



## Management's Discussion and Analysis

For the year ended December 31, 2016

## FORWARD-LOOKING INFORMATION

The following **Management's Discussion and Analysis (MD&A)** highlights Inter Pipeline Ltd. and its subsidiaries (together, Inter Pipeline) significant business results and statistics for the three month period and year ended December 31, 2016, to provide readers with information about Inter Pipeline, including management's assessment of its future plans and operations. This information may not be appropriate for other purposes. This MD&A contains certain forward-looking statements or information (collectively referred to as "forward-looking statements") within the meaning of applicable securities legislation. All statements, other than statements of historical fact included in the MD&A, which address activities, events or developments that Inter Pipeline expects or anticipates to occur in the future, are forward-looking statements. Forward-looking statements often contain terms such as "may", "will", "should", "anticipate", "expect", "continue", "estimate", "believe", "project", "forecast", "plan", "intend", "target", "outlook", "focus", "could" and similar words suggesting future outcomes or statements regarding an outlook. Forward-looking statements in this MD&A may include, but are not limited to, statements regarding: 1) Inter Pipeline's belief that it is well positioned to maintain its current level of dividends to its shareholders; 2) Inter Pipeline being well positioned to operate and grow in the future including anticipated benefits of acquisitions, growth and development opportunities associated with acquisitions; 3) financial forecasts or anticipated financial performance; 4) timing and cost of capital projects, and forward EBITDA (as defined herein) estimates in respect of these projects; 5) capital expenditure forecasts; and 6) the plans and forecasts described under the **OUTLOOK** section.

Readers are cautioned not to place undue reliance on forward-looking statements; as such statements are not guarantees of future performance. Inter Pipeline in no manner represents that actual results, levels of activity and achievements will be the same in whole or in part as those set out in the forward-looking statements herein. Such information, although considered reasonable by Inter Pipeline may later prove to be incorrect and actual results may differ materially from those anticipated in the forward-looking statements. Inter Pipeline applies a variety of factors and assumptions when making forward-looking statements and making forecasts, projections, predictions or estimations, which include, but are not limited to, Inter Pipeline's ability to successfully implement its strategic initiatives and achieve expected benefits; Inter Pipeline's ability to maintain its investment grade credit ratings; the availability and price of labour, equipment and materials; assumptions concerning operational reliability; the availability and price of energy commodities; the availability of adequate levels of insurance; and general economic and business conditions.

By their nature, forward-looking statements are subject to various known and unknown risks, uncertainties and other factors, which are beyond Inter Pipeline's control, including, but not limited to: the status, credit risk and continued existence of customers having contracts with Inter Pipeline and its affiliates; competitive factors, pricing pressures and supply and demand in the oil and gas transportation, natural gas liquids (NGL) extraction and storage industries; fluctuations in currency and interest rates; risks of war, hostilities, civil insurrection, instability and terrorist actions, as well as political and economic conditions, in or affecting countries in which Inter Pipeline and its affiliates operate; public opinion regarding the production, transportation and use of oil and gas; severe weather and environmental conditions; risks associated with technology; Inter Pipeline's ability to access external sources of debt and equity capital; the potential delays of, and costs of overruns on, construction projects in all of Inter Pipeline's business segments; Inter Pipeline's ability to make capital investments and the amounts of capital investments; changes in laws and regulations, including environmental, regulatory and taxation laws, and the interpretation of such changes to Inter Pipeline's business; the risks associated with existing and potential or threatened future lawsuits and regulatory actions against Inter Pipeline and its affiliates; increases in maintenance, operating or financing costs; difficulty in obtaining necessary regulatory approvals or land access rights and maintenance of support of such approvals and rights; the realization of the anticipated benefits of acquisitions; and such other risks and uncertainties described from time to time in Inter Pipeline's reports and filings with the Canadian securities authorities. The impact of any one assumption, risk, uncertainty or other factor on a particular forward-looking statement cannot be determined with certainty, as these are interdependent and Inter Pipeline's future course of action depends on management's assessment of all information available at the relevant time.

