lost to leakage, and positioning Bristol Water to effectively serve a growing population.

Management is also focused on achieving key regulatory output targets, including leakage of less than 51 million litres of water per day ("Ml/d") in 2012/2013, and is striving for a top quartile ranking in Ofwat's Service Incentive Mechanism ("SIM") customer service measure. Strong performance on the SIM, which is measured through customer satisfaction surveys and quantitative data related to complaints, can result in an increased revenue allowance for Bristol Water in the next regulatory period.





Infrastructure - Utilities

District Heating

Capstone's district heating utilities segment includes a 33.3% interest in Värmevärden, located in Sweden, which was acquired on March 31, 2011.

($000s)	Three months ended Jun 30, 2012	Three months ended Jun 30, 2011	Six Months ended Jun 30, 2012	Six Months ended Jun 30, 2011[1]
Heat production (GWh)	209	267	602	267
Equity accounted income (loss)	(602)	1,475	843	(3,889)
Interest income	654	1,692	2,005	1,692
Dividends	983	-	983	-
Adjusted EBITDA and AFFO	1,637	1,692	2,988	1,692

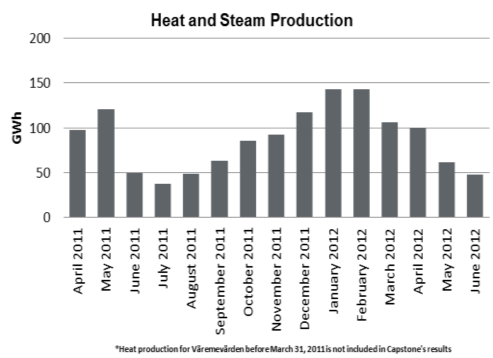
(1) Only three months of activity from the date of acquisition are included in the six months ended June 30, 2011.

Interest income

Interest is earned on the outstanding balance of the shareholder loan receivable from Värmevärden. During the first four months of 2012, Värmevärden used the bond issuance proceeds to reduce the shareholder loan by $48,100 resulting in lower interest income in the second quarter of 2012. For further details, refer to the changes in the business section on page 5 of this MD&A.

Dividends

During the second quarter, Capstone received a $983 dividend from Värmevärden for its 33.3% ownership interest in the business in addition to $654 of interest income.

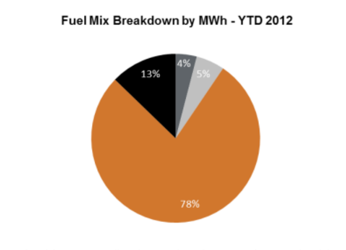


Equity accounted income

During the second quarter, Värmevärden's equity accounted loss was $602, while on a year-to-date basis Värmevärden contributed $843 to Capstone's net income. Second quarter results are typically lower due to the seasonality in the business. The loss in 2011 reflects $2,414 of transaction costs from acquisition.

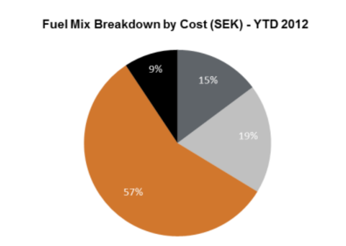
Seasonality

Heat production is typically highest during the first quarter of the year, which represents the coldest months of the year. The first and fourth quarters combined have historically accounted for approximately 65% of Värmevärden's annual revenue.



Outlook

In 2012, Värmevärden continues to seek opportunities to enhance its operational efficiency, including exploring options to improve the cost effectiveness of its fuel mix. Another area of focus for the company will be the continuing development of residential and industrial pricing strategies and enhancing relationships with customers.



Värmevärden's performance in 2012 is expected to continue to support interest payments on Capstone's loan receivable and dividends on Capstone's equity investment. Interest income from shareholder loans receivable is expected to be lower as a result of the lower receivable balance outstanding for 2012 from the capitalization of Värmevärden.

As a result, Capstone expects lower Adjusted EBITDA from the district heating segment compared with 2011.

Corporate

Corporate activities primarily comprise business development activities, capital structure expenses not specifically attributed to the businesses, and costs to manage, oversee and report on Capstone's investments.

	Three months ended		Six months ended	
($000s)	Jun 30,2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
Administrative expenses	(3,679)	(21,066)	(5,851)	(25,795)
Interest income	8	20	12	232
Adjusted EBITDA	(3,671)	(21,046)	(5,839)	(25,563)
Interest paid	(2,112)	(1,826)	(3,898)	(2,318)
Dividends paid on Capstone's preferred shares	(938)	-	(1,876)	-
Income taxes (paid) recovery	(93)	(7)	(429)	(7)
AFFO	(6,814)	(22,879)	(12,042)	(27,888)
Internalization costs	-	18,611	-	19,246
AFFO before internalization costs	(6,814)	(4,268)	(12,042)	(8,642)

Administrative expenses

	Three months ended		Six months ended	
($000s)	Jun 30,2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
Internalization expenses and manager fees	-	18,611	-	20,891
Salaries and benefits	1,660	1,148	3,207	1,148
Business development	26	454	82	1,686
Other administrative expenses	1,993	853	2,562	2,070
	3,679	21,066	5,851	25,795

Salaries and benefits reflect amounts paid to corporate employees beginning April 15, 2011 following the internalization of management. Internalization expenses represented amounts paid for professional fees and other administrative costs for the termination of the management contracts with MGL. Accordingly, Capstone does not have any internalization expenses or manager fees in 2012.

Business development expenses for the second quarter were $428, or 94.3%, lower than in 2011 and $1,604, or 95.1%, lower on a year-to-date basis.

Other administrative expenses for the second quarter were $1,140, or 134%, higher than in 2011 and $492, or 23.8%, higher on a year-to-date basis, primarily due to professional fees. Other administrative expenses include audit fees, investor relations costs, office administration costs and professional fees other than for business development.

Interest income

Interest income is primarily earned on surplus cash balances. Interest income for the second quarter was $12, or 60.0%, lower than in 2011 and $220, or 94.8%, lower on a year-to-date basis. The decline from 2011 for both periods primarily reflected lower average surplus cash balances in 2012.

Interest paid

Interest paid in the second quarter was $286, or 15.7%, higher than in 2011 and $1,580, or 68.2%, higher on a year-to-date basis due to higher balances on the CPC-Cardinal credit facility and the senior debt facility following the acquisition of Bristol Water. This was offset by a lower average balance on the convertible debentures in 2012 due to conversions during 2011.

Preferred share dividends paid and taxes paid

On June 30, 2011, Capstone issued preferred shares that pay $938 of dividends quarterly at a fixed rate of 5.0% per year. Taxes paid relate to the preferred share dividend and will be fully deductible against future taxable income of the Corporation.

FINANCIAL POSITION REVIEW

Overview

As at June 30, 2012, Capstone had a consolidated working capital surplus of $54,419 compared with a deficit of $86,694 at December 31, 2011. The increase of $141,113 in working capital primarily reflected $191,536 of debt repayment during the first six months of 2012. The utilities – water and power segments had surpluses of $48,737 and $9,486, respectively, while corporate had a deficit of $3,804.

Unrestricted cash and equivalents totaled $64,318 on a consolidated basis with the utilities – water and power segments contributing $43,249 and $15,519, respectively.

During the first six months of 2012, Capstone's debt to capitalization ratio (refer to page 22) declined from 71.0% to 62.9% on a fair value basis and from 65.7% to 58.4% on a book value basis. On a fair value basis, the decline reflected a 5.2% increase in the share price as well as a $112,534 decrease in debt at the power segment and corporate due to repaying the senior debt facility and a portion of the CPC-Cardinal credit facility. In addition, following the partial sale of Bristol Water, debt was also reduced by $100,155 to reflect Capstone's new proportionate share.

As at June 30, 2012, Capstone and its subsidiaries were in compliance with all debt covenants.

Liquidity

Working capital

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Power	9,486	(52,764)
Utilities – water	48,737	91,864
Corporate	(3,804)	(125,794)
Working capital	54,419	(86,694)

The working capital surplus of $54,419 increased $141,113 from December 31, 2011. The improvement primarily reflects debt repayment of the power segment and corporate, during the second quarter of 2012. This was partially offset by a $43,127 decrease in the utilities – water segment to fund the capital expansion program.

The power working capital surplus of $9,486 includes $12,300 remaining on the CPC-Cardinal credit facility. On July 31, 2012, Capstone obtained a commitment from a Canadian chartered bank for a new credit facility (the "New Facility") in the aggregate amount of up to $27,300, comprising a $12,300 term loan to be used to repay the outstanding balance on the CPC-Cardinal credit facility and a $15,000 revolving facility. The New Facility will mature on June 30, 2014 and financial close is expected to occur in the third quarter of 2012.

