ACCOUNTING POLICIES AND INTERNAL CONTROL

Significant Changes in Accounting Standards

The consolidated financial statements have been prepared in accordance with IFRS.

Future Accounting Changes

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after January 1, 2013 and 2015, and have not been applied in preparing these consolidated financial statements. Those which may be relevant to Capstone are set out below. Capstone does not plan to adopt these standards early.

Title of the New IFRS (1)	Impact to Capstone
IFRS 9, Jan 1, 2015 Financial Instruments	Capstone's assessment of the impact of this standard is ongoing.
IFRS 10, 11 and 12, Jan 1, 2013 Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities	Capstone will adopt IFRS 10, 11 and 12 for the annual period beginning on January 1, 2013. Implementation of these standards will have no material impact on Capstone's consolidated financial statements, but will increase disclosure of interests in other entities.
IFRS 13, Jan 1, 2013 Fair Value Measurement	Capstone will adopt IFRS 13 prospectively beginning on January 1, 2013. Implementation of this standard will have no material impact on Capstone's consolidated financial statements.
IAS 19, Jan 1, 2013 Employee Benefits	Capstone will adopt the amendment to IAS 19 retrospectively as a change in accounting policy for the annual period beginning on January 1, 2013. Implementation of this amendment is limited to Bristol Water which has a defined benefit pension plan. The impact on Capstone's consolidated financial statements is: i) The expected return on plan assets must be calculated using the same discount rate as the pension obligation, which will affect interest expense and net income, and is then offset in comprehensive income. ii) Certain costs will be required to be recognized as period costs and will be reclassified from net interest in the statement of income to current service costs which are included in operating expenses.
IAS 27, Jan 1, 2013 Separate Financial Statements	Capstone will adopt the amendment to IAS 27 for the annual period beginning on January 1, 2013. Implementation will have no material impact on Capstone's consolidated financial statements.
IAS 28, Jan 1, 2013 Investments in Associates and Joint Ventures	Capstone will adopt the amendment to IAS 28 for the annual period beginning on January 1, 2013. Implementation will have no material impact on Capstone's consolidated financial statements.

(1) See the note 2 to the consolidated financial statement for the year ended December 31, 2012 for further detail about the nature of these future accounting changes.

Accounting Estimates

The 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 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, tax rates and current and future taxable income
• 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

Capstone's CEO and CFO are required by the various provincial securities regulators to certify annually that they have designed, or caused to be designed, Capstone's disclosure controls and procedures, as defined in the Canadian Securities Administrators' National Instrument 52-109 ("NI 52-109"), and that they have evaluated the effectiveness of these controls and procedures in the applicable period. Disclosure controls are those controls and other procedures that are designed to provide reasonable assurance that the relevant information that Capstone is required to disclose is recorded, processed and reported within the timeframes specified by such securities regulators.

Capstone's management, under the supervision of and with the participation of the CEO and CFO, has designed internal controls over financial reporting, as defined in NI 52-109. The purpose of internal controls over financial reporting is to provide reasonable assurance regarding the reliability of Capstone's financial reporting, in accordance with IFRS, focusing in particular on controls over information contained in the audited annual and unaudited interim consolidated financial statements. The internal controls are not expected to prevent and detect all misstatements due to error or fraud.

During 2012, Capstone continued to improve internal control over financial reporting by adding a third-party internal audit function to objectively evaluate and advise management and the Board of Directors.

The CEO and CFO have concluded that Capstone's disclosure controls and procedures were effective as at December 31, 2012 to ensure that information required to be disclosed in reports that Capstone files or submits under Canadian securities legislation is recorded, processed, summarized and reported within applicable time periods.

As at December 31, 2012, Capstone's management had assessed the effectiveness of Capstone's internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission in Internal Control – Integrated Framework. Based on this assessment, management has determined that Capstone's internal control over financial reporting was effective as at December 31, 2012.