**Readers are cautioned that the foregoing list of assumptions, risks, uncertainties and factors is not exhaustive. See also the section entitled RISK FACTORS for further risk factors. The forward-looking statements contained in this MD&A are made as of the date of this document and, except to the extent expressly required by applicable securities laws and regulations, Inter Pipeline assumes no obligation to update or revise forward-looking statements made herein or otherwise, whether as a result of new information, future events, or otherwise. The forward-looking statements contained in this document and all subsequent forward-looking statements, whether written or oral, attributable to Inter Pipeline or persons acting on Inter Pipeline's behalf are expressly qualified in their entirety by these cautionary statements.**

# Management's Discussion and Analysis

## For the three month period and year ended December 31, 2016

The MD&A provides a detailed explanation of Inter Pipeline's operating results for the three month period and year ended December 31, 2016, as compared to the three month period and year ended December 31, 2015. The MD&A should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2016, the unaudited condensed interim consolidated financial statements (interim financial statements) and MD&A for the quarterly periods ended March 31, June 30 and September 30, 2016, the MD&A and audited consolidated financial statements for the year ended December 31, 2015, the **Annual Information Form**, and other information filed by Inter Pipeline at [www.sedar.com](http://www.sedar.com).

Financial information presented in this MD&A is based on information in Inter Pipeline's consolidated financial statements prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

This MD&A reports certain financial measures that are not recognized by Canadian generally accepted accounting principles (GAAP), as outlined in the Chartered Professional Accountant (CPA) Handbook Part I, and used by management to evaluate the performance of Inter Pipeline and its business segments. Since certain non-GAAP financial measures may not have a standardized meaning, securities regulations require that non-GAAP financial measures are clearly defined, qualified and reconciled with their nearest GAAP measure. See the **NON-GAAP FINANCIAL MEASURES** section for further information on the definition, calculation and reconciliation of non-GAAP financial measures. All amounts are in Canadian dollars unless specified otherwise.

Management determines whether information presented in this MD&A is material based on whether it believes a reasonable investor's decision to buy, sell or hold securities in Inter Pipeline would likely be influenced or changed if the information was omitted or misstated.

## Table of Contents

FORWARD-LOOKING INFORMATION.....	2	OUTSTANDING SHARE DATA .....	33
2016 HIGHLIGHTS .....	4	RISK MANAGEMENT AND FINANCIAL INSTRUMENTS.....	33
FOURTH QUARTER HIGHLIGHTS .....	4	TRANSACTIONS WITH RELATED PARTIES.....	35
PERFORMANCE OVERVIEW .....	5	CONTROLS AND PROCEDURES .....	35
OUTLOOK.....	7	CRITICAL ACCOUNTING ESTIMATES.....	36
RESULTS OF OPERATIONS.....	9	FUTURE ACCOUNTING PRONOUNCEMENTS .....	45
SUMMARY OF QUARTERLY RESULTS .....	25	RISK FACTORS.....	46
LIQUIDITY AND CAPITAL RESOURCES .....	26	NON-GAAP FINANCIAL MEASURES.....	66
DIVIDENDS TO SHAREHOLDERS.....	32	ADDITIONAL INFORMATION.....	69

## 2016 HIGHLIGHTS

- Generated record funds from operations (FFO) of \$849 million, a 10 percent increase over 2015 results
- Realized a net income increase of 3 percent, to a record \$478 million for the year
- Declared annual cash dividends of \$539 million, or \$1.57 per share
- Attractive annual payout ratio\* of 66 percent
- Announced an annualized dividend increase of \$0.06 per share, the 14<sup>th</sup> consecutive increase for Inter Pipeline shareholders
- Average annual throughput volumes on Inter Pipeline's pipeline systems averaged a record 1,296,600 barrels per day (b/d)
- Acquired a large scale Canadian natural gas liquids midstream business for \$1.35 billion, providing a new platform for future growth
- Bulk liquid storage capacity utilization averaged a new record of 98 percent for the year, up from 94 percent in 2015
- Successfully raised over \$775 million of equity capital and \$800 million of term debt at attractive rates