Cash and cash equivalents

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Power	15,519	13,972
Utilities – water	43,249	35,434
Corporate	5,550	8,181
Unrestricted cash and cash equivalents	64,318	57,587
Less: cash with access limitations		
Power	(9,824)	(10,135)
Utilities – water [1]	(43,249)	(35,434)
Cash and cash equivalents available to Capstone	11,245	12,018

[1] Utilities – water cash and cash equivalents is in addition to $40,325 of short-term deposits

Unrestricted cash represents funds available for operating activities, capital expenditures and future acquisitions. The $6,731 increase in cash from December 31, 2011 was primarily attributable to Bristol Water moving funds from short-term deposits for use in the capital expansion program.

Cash and cash equivalents available to Capstone are funds available for general purposes, including payment of dividends to shareholders. Bristol Water's $43,249 of cash and cash equivalents along with $40,325 of short-term deposits as at June 30, 2012 are primarily earmarked for capital expenditure projects for the company's five-year asset management plan approved by the regulator. For the power segment, $9,824 is only periodically accessible to Capstone through distributions under the terms of the credit agreements for the Hydro facilities, Erie Shores and Amherstburg.

Restricted cash increased by $5,076 from December 31, 2011 to $19,951 at June 30, 2012. The increase was mainly attributable to new debt service and maintenance reserve accounts required by the new credit agreement for the Hydro facilities. Restricted cash represents reserve accounts at the power segment and Bristol Water of $11,159 and $8,791, respectively.

Cash flow

Capstone's cash and cash equivalents increased by $6,731 in the first six months of 2012 compared with a decrease of $27,932 in the first six months of 2011. Details of the decrease are presented in the consolidated statement of cash flows and are summarized as follows:

Six months ended ($000s)	Jun 30, 2012	Jun 30, 2011
Operating activities	55,100	5,764
Investing activities	93,791	(164,332)
Financing activities (excluding dividends to shareholders)	(122,529)	150,868
Dividends paid to shareholders	(20,203)	(20,232)
Effect of exchange rate changes on cash and cash equivalents	572	-
Change in cash and cash equivalents	6,731	(27,932)

During the first six months of 2012, Capstone's operating activities generated $49,336 more cash than in 2011 primarily because Bristol Water contributed $31,884. Capstone's power segment generated $4,470 less cash flow in 2012 primarily due to lower operating income and working capital requirements, partially offset by the commencement of operations at Amherstburg. In addition, corporate operating activities were $21,922 higher in the first six months of 2012, resulting mainly from internalization costs only in 2011.

Cash flow from investing activities were $258,123 higher in the first six months of 2012 than in the comparable period of 2011, primarily due to transactions related to the capitalization of Värmevärden and partial sale of Bristol Water. In the first quarter of 2011, Capstone acquired Värmevärden for $109,146, comprising equity investment and shareholder loans. Additionally, Capstone invested $49,070 in the construction of Amherstburg during the first six months of 2011. In the first six months of 2012, Värmevärden returned $48,100 by repaying a portion of the shareholder loans from bond issue proceeds at Sefyr Värme. On May 10, 2012, Capstone received $70,274 from ITOCHU for a 20% interest in Bristol Water before transaction costs of $1,061. Lastly, Bristol Water invested $59,968 to expand the water network using short-term deposits of $41,949 to fund the capital expansion.

Cash flow from financing activities were $273,397 lower in the first six months of 2012 than in the prior year primarily because Capstone repaid $219,169 of debt in 2012 while adding $100,621 of long-term debt for the Hydro facilities. In the first six months of 2011, Capstone added $65,200 for the construction of Amherstburg along with raising $79,248 of preferred shares. The remaining difference is due to debt servicing principal reduction.

Capital Structure

Capstone considers shareholders' equity and long-term debt (proportionately attributable to Capstone's shareholders), both the current and non-current portions, to be the basis of capital structure. Capstone measures capital structure using the capitalization ratio based on the fair values of long-term debt and shareholders' equity. Capstone's capitalization ratios using fair values and carrying values were as follows:

	Jun 30, 2012		Dec 31, 2011	
As at ($000s)	**Fair Value**	**Carrying Value**	**Fair Value**	**Carrying Value**
Long-term debt				
Power	312,755	303,662	314,196	308,513
Utilities - water (1)	252,980	244,690	353,135	336,237
Corporate	44,031	40,457	155,124	152,613
Deferred financing fees	-	(6,331)	-	(6,421)
	609,766	582,478	822,455	790,942
Equity				
Shareholders' equity (2)	358,996	415,014	335,228	413,520
Total capitalization	968,762	997,492	1,157,683	1,204,462
Debt to capitalization	62.9%	58.4%	71.0%	65.7%

(1) Only 50% of the long-term debt at Bristol Water has been included at in the calculation to reflect the impact of the non-controlling interest (December 31, 2011 - 70%).
(2) The carrying value of shareholders' equity does not include the amount attributed to the non-controlling interest.

Power

The composition of the power segment's long-term debt was as follows:

			Jun 30, 2012		Dec 31, 2011	
As at ($000s)	**Maturity**	**Interest Rate**	**Fair Value**	**Carrying Value**	**Fair Value**	**Carrying Value**
CPC-Cardinal credit facility	2012	5.00%	12,300	12,300	85,000	85,000
Erie Shores project debt	2016 & 2026	5.28 – 6.15%	110,317	100,356	108,616	102,933
Amherstburg Solar Park project debt	2016	7.32%	92,169	92,169	94,267	94,267
Hydro facilities senior secured bonds	2040	4.56%	77,917	78,595	-	-
Hydro facilities subordinated secured bonds	2041	7.0%	20,052	20,242	-	-
Wawatay facility's levelization liability	2032	6.87%	-	-	26,313	26,313
			312,755	303,662	314,196	308,513

The $4,851 decrease in the carrying value of power segment's long-term debt in the first six months of 2012 is summarized as follows:

($000s)	Dec 31, 2011	Unscheduled repayments(1)	Scheduled repayments(2)	Debt proceeds(3)	Other(4)	Jun 30, 2012
For the six months ended	308,513	(99,672)	(6,461)	100,621	661	303,662

(1) Unscheduled debt repayments included $72,700 to settle the power portion of CPC-Cardinal credit facility along with the $27,239 to settle the Wawatay facility's levelization liability. Additionally, a $267 receivable with the OEFC as at June 30, 2012 partially offsets the Wawatay facility's levelization liability repayment.
(2) Scheduled repayments are regular repayments under the credit agreements.
(3) Debt proceeds include the issue of senior and subordinated secured bonds for the Hydro facilities, net of deferred financing costs.
(4) Other includes $688 of accrued interest partially offset by a reduction in the Wawatay facility's levelization liability of $27.

Covenant compliance

All of the power segment's long-term debt is subject to financial covenant requirements. The Hydro facilities, senior secured and subordinated secured bonds and the Erie Shores and Amherstburg facilities are individually required to maintain minimum debt service coverage ratios to allow for distributions to the Corporation. During the first six months of 2012, Capstone operated in compliance with all covenants and expects to continue to comply for the remainder of 2012.

Utilities - Water

The composition of the utilities - water segment's long-term debt was as follows:

			Jun 30, 2012		Dec 31, 2011	
As at ($000s)	Maturity	Interest Rate	Fair Value	Carrying Value	Fair Value	Carrying Value
Bank loans	2012 & 2017	1.27 - 1.37%	39,259	39,457	39,662	38,956
Term loans	2017 - 2041	5.73 – 7.54%(1)	436,486	421,910	436,205	413,702
Debentures	Irredeemable	3.50 – 4.25%	2,193	2,039	2,125	2,008
Cumulative preferred shares	Irredeemable	8.75%	28,022	25,974	26,487	25,673
Consolidated long-term debt			505,960	489,380	504,479	480,339
Less: non-controlling interest			(252,980)	(244,690)	(151,344)	(144,102)
Capstone share of long-term debt			252,980	244,690	353,135	336,237

(1) The interest rate on certain term loans includes an index-linked component to RPI, which was 3.9% after April 1, 2012 (For January 1 to March 31, 2012 - 5%).

Long-term debt for the utilities - water segment was used to fund current and ongoing capital expenditures to grow Bristol Water's network. Each long-term debt balance matures beyond one year with the exception of a $23,699 bank loan that matures in 2012. Existing undrawn credit facilities are sufficient to repay the maturing bank loan. The preferred shares are classified as long-term debt on the basis that they are irredeemable. All Bristol Water debt is non-recourse to Capstone.

Covenant compliance

The principal debt agreements require Bristol Water to comply with covenants relating to the minimum levels of interest coverage and net debt in relation to regulatory capital value. During the first six months of 2012, Bristol Water complied with all its covenants and expects to comply for the remainder of 2012.

Corporate

The composition of Capstone's corporate long-term debt was as follows:

			Jun 30, 2012		Dec 31, 2011	
As at ($000s)	Maturity	Interest Rate	Fair Value	Carrying Value	Fair Value	Carrying Value
Senior debt facility	2012	6.73%	-	-	78,375	78,375
CPC-Cardinal credit facility	2012	5.00%	-	-	34,000	34,000
Convertible debentures	2016	6.50%	44,031	40,457	42,749	40,238
			44,031	40,457	155,124	152,613

Long-term debt decreased by $112,156 in the first six months of 2012. Capstone repaid the full $78,375 of the senior debt facility and $34,000 of the CPC-Cardinal credit facility using funds received from the Värmevärden recapitalization, sale proceeds from the Bristol Water partial sale and financing proceeds from the Hydro facilities. The CPC-Cardinal credit facility maturity was extended to September 28, 2012 to accommodate refinancing agreements with the existing lender.

Covenant compliance

The CPC-Cardinal credit facility requires minimum interest coverage and maximum debt to EBITDA ratios to remain in compliance and determine the interest rate on the obligation. During the first six months of 2012, Capstone has complied with all covenants and expects to comply for the remainder of 2012.

Shareholders' equity

Shareholders' equity was composed of:

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Common shares	630,974	626,861
Class B exchangeable units	26,710	26,710
Preferred shares	72,020	72,020
	729,704	725,591
Equity portion of convertible debentures	9,284	9,284
Accumulated other comprehensive income (loss)	(3,481)	(6,729)
Retained earnings (deficit)	(320,493)	(314,626)
Equity to Capstone shareholders	415,014	413,520
Non-controlling interests	88,086	34,450
Total shareholders' equity	503,100	447,970

Capstone is authorized to issue an unlimited number of common shares as well as a limited number of preferred shares equal to 50% of the outstanding common shares. The increase in common shares outstanding was as follows:

	Six months ended Jun 30, 2012		Year ended Dec 31, 2011	
($000s and 000s of shares)	Shares	Amount	Shares	Amount
Opening balance	70,957	626,861	56,352	536,278
Shares issued(1)	-	(89)	12,856	77,526
Conversion of convertible debentures	-	-	1,496	11,819
Dividend reinvestment plan (DRIP)	1,104	4,202	253	1,238
Ending balance	72,061	630,974	70,957	626,861

(1) During 2012, additional transaction costs of $95 were included in share capital in relation to the November 10, 2011 common share offering.

The composition of shareholders' equity fair value was as follows:

As at	Jun 30, 2012			Dec 31, 2011		
($000s, except per share amounts)	Market price per share	Outstanding amount	Fair Value	Market price per share	Outstanding amount	Fair Value
Common shares	$4.01	72,061	288,966	$3.81	70,957	270,348
Class B units	$4.01	3,249	13,030	$3.81	3,249	12,380
Preferred shares	$19.00	3,000	57,000	$17.50	3,000	52,500
			358,996			335,228

Retained earnings (deficit) reflects the aggregate of Capstone's net income (loss) since formation of the Corporation less cumulative dividends paid to shareholders and cumulative distributions paid to Class B exchangeable unitholders.

Contractual Obligations

Capstone enters into contractual commitments in the normal course of business. These contracts include leases, purchase obligations, electricity supply contracts, gas purchase contracts, wood waste agreements, operations and management agreements and guarantees. All material changes in contractual obligations outside the normal course of operations during the first six months of 2012 were previously disclosed in the annual MD&A for the year ended December 31, 2011, or the Annual Information Form filed March 21, 2012. Additionally, there have been no other significant changes to the specified contractual obligations that are outside the ordinary course of business and Capstone is not engaged in any off-balance sheet financing transactions.

Equity Accounted Investments

See discussion in the results of operations on page 18 of this MD&A for detailed discussion on Capstone's equity accounted investment in Värmevärden.

For Capstone's equity interest in Chapais Électrique Limitée ("CHEL"), the general partner in the Chapais investment, no income has been recorded on the investment since its acquisition in 2007. Capstone does not expect to earn any future equity accounted income from this investment. Additionally, Capstone's investment in MLTCLP had no activity during the six months ended June 30, 2012.

Capital Expenditure Program

Capstone made $33,493 in capital expenditures during the second quarter of 2012 and $76,415 on a year-to-date basis. Below is the breakdown of the investment by operating segment:

	Three months ended		Six months ended	
($000s)	**Jun 30, 2012**	**Jun 30, 2011**	**Jun 30, 2012**	**Jun 30, 2011**
Power	2,392	42,374	2,862	87,014
Utilities – water	31,066	-	73,491	-
Corporate	35	-	62	-
	33,493	42,374	76,415	87,014

Capital expenditures for the power segment in the second quarter of 2012 and year to date were in the normal course of operations and primarily related to the Cardinal, Whitecourt and the Hydro facilities as they completed scheduled outages in the second quarter of 2012. In 2011, the capital expenditures primarily related to the construction of the Amherstburg facility. For the utilities – water segment, expenditures included both growth and maintenance initiatives as outlined in Bristol Water's regulatory capital expenditures program. In aggregate, Bristol Water's capital expenditure program spans the five-year AMP5 period. Overall, Bristol Water's expenditures to date are behind the five-year plan but are expected to catch up before the end of AMP5 in 2015.

Retirement Benefit Plans

Bristol Water has a defined benefit retirement plan for current and former employees. The defined benefit retirement plan is closed to new employees, who are allowed to join the defined contribution plan.

As at June 30, 2012, the defined benefit retirement plan was in a $48,804 surplus position in accordance with IFRS. The surplus is subject to a number of critical accounting estimates which can materially impact the balances. The fair values included in the surplus are calculated with the assistance of an actuary and assumptions used are considered to be reasonable by management.

Bristol Water, employer contributions paid in the three and six months ended June 30, 2012 to the defined benefit plan were $1,032 and $2,425, respectively. The expense is entirely incurred at Bristol Water.

The total defined contribution pension expense recorded in the consolidated statement of income for the three and six months ended June 30, 2012 was $334 and $632, respectively. The expense is composed of $542 for Bristol Water and $90 for Cardinal for the six months ended June 30, 2012.

Income Taxes

The current income tax expense for the second quarter and year-to-date of $460 and $508, respectively, were entirely attributable to Bristol Water.

Deferred income tax assets and liabilities are recognized on Capstone's interim consolidated statement of financial position based on temporary differences between the accounting and tax bases of existing assets and liabilities.

As at ($000s)	**Jun 30, 2012**	**Dec 31, 2011**
Deferred income tax assets	32,374	32,897
Deferred income tax liabilities	(184,217)	(178,201)
	(151,843)	(145,304)

Capstone’s total deferred income tax assets include $17,301 ($16,924 at December 31, 2011) attributable to the Canadian entities and $15,073 ($15,973 at December 31, 2011) for Bristol Water. Deferred income tax assets primarily relate to financial instruments fair value adjustments and differences in the amortization of deferred financing costs for tax and accounting purposes.

Deferred income tax liabilities of $66,810 ($60,286 at December 31, 2011) were attributable to Capstone’s Canadian entities while $117,407 ($117,915 at December 31, 2011) was attributable to Bristol Water. Deferred income tax liabilities primarily relate to differences in the amortization of intangible and capital assets for tax and accounting purposes.

Capstone’s net deferred income tax liability increased by $6,539 during the first six months of 2012. The increase was primarily attributable to the difference between accounting and tax depreciation. Offsetting this was a substantively enacted tax rate reduction in the United Kingdom from 25% to 24%, effective April 1, 2012. The reduction resulted in a recovery of $3,647, which is offset by differences between accounting and tax depreciation at Bristol Water. The increase in the deferred income tax liability not attributable to the deferred income tax expense relates to amounts recorded to other comprehensive income.

The $32,701 income tax recovery for the six-months ended June 30, 2011 was primarily attributable to Capstone’s conversion to a corporation. As a trust in 2010, IFRS required Capstone to use an “undistributed” tax rate to determine deferred taxes. Upon conversion to a corporation, Capstone recognized the recovery from changing tax rates from 46%, the trust rate, to 25%, the general corporate rate.

DERIVATIVE FINANCIAL INSTRUMENTS

Capstone has exposure to market, credit and liquidity risks from its use of financial instruments as described in notes 11 (Financial Instruments) and 12 (Financial Risk Management) in the consolidated financial statements for the year ended December 31, 2011. These notes contain further details on the implicit risks and valuation methodology employed for Capstone’s financial instruments.

To manage the risks inherent in the business, Capstone enters into derivative contracts to mitigate the economic impact of the fluctuations in interest rates, the price of natural gas and foreign exchange rates. The fair value of these contracts, as reported in Capstone’s interim consolidated statements of financial position was:

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Derivative contract assets	2,791	3,144
Derivative contract liabilities	(33,876)	(34,143)
Net derivative contract liabilities	(31,085)	(30,999)

The composition of derivative contracts in 2012 is consistent with 2011, aside from the expiry of the gas swap and certain interest rate swaps during the first six months of 2012. In the second quarter of 2012, interest rate swaps that coincided with the original expiry of the CPC-Cardinal credit facility expired. The $86 decrease in the net derivative contract liabilities is included in the $51 loss apart of other gains and losses on the consolidated statement of income for the six-month period ended June 30, 2012. The unrealized gain (loss) on derivatives on the interim consolidated statements of income and comprehensive income comprised:

	Three months ended		Six months ended	
($000s)	Jun 30, 2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
Interest rate swap contracts	(2,495)	(2,520)	(125)	(220)
Gas swap contracts	-	(820)	-	(708)
Foreign currency option contracts	(48)	151	(457)	151
Embedded derivative	1,138	(1,300)	576	(1,833)
Unrealized gain (losses) on derivatives in net income	(1,405)	(4,489)	(6)	(2,610)
Interest rate swap contracts	(261)	-	(51)	-
Unrealized gain (losses) on derivatives in OCI	(1,666)	(4,489)	(57)	(2,610)

The unrealized loss on derivatives in the second quarter of 2012 was primarily attributable to the interest rate swap for the Amherstburg debt, which contributed $2,456 of the loss. The fair value of the interest rate swaps decreased primarily due to lower long-term interest rates. The loss for the six months ended 2012 was partially offset by the unrealized gains in the first quarter.