## FOURTH QUARTER HIGHLIGHTS

- Record quarterly FFO of \$255 million, an increase of 20 percent from the same period in 2015
- Conservative quarterly payout ratio\* of 58 percent
- Average throughput volumes for Inter Pipeline's oil sands and conventional pipeline systems reached a new quarterly record of 1,372,800 b/d
- Purchased the remaining 15 percent interest in the Cold Lake pipeline system from Canadian Natural Resources Ltd. (Canadian Natural) for \$527.5 million
- Entered into a long-term transportation agreement with Canadian Natural for its Kirby North SAGD oil sands project
- Awarded \$200 million in royalty credits from the Government of Alberta's Petrochemical Diversification Program for the proposed propane dehydrogenation (PDH) facility

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section



## Year Ended December 31, 2016

Inter Pipeline generated record annual financial results as FFO increased \$74.7 million or 9.6% from \$774.1 million in 2015 to \$848.8 million in 2016. All four of Inter Pipeline's business segments surpassed prior year results led by the NGL processing business which benefitted from the inclusion of offgas processing FFO from the date of acquisition of Williams Canada, as well as, higher realized propane-plus frac-spreads and propane-plus volumes at the Cochrane straddle plant. The bulk liquid storage business generated record annual financial results due to the inclusion of results from Inter Terminals Sweden for the full year and increased utilization rates. The oil sands transportation business also produced record annual results largely due to expanded transportation service on the Polaris pipeline system. Record annual results were also obtained from the conventional oil pipelines business due to increased midstream marketing activities. Annual corporate costs increased from higher employee, rent and interest costs which were partially offset by leasehold inducement proceeds related to the new head office premises and lower current income taxes from tax synergies created from the acquisition of Williams Canada.

Inter Pipeline's net income increased \$14.6 million from \$463.0 million in 2015 to \$477.6 million in 2016. Net income was favourably impacted by the increase in FFO discussed above which included leasehold inducement proceeds of \$14.6 million that is not included in net income as it will be taken into net income over the term of the lease. Net income was also impacted by higher depreciation and amortization expense, a one-time onerous contract adjustment in the first quarter of 2016 and lower deferred income taxes.

Total dividends to shareholders increased \$42.1 million or 8.5% from \$497.1 million in 2015 to \$539.2 million in 2016, due to an increase in the number of common shares outstanding and higher monthly dividend rates. Common shares outstanding increased as a result of the common shares issued upon closing of the Williams Canada acquisition, the issuance of common shares related to the acquisition of the remaining 15% ownership interest in the Cold Lake pipeline system and from strong shareholder participation in Inter Pipeline's dividend reinvestment plan. Monthly dividend rates rose as a result of annualized dividend rate increases of \$0.09 and \$0.06 per share, effective November 2015 and November 2016, respectively. Inter Pipeline's payout ratio\* was 66.0% for the year ended December 31, 2016.

At December 31, 2016, Inter Pipeline's total debt outstanding was \$5,828.6 million, an increase of \$976.9 million from \$4,851.7 million at December 31, 2015. The increase was due to partially debt financing the acquisition of Williams Canada and the acquisition of the remaining 15% ownership interest in the Cold Lake pipeline system, and investing \$207.9 million (Inter Pipeline's share) on capital projects. Total debt includes non-recourse debt of \$1,490.6 million held at Inter Pipeline (Corridor) Inc. at December 31, 2016.

## Three Months Ended December 31, 2016

Inter Pipeline also generated strong fourth quarter financial results, as FFO increased \$43.3 million or 20.5% from \$211.4 million in 2015 to \$254.7 million in 2016. The increase in FFO primarily results from an incremental contribution from the NGL processing business due to the inclusion of offgas processing FFO from the Williams Canada acquisition, and higher realized propane-plus frac-spreads and propane-plus volumes at the Cochrane straddle plant. FFO was also favourably impacted by lower corporate costs due to a reduction in current income taxes, as discussed above, offset in part by higher employee, rent and interest expense.

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

Inter Pipeline's net income in the fourth quarter decreased \$9.2 million from \$138.0 million in 2015 to \$128.8 million in 2016. Net income benefitted from higher FFO as discussed above, which was more than offset by higher deferred income taxes, depreciation and amortization expense and loss on disposal of assets.