The unrealized loss on foreign currency contracts is due to the net depreciation of the Swedish Kronor and British pound sterling relative to the fixed Canadian dollar conversion rate.

The embedded derivative gain was primarily due to lower natural gas spot and forward prices as determined at a regional gas interconnection, storage and trading hub in southwest Ontario (the Union Gas Dawn facility).

FOREIGN EXCHANGE

The foreign exchange gain (loss) for 2012 and 2011 were primarily due to translation of Capstone's SEK denominated shareholder loan receivable with Värmevärden. Capstone's foreign exchange loss of $652 for the second quarter of 2012 was $25, or 4.0%, higher than in 2011. In both periods the Swedish Kronor depreciated against the Canadian dollar reducing the carrying value of the loans in Canadian dollars. The $452 foreign exchange gain for the first six months of 2012 was attributed to appreciation of the Swedish Kronor during the first quarter. Repayment of more than half of the shareholder loan reduced the impact of Swedish Kronor depreciation for both the second quarter and year-to-date results .

RISKS AND UNCERTAINTIES

Capstone is subject to a variety of risks and uncertainties, including the recontracting of the Cardinal PPA, which expires at the end of 2014, that could impact operating results and financial condition, which could adversely affect our ability to pay dividends to shareholders. For a comprehensive description of the risk factors that could affect the Corporation's future results, please refer to the "Risk Factor" section of the Corporation's Annual Information Form dated March 21, 2012 as supplemented by risk factors contained in any material change reports (except confidential material change reports), business acquisition reports, interim financial statements, interim management's discussion and analysis and information circulars filed by the Corporation with securities commissions or similar authorities in Canada, which are available on the SEDAR website at www.sedar.com.

ENVIRONMENTAL, HEALTH AND SAFETY REGULATION

Capstone monitors developments with respect to environmental, health and safety regulation. Please refer to the Corporation's prior environmental, health and safety regulation disclosure in the Corporation's Annual Report for the year ended December 31, 2011, which is available on the SEDAR website at www.sedar.com.

SUMMARY OF QUARTERLY RESULTS

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

($000s, except for per share amounts)	2012		2011				2010	
	Q2	Q1	Q4[1]	Q3	Q2[2, 3]	Q1	Q4	Q3
Revenue	85,849	92,156	91,663	40,361	37,028	46,915	44,265	34,598
Net income (loss) [4]	(4,568)	13,381	(4,891)	(11,783)	(30,370)	41,332	(2,648)	(6,845)
Adjusted EBITDA	27,605	37,295	31,120	13,253	(6,570)	17,869	16,531	10,166
AFFO	3,707	14,915	9,657	5,891	(13,888)	13,484	9,795	6,223
Common dividends [5]	10,231	12,299	11,569	10,225	10,217	10,015	8,232	7,700
Preferred dividends	938	938	1,264	-	-	-	-	-
Earnings Per Share – Basic	(0.073)	0.167	(0.086)	(0.190)	(0.492)	0.685	(0.055)[6]	(0.147)[6]
Earnings Per Share – Diluted	(0.073)	0.161[7]	(0.086)	(0.190)	(0.492)	0.625[7]	(0.055)	(0.163)[7]
AFFO per share [8]	0.049	0.200	0.136	0.095	(0.225)	0.223	0.192	0.125
Dividends declared per common share	0.135	0.165	0.165	0.165	0.165	0.165	0.165	0.165

(1) AFFO and AFFO per share have been adjusted to conform to the Corporation's revised definition of AFFO; refer to page 7 of this MD&A.
(2) Net loss, Adjusted EBITDA, AFFO, Earnings Per Share, and AFFO per share were significantly impacted by $18,611 of internalization costs incurred during the second quarter.
(3) Net loss has been adjusted by $2,409 for acquisition costs on Capstone's investment in Värmevärden.
(4) Net income (loss) attributable to the shareholders of Capstone.
(5) Common dividends include amounts declared for both the common shares of the Corporation and the Class B exchangeable units.
(6) Class B exchangeable units were not included in the weighted average shares outstanding during this period as they were classified as debt.
(7) Convertible debentures were dilutive during the period.
(8) 2010 includes the Class B exchangeable units to allow the non-GAAP measures to be comparative.

RELATED PARTY TRANSACTIONS

No related party transactions occurred in the six months ended June 30, 2012.

ACCOUNTING POLICIES AND INTERNAL CONTROL

Significant Changes in Accounting Standards

Capstone's accounting policies are consistent with those disclosed in the notes to the December 31, 2011 consolidated financial statements included in the Annual Report.

Future Accounting Changes

The International Accounting Standards Board ("IASB") has not issued any significant accounting changes that impact the Corporation since the standards described in the most recent annual financial statements for the year ended December 31, 2011.

The Corporation has completed a preliminarily assessment of the new and amended standards with effective implementation dates on or before January 1, 2013 as described in the most recent annual financial statements. Adoption of the new and amended standards is not expected to have a material impact on the Corporation's consolidated financial statements.

Accounting Estimates

The interim consolidated financial statements are prepared in accordance with IFRS, which require the use of estimates and judgment in reporting assets, liabilities, revenues, expenses and contingencies.

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

Area of significant estimate	Assumptions and judgements
• Purchase price allocations	• Initial fair value of net assets
• Depreciation on capital assets	• Estimated useful lives and residual value
• Amortization on intangible assets	• Estimated useful lives
• Asset retirement obligations	• Expected settlement date, amount and discount rate
• Impairment of trade receivables	• Probability of failing to recover amounts when they fall into arrears
• Derivative financial instruments	• Interest rate, natural gas price, and direct consumer rate
• Retirement benefits	• Future cash flows and discount rate
• Income taxes	• Timing of reversal of temporary differences
• Impairment assessments of capital, assets, intangibles and goodwill	• Future cash flows and discount rate

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

Internal Controls over Financial Reporting and Disclosure Controls and Procedures

Since December 31, 2011, no material changes have occurred in Capstone's policies and procedures and other processes that comprise its internal control over financial reporting and disclosure controls and procedures.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at ($000s)	Notes	Jun 30, 2012	Dec 31, 2011
Current assets			
Cash and cash equivalents		64,318	57,587
Restricted cash		19,951	14,875
Short-term deposits		40,325	82,274
Accounts receivable		65,847	73,583
Other assets		3,646	4,719
Current portion of loans receivable	6	1,039	984
Current portion of derivative contract assets		222	261
		195,348	234,283
Non-current assets			
Loans receivable	6	37,243	85,824
Derivative contract assets		2,569	2,883
Equity accounted investments	7	15,779	15,993
Capital assets	8	1,035,875	977,456
Intangible assets	9	285,800	288,304
Retirement benefit surplus	10	48,804	60,104
Deferred income tax assets		32,374	32,897
Total assets		1,653,792	1,697,744
Current liabilities			
Accounts payable and other liabilities		83,617	81,734
Current portion of derivative contract liabilities		3,044	3,088
Current portion of finance lease obligations		5,121	5,256
Current portion of long-term debt	11	49,147	230,899
		140,929	320,977
Long-term liabilities			
Derivative contract liabilities		30,832	31,055
Electricity supply and gas purchase contracts	9	4,081	4,894
Deferred income tax liabilities		184,217	178,201
Deferred revenue		3,797	1,363
Finance lease obligations		6,827	6,727
Long-term debt	11	778,021	704,145
Liability for asset retirement obligation		1,988	2,412
Total liabilities		1,150,692	1,249,774
Equity attributable to shareholders' of Capstone		415,014	413,520
Non-controlling interest		88,086	34,450
Total liabilities and shareholders' equity		1,653,792	1,697,744
Commitments and contingencies	18		

See accompanying notes to these interim consolidated financial statements

UNAUDITED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

($000s)	Notes	Equity attributable to shareholders of Capstone					
		Share Capital (1)	Convertible Debentures	AOCI (2)	Retained Earnings	NCI (3)	Total Equity
Balance, December 31 2010		536,278	-	-	(272,183)	-	264,095
Common shares issued		6,898	-	-	-	-	6,898
Preferred shares issued		73,016	-	-	-	-	73,016
Other comprehensive income (loss)		-	-	(133)	-	-	(133)
Net income for the period		-	-	-	10,962	-	10,962
Dividends declared to common shareholders of Capstone	12b	-	-	-	(20,232)	-	(20,232)
Reclassification of debt instruments to equity on conversion to a corporation		26,710	11,554	-	-	-	38,264
Debenture conversions, net of costs		11,800	(2,266)	-	-	-	9,534
Balance June 30, 2011		654,702	9,288	(133)	(281,453)	-	382,404

($000s)	Notes	Equity attributable to shareholders of Capstone					
		Share Capital (1)	Convertible Debentures	AOCI (2)	Retained Earnings	NCI (3)	Total Equity
Balance, December 31, 2011		725,591	9,284	(6,729)	(314,626)	34,450	447,970
Common shares issued (4)		(89)	-	-	-	-	(89)
Other comprehensive income (loss)		-	-	2,499	(6,229)	(2,697)	(6,427)
Net income for the period		-	-	-	8,813	6,762	15,575
Dividends declared to common shareholders of Capstone	12a&b	4,202	-	-	(22,530)	-	(18,328)
Dividends declared to preferred shareholders of Capstone	12b	-	-	-	(1,876)	-	(1,876)
Dividends declared by Bristol Water		-	-	-	-	(2,088)	(2,088)
Disposal of partial interest in Bristol Water	5	-	-	749	15,955	51,659	68,363
Balance, June 30, 2012		729,704	9,284	(3,481)	(320,493)	88,086	503,100

(1) Share capital includes common and preferred shares and class B exchangeable units.
(2) Accumulated other comprehensive income (loss) ("AOCI").
(3) Non-controlling interest ("NCI").
(4) During 2012, additional transaction costs of $89 were included in relation to the common share offering on November 10, 2011.

See accompanying notes to these interim consolidated financial statements

UNAUDITED CONSOLIDATED STATEMENTS OF INCOME

($000s, except per share amounts)	Notes	Three months ended Jun 30, 2012	Three months ended Jun 30, 2011	Six months ended Jun 30, 2012	Six months ended Jun 30, 2011
Revenue		85,849	37,028	178,005	83,943
Operating expenses		(46,862)	(24,425)	(95,562)	(49,175)
Administrative expenses		(3,679)	(21,066)	(5,851)	(25,795)
Equity accounted income (loss)	7	(602)	(1,475)	843	(3,876)
Interest income		1,043	1,893	2,875	2,326
Other gains and (losses), net		(2,163)	(4,489)	(760)	(2,610)
Foreign exchange gain (loss)		(652)	(627)	452	(633)
Earnings before, interest expense, taxes, depreciation and amortization		32,934	(13,161)	80,002	4,180
Interest expense		(13,007)	(5,004)	(27,863)	(10,111)
Depreciation of capital assets	8	(11,588)	(5,946)	(23,155)	(11,895)
Amortization of intangible assets	9	(2,477)	(1,962)	(4,933)	(3,905)
Income before income taxes		5,862	(26,073)	24,051	(21,731)
Income tax recovery (expense)					
Current		(460)	(8)	(508)	(8)
Deferred		(6,011)	(4,289)	(7,968)	32,701
Total income tax recovery (expense)		(6,471)	(4,297)	(8,476)	32,693
Net income (loss)		(609)	(30,370)	15,575	10,962
Net income (loss) attributable to:					
Shareholders of Capstone		(4,568)	(30,370)	8,813	10,962
Non-controlling interest		3,959	-	6,762	-
		(609)	(30,370)	15,575	10,962
Earnings per share					
Basic and diluted	13	(0.073)	(0.492)	0.093	0.180

UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

($000s)	Notes	Three months ended Jun 30, 2012	Three months ended Jun 30, 2011	Six months ended Jun 30, 2012	Six months ended Jun 30, 2011
Cumulative differences on translation of foreign operations		364	-	3,111	-
Other comprehensive loss on equity accounted investments	7	(434)	(133)	(74)	(133)
Losses on financial instruments designated as cash flow hedges (net of tax in 2012 - $96 and $16, respectively)		(251)	-	(287)	-
Actuarial losses recognized in respect of retirement benefit obligations (net of tax in 2012 - $391 and $3,660, respectively)		(1,359)	-	(9,177)	-
Other comprehensive income (loss)		(1,680)	(133)	(6,427)	(133)
Net income (loss)		(609)	(30,370)	15,575	10,962
Total comprehensive income		(2,289)	(30,503)	9,148	10,829
Comprehensive income attributable to:					
Shareholders of Capstone		(5,528)	(30,503)	5,083	10,829
Non-controlling interest		3,239	-	4,065	-
		(2,289)	(30,503)	9,148	10,829

See accompanying notes to these interim consolidated financial statements

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

Six months ended ($000s)	Notes	Jun 30 2012	Jun 30 2011
Operating activities:			
Net income		15,575	10,962
Deferred income tax expense (recovery)		7,968	(32,701)
Depreciation and amortization		28,088	15,800
Other gains and losses (net)		627	90
Amortization of deferred financing costs and non-cash financing costs		8,330	2,264
Equity accounted (income) loss	7	(843)	3,876
Unrealized foreign exchange (gain) loss on loan receivable	6	84	2,610
Change in non-cash working capital	17	(4,729)	2,863
Total cash flows from operating activities		55,100	5,764
Investing activities:			
Proceeds from sale of Bristol Water	5	70,274	-
Receipt of loans receivable		48,443	430
Change in restricted cash and short term investments		37,597	(5,186)
Return of capital from equity accounted investments	7	983	-
Proceeds from sale (purchase) of foreign currency contracts		38	(710)
Investment in capital assets	8	(63,544)	(49,070)
Loan to equity accounted investments		-	(84,170)
Investment in equity accounted investments		-	(25,626)
Total cash flows from (used in) investing activities		93,791	(164,332)
Financing activities:			
Proceeds from long-term debt		100,621	65,200
Repayment of long-term debt and finance lease obligations		(219,169)	(1,639)
Dividends paid to common and preferred shareholders		(20,203)	(20,232)
Dividends paid to non-controlling interests		(2,045)	-
Transaction costs on debt issuance		(1,936)	(839)
Proceeds from issuance of common and preferred shares, net of costs		-	79,248
Proceeds from loans payable		-	8,898
Total cash flows from (used in) financing activities		(142,732)	130,636
Effect of exchange rate changes on cash and cash equivalents		572	-
Increase (decrease) in cash and cash equivalents		6,731	(27,932)
Cash and cash equivalents, beginning of year		57,587	128,413
Cash and cash equivalents, end of period		64,318	100,481
Supplemental information:			
Interest paid		21,082	7,860
Taxes paid (recovery)		429	8

See accompanying notes to these interim consolidated financial statements

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. CORPORATE INFORMATION

Capstone is incorporated and domiciled in Canada and principally located at 155 Wellington Street West, Suite 2930, Toronto, Ontario, M5V 3H1. The mission of Capstone Infrastructure Corporation and its subsidiaries (together the "Corporation" or "Capstone") is to build and responsibly manage a high quality portfolio of infrastructure businesses in Canada and internationally in order to deliver a superior total return to our shareholders by providing reliable income and capital appreciation. Capstone's portfolio includes investments in gas cogeneration, wind, hydro, biomass and solar power generating facilities, representing approximately 370 MW of installed capacity, a 33.3% interest in a district heating business in Sweden, and a 50% interest in a regulated water utility in the United Kingdom.

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

2. BASIS OF PREPARATION

Statement of Compliance

The interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), including International Accounting Standard ("IAS") 34 Interim Financial Reporting ("IAS 34") on a basis consistent with the accounting policies disclosed in the audited consolidated financial statements for the year ended December 31, 2011. Certain information and footnote disclosures included in the annual financial statements prepared in accordance with IFRS, as issued by the International Accounting Standards Board ("IASB") have been omitted or condensed. These unaudited interim consolidated financial statements should be read in conjunction with the audited 2011 annual consolidated financial statements.

The policies applied in these interim condensed consolidated financial statements are based on IFRS issued and in effect as at August 13, 2012, the date that the Board of Directors approved the interim consolidated financial statements.

3. SEASONALITY

The seasonality of wind speed, volume of water flows, sunlight, ambient temperatures and pricing provisions within the power purchase agreements ("PPA") with the Ontario Electricity Financial Corporation ("OEFC") may result in fluctuations in revenue and net income during the period.

Operating expenses of the regulated water utility in the United Kingdom can fluctuate depending on the availability of water from various sources, the quantity of water requiring treatment as a result of dry weather, and pipe bursts in periods where freezing and thawing occur. As well, the level of capital expenditure activity can fluctuate with weather.

Warm weather reduces demand for heat from the Swedish district heating business.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

There have been no material changes to Capstone's accounting policies during the first six months of 2012.