In the three months ended December 31, 2016, total dividends to shareholders increased by \$16.4 million or 12.7% from \$128.7 million in 2015 to \$145.1 million in 2016, for the same reasons discussed above. Inter Pipeline's payout ratio<sup>\*</sup> was 57.8% for the three months ended December 31, 2016.

Inter Pipeline's total debt outstanding at December 31, 2016 of \$5,828.6 million, increased \$232.0 million from September 30, 2016 of \$5,596.6 million, primarily due to funding the acquisition of the remaining 15% ownership interest in the Cold Lake pipeline system and incurring \$72.1 million (Inter Pipeline's share) in capital projects.

## OUTLOOK

Inter Pipeline owns and operates world scale energy infrastructure assets in Western Canada and Europe. Our long-term strategy is to acquire and develop high-quality assets that generate stable and predictable cash flow, while delivering strong returns to shareholders. In 2016, Inter Pipeline focused on leveraging value from our diversified asset base, controlling costs and capturing additional growth opportunities by completing two noteworthy acquisitions.

In September 2016, Inter Pipeline completed the acquisition of Williams Canada's Canadian NGL midstream businesses for approximately \$1.35 billion. Inter Pipeline is one of Canada's largest NGL processing businesses with ownership in three major straddle plants, two offgas plants, an offgas liquids pipeline and a fractionator, all located in Alberta. These facilities are capable of processing in excess of 6 billion cubic feet of natural gas per day and producing over 240,000 barrels per day of NGL.

In December, Inter Pipeline completed its second acquisition by purchasing Canadian Natural's 15% interest in the Cold Lake pipeline system for \$527.5 million. As a result, Inter Pipeline now owns 100% of the Cold Lake pipeline system. Both of these acquisitions were immediately accretive to FFO per share<sup>\*</sup> and are expected to provide Inter Pipeline with significant short-term and long-term growth opportunities.

In 2017, Inter Pipeline's planned \$570 million capital expenditure program, including approximately \$75 million of sustaining capital<sup>\*</sup>, will focus on developing, expanding and maintaining our four business segments. In particular, Inter Pipeline will place a high priority on advancing the development of an estimated \$3.1 billion integrated PDH and polypropylene (PP) facility within our NGL processing business segment. These facilities would convert low-cost, locally sourced propane into higher value polypropylene, a valuable recyclable plastic. Up to \$75 million is expected to be invested to advance detailed engineering and procure long-lead items prior to sanctioning. Should these proposed projects be fully sanctioned an additional \$195 million is expected to be invested in 2017 to continue the front-end design work and to begin construction. Subject to a sanctioning decision to be made by mid-2017, both the PDH and PP facilities are expected to enter commercial service by mid-2021. Approximately \$35 million of additional capital will be invested in the NGL processing business for smaller scale debottlenecking activities and other organic growth projects.

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<sup>\*</sup> Please refer to the NON-GAAP FINANCIAL MEASURES section

Inter Pipeline's oil sands transportation business is comprised of the Corridor, Cold Lake and Polaris pipeline systems and is underpinned by long-term commercial arrangements with creditworthy counterparties that generate stable cost-of-service FFO. Approximately \$115 million of growth capital will be invested across our three oil sands pipeline systems in 2017 with a primary focus on the construction of new diluent receipt and bitumen blend delivery connections. Inter Pipeline's three major oil sands pipeline systems have over 2.5 million b/d of installed pipeline capacity. This includes approximately 1.2 million b/d of bitumen blend capacity on the Cold Lake pipeline system, 879,000 b/d of diluent capacity on the Polaris pipeline system and 465,000 b/d of bitumen blend capacity on the Corridor pipeline system. Ultimate throughput capacities of 1.9 million b/d, 1.3 million b/d and 1.4 million b/d on the Cold Lake, Polaris and Corridor pipeline systems, respectively, can be achieved through the addition of pump stations and associated infrastructure.

Inter Pipeline's oil sands pipeline systems transported approximately 1,095,900 b/d of bitumen blend and diluent in 2016, up 4.8% compared to a year ago. The strong surplus capacity position that has been established in recent years on the Cold Lake, Polaris, and Corridor pipeline systems positions Inter Pipeline to capture new oil sands transportation connections over the longer-term. We have identified new investments involving potential long-term capital commitments of over \$4 billion. Though a number of developments have been delayed in the current commodity price environment, we will continue to aggressively pursue opportunities to utilize available spare capacity on our oil sands pipeline systems.