Basis of Measurement

The interim consolidated financial statements have been prepared under the historical cost basis, except for the revaluation of certain financial instruments, which are measured at fair value and on a going concern basis of accounting. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

Future Accounting Changes

The IASB has not issued any significant new accounting standards that impact the Corporation since the standards described in the most recent annual financial statements for the year ended December 31, 2011.

The Corporation has completed a preliminary assessment of the new and amended standards with effective implementation dates on or before January 1, 2013 as described in the most recent annual financial statements. Adoption of the new and amended standards is not expected to have a material impact on the Corporation's consolidated financial statements.

5. ACQUISITIONS AND DISPOSALS

Acquisition of Bristol Water

On October 5, 2011, Capstone acquired a 70% indirect interest in Bristol Water, a regulated water utility in the United Kingdom, from Suez Environnement through its subsidiary, Agbar (Sociedad General de Aguas de Barcelona), for $213,476. Transaction costs on acquisition of $5,997 were expensed in the consolidated statement of income as part of administrative expenses for the year ended December 31, 2011.

The acquisition was accounted for using the purchase method of accounting. IFRS requires that Capstone recognize the identifiable assets acquired and liabilities assumed at their fair values. Goodwill is then recognized for the excess of the consideration paid over the net of the identifiable assets acquired and liabilities assumed measured at their fair values. Goodwill represents Capstone's ability to achieve financial and operational outperformance. The non-controlling interest has only been calculated on the fair value of the net identifiable assets.

The purchase price allocation is preliminary and will be finalized within a year of the purchase date. The preliminary allocation of total consideration was allocated to net assets acquired and adjusted in 2012 as follows:

As at October 5, 2011 ($000s)	Original	Adjustment	Revised
Working capital	804	849	1,653
Tangible assets	506,792	-	506,792
Intangible assets – licence	21,591	-	21,591
Intangible assets – goodwill	139,255	953	140,208
Incremental deferred income tax asset on acquisition	15,285	-	15,285
Less: net financial liabilities (net of cash received £24,324, $39,487)	(375,310)	-	(375,310)
Other	(51,392)	-	(51,392)
Incremental deferred income tax liability on acquisition	(11,739)	(1,802)	(13,541)
Non-controlling interest	(31,810)	-	(31,810)
Total cash consideration	213,476	-	213,476

The amount allocated to goodwill is not deductible for income tax purposes.

Disposition of Partial Interest in Bristol Water

On May 10, 2012, Capstone sold to I-Environment Investments Ltd, a subsidiary of ITOCHU Corporation, a 20% indirect interest in Bristol Water plc. I-Environment Investments Ltd acquired a 2/7^{ths} ownership interest in CSE Water UK Limited, which indirectly owns a 70% interest in Bristol Water plc. Capstone received $69,213 of net proceeds on sale and used the funds to repay the remaining $28,975 on the senior debt facility and $39,000 on the CPC-Cardinal credit facility, retaining cash of $1,238.

Following this sale, Capstone retained a 50% beneficial interest in Bristol Water and will continue to consolidate based on retention of control. Capstone recorded the transaction as a transfer of equity to non-controlling interest holders as follows:

As at May 10, 2012 ($000s)	$
Proceeds on sale (£43,500)	70,274
Transaction costs	(1,061)
Net proceeds on sale	69,213
Taxes payable for gain on sale	(850)
Adjustment to total equity	68,363
Non-controlling interest adjustment	(52,408)
Retained earnings adjustment	15,955

In addition, the portion of cumulative differences on translation related to Bristol Water has been adjusted to the non-controlling interest acquired by ITOCHU Corporation as follow:

($000s)	AOCI	NCI
Non-controlling interest adjustment for sale of partial interest	-	52,408
Transfer of cumulative differences on translation of foreign operations	749	(749)
Non-controlling interest adjustment, net	749	51,659

6. LOANS RECEIVABLE

The following table summarizes the loans receivable from Värmevärden and Chapais:

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Värmevärden	33,539	81,587
Chapais	4,743	5,221
	38,282	86,808
Less: current portion	(1,039)	(984)
Total long-term loans receivable	37,243	85,824

The following table summarizes the change in the loan receivable from Värmevärden during the period:

	Six months ended Jun 30, 2012		Year ended Dec 31, 2011	
($000s)	SEK	$	SEK	$
Opening balance	551,808	81,587	551,808	84,828
Principal repayment	(324,267)	(48,100)	-	-
Realized foreign exchange gain	-	136	-	-
Unrealized foreign exchange gain (loss)	-	(84)	-	(3,241)
Ending balance	227,541	33,539	551,808	81,587

During the first quarter of 2012, Värmevärden's parent company, Sefyr Värme AB, in which Capstone holds a 33.3% indirect investment, completed an approximately $150,000 (1,000,000 SEK) offering of senior secured bonds to select institutional investors. The bonds have a five-year term, are non-amortizing and carry a coupon of 7.0%.

Proceeds from the issuance were distributed to the owners of Sefyr Värme AB, with Capstone receiving approximately $49,400 which was used to repay a portion of the senior credit facility. The distribution of $49,400 was comprised of a $48,100 shareholder loan repayment and a payment of $1,300 of accrued interest. Refer to note 11 (Long-term debt).

In March 2012, the shareholder loan receivable from Värmevärden was amended. The annual interest rate is 7.944%, effective January 1, 2012. (2011 - 7.965%)

7. EQUITY ACCOUNTED INVESTMENTS

As at ($000s)	Jun 30, 2012 Ownership %	Jun 30, 2012 Carrying value	Dec 31, 2011 Ownership %	Dec 31, 2011 Carrying value
Macquarie Long Term Care L.P. (“MLTCLP”)	45.0%	106	45.0%	106
Värmevärden	33.3%	15,673	33.3%	15,887
Chapais	31.3%	-	31.3%	-
		15,779		15,993

See note 6 for detail on loans receivable with Värmevärden and Chapais.

The change in the Corporation’s total equity accounted investments for the periods ended is as follow:

($000s)	Opening balance	Equity accounted income (loss)	Equity share of OCI	Return of capital	Ending balance
Three months ended June 30, 2012	17,798	(602)	(434)	(983)	15,779
Six months ended June 30, 2012	15,993	843	(74)	(983)	15,779

8. CAPITAL ASSETS

($000s)	Jan 1, 2012	Additions	Disposals	Foreign exchange	Transfers	Jun 30, 2012
Cost						
Land	2,707	-	-	29	-	2,736
Equipment and vehicles	8,389	468	(20)	211	1,261	10,309
Property and plant	790,178	2,456	(3,149)	4,416	21,036	814,937
Infrastructure assets	271,485	33,888	-	4,260	1,500	311,133
Construction in progress	35,750	39,603	-	542	(24,177)	51,718
	1,108,509	76,415	(3,169)	9,458	(380)	1,190,833
Accumulated depreciation						
Equipment and vehicles	(3,568)	(857)	20	(168)	-	(4,573)
Property and plant	(126,465)	(19,925)	2,283	(2,069)	-	(146,176)
Infrastructure assets	(1,020)	(2,373)	13	(829)	-	(4,209)
Net carrying value	977,456	53,260	(853)	6,392	(380)	1,035,875

The reconciliation of capital asset additions to cash additions on the consolidated statement of cash flow was:

Six months ended ($000s)	Jun 30, 2012	Jun 30, 2011
Additions	76,415	87,014
Adjustment for change in capital amounts included in accounts payable and accrued liabilities	(13,476)	(37,944)
Additions to computer software (intangible assets)	380	-
Net foreign exchange difference	225	-
Cash additions	63,544	49,070

9. INTANGIBLES

($000s)	Jan 1, 2012	Additions	Foreign exchange	Transfers	Jun 30, 2012
Assets					
Computer software	4,220	28	347	380	4,975
Electricity supply and gas purchase contracts	108,048	-	-	-	108,048
Water rights	73,018	-	-	-	73,018
Licence	21,012	-	246	-	21,258
Goodwill	135,512	-	2,550	-	138,062
Accumulated amortization					
Computer Software	(550)	(917)	(309)	-	(1776)
Electricity supply and gas purchase contracts	(43,395)	(3,774)	-	-	(47,169)
Water rights	(9,561)	(1,055)	-	-	(10,616)
	288,304	(5,718)	2,834	380	285,800
Provisions					
Electricity supply and gas purchase contracts	12,257	-	-	-	12,257
Utilization	(7,363)	(813)	-	-	(8,176)
	4,894	(813)	-	-	4,081

10. RETIREMENT BENEFIT PLANS

Employees of the Corporation's operating businesses participate in various retirement benefit plans as follows.

Defined Contribution Plan

The total expense recorded in the consolidated statement of income for the three and six months ended June 30, 2012 was $334 and $632, respectively. The expense is composed of $542 for Bristol Water and $90 for Cardinal for the six months ended June 30, 2012.

Defined Benefit Plan

The retirement benefit surplus on the statements of financial position at June 30, 2012 was $48,804 (December 31, 2011 - $60,104)

Employer contributions paid in the three and six months ended June 30, 2012 to the defined benefit plan were $1,032 and $2,425, respectively. The contributions are entirely incurred at Bristol Water.

11. LONG-TERM DEBT

(A) Components of Long-term Debt

As at ($000s)	Jun 30, 2012	Dec 31, 2011
CPC-Cardinal credit facility	12,300	85,000
Erie Shores project debt	100,356	102,933
Amherstburg Solar Park project debt	92,169	94,267
Hydro facilities senior secured and subordinated bonds	98,837	-
Wawatay facility's levelization liability	-	26,313
Power	303,662	308,513
Bank loans	39,457	38,956
Term loans	421,910	413,702
Debentures	2,039	2,008
Irredeemable cumulative preferred shares	25,974	25,673
Utilities - water	489,380	480,339
Senior debt facility	-	78,375
CPC-Cardinal credit facility	-	34,000
Convertible debentures	40,457	40,238
Corporate	40,457	152,613
	833,499	941,465
Less: deferred financing costs	(6,331)	(6,421)
Long-term debt	827,168	935,044
Less: current portion	(49,147)	(230,899)
	778,021	704,145

CPC-Cardinal credit facility

Capstone repaid $106,700 of the CPC-Cardinal credit facility. On May 10, 2012, $39,000 was repaid with proceeds from the partial sale of Bristol Water (refer to note 5 Acquisition and Disposal). Additionally, $67,700 was repaid on June 6, 2012 with proceeds from the financing of the hydro power facility.

On July 31, 2012, Capstone obtained a commitment from a Canadian chartered bank for a new credit facility (the "New Facility") in the aggregate amount of up to $27,300, comprised of a $12,300 term loan to be used to repay the outstanding balance on the CPC-Cardinal credit facility and a $15,000 revolving facility. The New Facility will mature on June 30, 2014 and financial close is expected to occur in the third quarter of 2012.

Hydro facilities senior secured and subordinated secured bonds

On June 6, 2012, MPT Hydro LP completed a $100,621 debt offering to recapitalize the Dryden, Hluey Lakes, Sechelt and Wawatay facilities (the "Hydro facilities"). The debt offering comprising $80,379 of senior secured bonds and $20,242 of subordinated secured bonds. The senior secured and subordinated secured bonds are fully amortizing with terms of 28 and 29 years and bearing interest at fixed rates of 4.56% and 7.0%, respectively. The bonds are secured by the Hydro facilities alone and are non-recourse to the Corporation's other businesses.

Proceeds of the bond offerings were first used to repay $27,239, the balance of the levelization debt at the Wawatay hydro facility, along with $1,785 of transaction costs, which were capitalized to the debt. In addition, Capstone cash funded $3,846 to the debt service and maintenance reserve accounts in accordance with the bond indenture which is presented as restricted cash and used $67,700 net proceeds to repay a portion of the CPC-Cardinal credit facility.

Senior debt facility

The Corporation repaid $49,400 from the proceeds of the Värmevärden bond issue (refer to note 6 Loan Receivable). On May 10, 2012, Capstone repaid the remaining $28,975 with proceeds from the partial sale of Bristol Water.

(B) Long-term Debt Covenants

For the three and six months ended and as at June 30, 2012, the Corporation and its subsidiaries were in compliance with all financial and non-financial debt covenants.

12. SHAREHOLDERS' EQUITY

The share capital of the Corporation was as follows:

As at ($000s)	Jun 30, 2012	Dec 31, 2011
Common shares	630,974	626,861
Class B exchangeable units	26,710	26,710
Preferred shares	72,020	72,020
	729,704	725,591

(A) Common Shares

	Three months ended Jun 30, 2012		Six months ended Jun 30, 2012	
($000s and 000s shares)	Shares	Carrying Value	Shares	Carrying Value
Opening balance	71,466	628,703	70,957	626,861
Common shares issued	-	-	-	(89)
Conversion of convertible debentures, net of cost	-	-	-	-
Dividend reinvestment plan	595	2,271	1,104	4,202
Ending balance	72,061	630,974	72,061	630,974

(B) Dividends Declared

	Three months ended		Six Months ended	
($000s)	Jun 30, 2012	Jun 30, 2011	Jun 30, 2012	Jun 30, 2011
Common shares	9,695	9,681	21,458	19,160
Class B exchangeable units	536	536	1,072	1,072
	10,231	10,217	22,530	20,232
Preferred shares	938	-	1,876	-
	11,169	10,217	24,406	20,232

13. EARNINGS PER SHARE ("EPS")

	Three months ended		Six months ended	
($000s)	Jun 2012	Jun 2011	Jun 2012	Jun 2011
Net income (loss)	(609)	(30,370)	15,575	10,962
Non-controlling interest	(3,959)	-	(6,762)	-
Dividends declared on preferred shares	(938)	-	(1,876)	-
Net income (loss) available to common shareholders	(5,506)	(30,370)	6,937	10,962
Weighted average number of common shares outstanding	75,013	61,759	74,734	61,058
Basic and Diluted EPS	(0.073)	(0.492)	0.093	0.180

The convertible debentures are anti-dilutive for the three- and six-month periods ended June 30, 2012 and 2011.

14. SHARE-BASED COMPENSATION

(A) Deferred Share Units ("DSU")

Capstone granted 3,500 DSUs during the second quarter of 2012 and 7,468 year-to-date. The five-day volume weighted average price ("VWAP") per DSU granted on April 2, 2012 was 4.29 dollars. As at June 30, 2012, the $68 carrying value of the DSUs was based on a market price of 4.01 dollars.

(B) Long-term Incentive Plan

Capstone granted 253,959 Restricted Stock Units ("RSU") and 141,431 Performance Share Units ("PSU") during the first six months of 2012. The five-day VWAP per RSU and PSU granted on January 3, 2012 was 3.78 dollars and 4.23 dollars per RSU granted on March 23, 2012. As at June 30, 2012, the carrying value of the RSUs was $1,395 and $770 for the PSUs based on a market price of 4.01 dollars.

15. EXPENSES – ANALYSIS BY NATURE

Three months ended Jun 30,		2012			2011	
($000s)	Operating	Administrative	Total	Operating	Administrative	Total
Fuel	17,700	-	17,700	18,631	-	18,631
Chemicals and supplies	18,266	-	18,266	279	-	279
Wages and benefits	6,359	1,660	8,019	1,651	1,148	2,799
Maintenance	1,444	-	1,444	1,421	-	1,421
Manager fees	522	-	522	458	-	458
Insurance	475	-	475	352	-	352
Property taxes	294	-	294	165	-	165
Business development	-	26	26	-	454	454
Internalization	-	-	-	-	18,611	18,611
Other	1,802	1,993	3,795	1,468	853	2,321
Total	46,862	3,679	50,541	24,425	21,066	45,491

Six months ended Jun 30,		2012			2011	
($000s)	Operating	Administrative	Total	Operating	Administrative	Total
Fuel	38,390	-	38,390	37,891	-	37,891
Chemicals and supplies	36,770	-	36,770	680	-	680
Wages and benefits	12,048	3,207	15,255	3,521	1,148	4,669
Maintenance	2,218	-	2,218	2,396	-	2,396
Insurance	957	-	957	788	-	788
Manager fees	797	-	797	944	1,645	2,589
Property taxes	607	-	607	438	-	438
Business development	-	82	82	-	1,686	1,686
Internalization	-	-	-	-	19,246	19,246
Other	3,775	2,562	6,337	2,517	2,070	4,587
Total	95,562	5,851	101,413	49,175	25,795	74,970

16. SEGMENTED INFORMATION

The Corporation has three reportable segments based on how management has organized the business to assess performance and for operating and capital allocation. Each reportable segment has similar economic characteristics based on the nature of the products or services, type of customers, method of distributing their products or services and regulatory environment. Management evaluates the performance of these segments primarily on revenue and cash flows from operations.

Infrastructure segments consist of:	Geographical Location
Power The Corporation's investments in gas cogeneration, wind, hydro, biomass power and solar power assets.	Canada
Utilities – water The regulated water services business (Bristol Water), in which the Corporation holds a 50% indirect interest (70% October 5, 2011 – May 10, 2012).	United Kingdom
Utilities – district heating ("DH") The district heating business (Värmevärden), in which the Corporation holds a 33.3% indirect interest.	Sweden

	Three months ended Jun 30, 2012					Three months ended Jun 30, 2011				
		Utilities					Utilities			
($000s)	Power	Water	DH	Corporate	Total	Power	Water	DH	Corporate	Total
Revenue	40,132	45,717	-	-	85,849	37,028	-	-	-	37,028
Depreciation of capital assets	(6,645)	(4,848)	-	(95)	(11,588)	(5,946)	-	-	-	(5,946)
Amortization of intangible assets	(2,001)	(455)	-	(21)	(2,477)	(1,959)	-	-	(3)	(1,962)
Interest income	148	233	654	8	1,043	181	-	1,692	20	1,893
Interest expense	(5,625)	(5,679)	-	(1,703)	(13,007)	(4,094)	-	-	(910)	(5,004)
Income tax recovery (expense)	-	(2,997)	-	(3,474)	(6,471)	-	-	-	(4,297)	(4,297)
Net income (loss)	(3,016)	9,496	(752)	(6,337)	(609)	(6,374)	-	(510)	(23,486)	(30,370)
Cash flow from operations	14,358	15,521	654	(6,654)	23,879	21,451	-	1,692	(31,496)	(8,353)
Additions to capital assets	2,392	31,066	-	35	33,493	42,374	-	-	-	42,374

	Six months ended Jun 30, 2012					Six months ended Jun 30, 2011				
		Utilities					Utilities			
($000s)	Power	Water	DH	Corporate	Total	Power	Water	DH	Corporate	Total
Revenue	90,775	87,230	-	-	178,005	83,943	-	-	-	83,943
Depreciation of capital assets	(13,272)	(9,690)	-	(193)	(23,155)	(11,895)	-	-	-	(11,895)
Amortization of intangible assets	(4,005)	(901)	-	(27)	(4,933)	(3,896)	-	-	(9)	(3,905)
Interest income	301	557	2,005	12	2,875	402	-	1,692	232	2,326
Interest expense	(11,963)	(11,822)	-	(4,078)	(27,863)	(8,215)	-	-	(1,896)	(10,111)
Income tax recovery (expense)	-	(1,596)	-	(6,880)	(8,476)	-	-	-	32,693	32,693
Net income (loss)	10,386	18,838	3,843	(17,492)	15,575	5,286	-	(2,924)	8,600	10,962
Cash flow from operations	37,706	31,884	2,005	(16,495)	55,100	42,176	-	1,692	(38,104)	5,764
Additions to capital assets	2,862	73,491	-	62	76,415	87,014	-	-	-	87,014

	As at Jun 30, 2012					As at Dec 31, 2011				
		Utilities					Utilities			
($000s)	Power	Water	DH	Corporate	Total	Power	Water	DH	Corporate	Total
Total assets	632,555	946,097	49,456	25,684	1,653,792	656,871	913,811	97,458	29,604	1,697,744
Total liabilities	344,081	690,087	-	116,524	1,150,692	287,780	663,454	-	298,540	1,249,774

17. NON-CASH WORKING CAPITAL

The change in non-cash working capital is composed of the following:

Six months ended ($000s)	Jun 30, 2012	Jun 30, 2011
Accounts receivable	8,555	1,175
Other assets	282	430
Accounts payable and other liabilities	(13,566)	1,258
	(4,729)	2,863

18. COMMITMENTS AND CONTINGENCIES

The Corporation, either directly or indirectly through its subsidiaries, has entered into various contracts and commitments as disclosed in the annual consolidated financial statements for the year ended December 31, 2011. No material developments arose during the six-month period ended June 30, 2012.

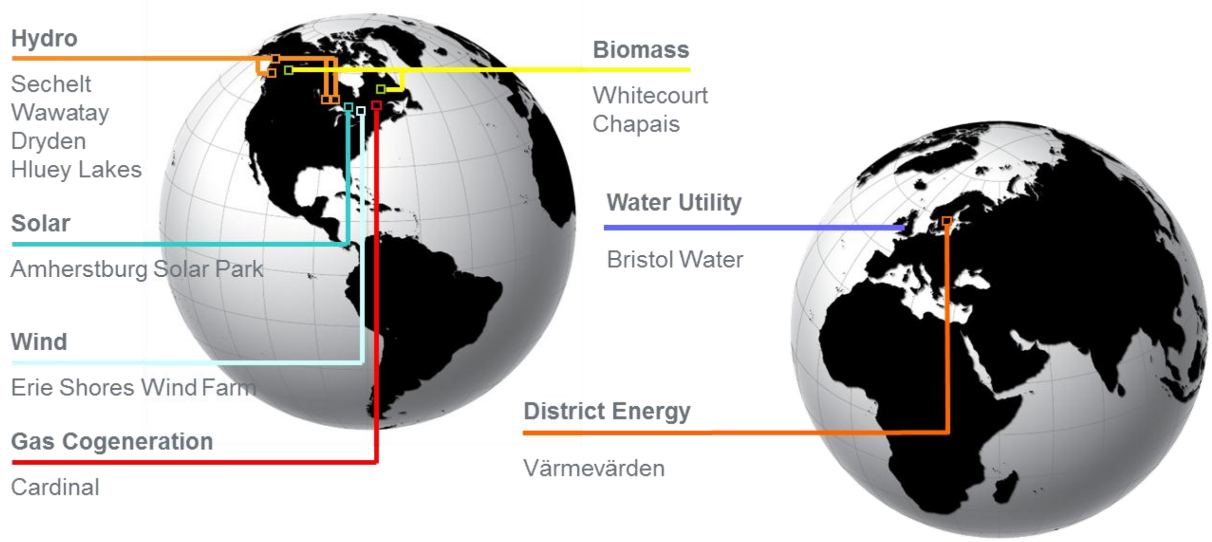
19. RELATED PARTY TRANSACTIONS

No related party transactions occurred in the six months ended June 30, 2012.

20. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the current period's presentation.

PORTFOLIO



POWER

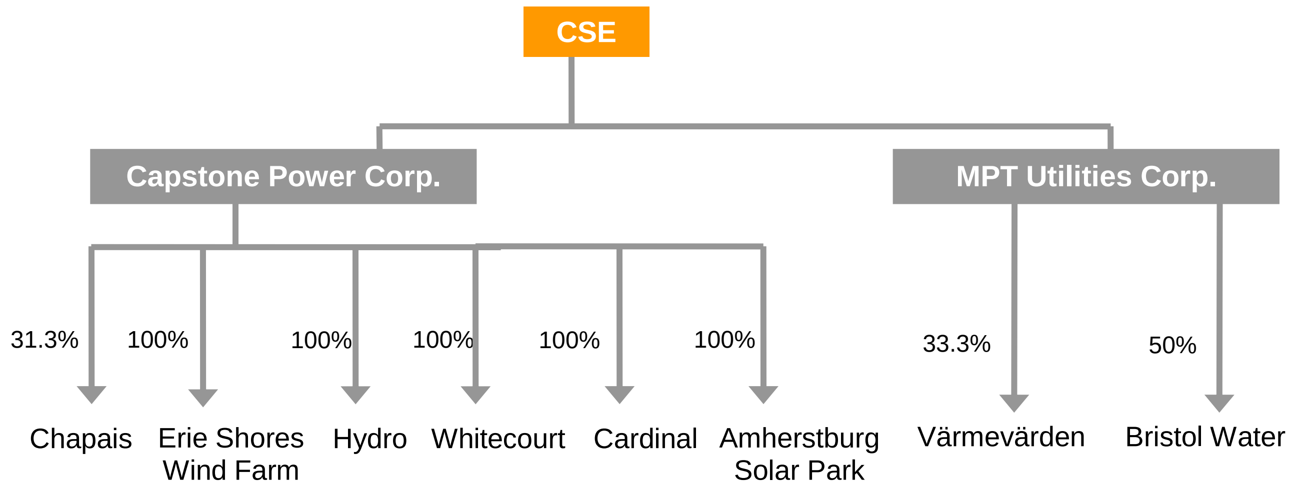
Business	Year Built	Interest	Net Capacity (MW)	PPA Counterparty	PPA Expiry	Fuel Supply Counterparty	Fuel Supply Expiry	Employees
Cardinal	1994	100%	156	OEFC	2014	Husky	2015	18
Erie Shores[1]	2006	100%	99	OPA	2026	n/a	n/a	10
Whitecourt	1994	100%	25	TransAlta	2014	Millar Western	2016	33
Sechelt	1997	100%	16	BC Hydro	2017	n/a	n/a	n/a
Wawatay	1992	100%	14	OEFC	2042	n/a	n/a	n/a
Hluey Lakes	2000	100%	3	BC Hydro	2020	n/a	n/a	n/a
Dryden	Various	100%	3	OEFC	2020	n/a	n/a	n/a
Amherstburg	2011	100%	20	OPA	2031	n/a	n/a	n/a
Chapais[2]	1995	31.3%	28	Hydro-Québec	2015	Barrette/Chantiers/ Société en commandite Scierie Opitciwan	2015	n/a

UTILITIES

Business	Interest	Capacity	Counterparties	Length of Network	Population Served	Regulated	Employees
Värmevärden	33.3%	Heat production capacity of 786 MWth	Mix of industrial and retail customers, with industrial counterparties representing approximately one-third of revenue	317 kilometres	163,000	No	89
Bristol Water	50%	Average daily supply of 278 million litres	Domestic or residential customers represent 75% of revenue with non-domestic customers representing the balance	6,670 kilometres	1.16 million	UK Water Services Regulation Authority	510

(1) One 1.5 MW turbine is owned by a landowner.
(2) CSE's investment in Chapais consists of a 31.3% interest in one of two classes of preferred shares, a 24.8% interest in Tranche A and B debt, and a 50% interest in Tranche C debt.

ORGANIZATIONAL STRUCTURE



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