Conventional oil pipelines average annual throughput volumes were 200,700 b/d in 2016. As part of the 2016 capital program for this business segment Inter Pipeline successfully commissioned three light crude oil tanks at the Kerrobert terminal, adding 400,000 barrels of storage capacity. In 2017, Inter Pipeline expects to invest \$35 million to expand oil battery connections, add services and increase storage capacity across its conventional oil pipelines business segment.

Inter Pipeline's European bulk liquid storage business diversifies our asset base by both geography and market. With operations now in the United Kingdom (UK), Sweden, Denmark, Germany and Ireland the focus for this business segment in 2017 will be maintaining strong utilization levels and storage rates, economically expanding storage capacity and diversifying our product handling capabilities.

Demand for oil and chemical storage in Europe remains strong with average utilization rates increasing from 94% in 2015 to 98% in 2016. Approximately \$40 million will be invested in this business in 2017 to support tank expansions and other growth projects. This includes approximately \$20 million to complete the construction of five new chemical storage tanks, with an aggregate capacity of 175,000 barrels, at the Seal Sands terminal in the UK. This new capacity is supported by two new long-term contracts and is expected to be in-service by mid-2017.

Inter Pipeline is committed to maintaining a strong balance sheet and financial flexibility. In 2017, we expect to finance our capital expenditure program primarily through undistributed cash flow, our revolving credit facility and proceeds from our dividend reinvestment programs. In addition, the premium component of our Premium Dividend<sup>TM</sup> and Dividend Reinvestment Plan (DRIP) was re-instated in October 2016, which raises additional equity capital on a monthly basis. As at December 31, 2016, Inter Pipeline had \$587 million of available capacity on its \$1.5 billion revolving credit facility and ended the year with a consolidated net debt to total capitalization ratio<sup>\*</sup> of 57.2%.

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<sup>TM</sup> denotes trademark of Canaccord Genuity Corp.

<sup>\*</sup> Please refer to the NON-GAAP FINANCIAL MEASURES section



As a result of our strong financial position and the stable nature of our business, Inter Pipeline has solid investment grade credit ratings. Standard & Poor's (S&P) and DBRS Limited (DBRS) have assigned Inter Pipeline credit ratings of BBB+ and BBB (high), respectively, each with a stable trend. Inter Pipeline (Corridor) Inc. has investment grade credit ratings of A (stable outlook) from S&P and DBRS and A2 (stable outlook) from Moody's Investors Service (Moody's).

The FFO that underpins our monthly dividend is stable, diversified and largely supported by investment grade counterparties. Our extensive energy infrastructure base continues to be well positioned to compete for future, accretive growth opportunities both locally and internationally. We also have an exciting new platform for growth with the acquisition of the offgas processing business, including the future development of Alberta's first PDH and PP facilities. With a strong balance sheet and proven operational capabilities, Inter Pipeline is well positioned to continue to generate long-term positive results for our shareholders.

## RESULTS OF OPERATIONS

### Oil Sands Transportation Business Segment

	Three Months Ended December 31			Years Ended December 31		
	2016	2015	% change	2016	2015	% change
<i>Volumes (000s b/d)</i>						
Cold Lake (100% basis) <sup>(1)</sup>	<b>611.6</b>	565.4	8.2	<b>558.5</b>	561.4	(0.5)
Corridor	<b>393.9</b>	378.8	4.0	<b>378.8</b>	346.0	9.5
Polaris	<b>167.0</b>	167.6	(0.4)	<b>158.6</b>	138.7	14.3
	<b>1,172.5</b>	1,111.8	5.5	<b>1,095.9</b>	1,046.1	4.8
<i>(millions)</i>						
Revenue <sup>(2)</sup>	\$ <b>200.8</b>	\$ 213.4	(5.9)	\$ <b>778.6</b>	\$ 768.7	1.3
Operating expenses <sup>(2)</sup>	\$ <b>33.8</b>	\$ 35.3	(4.2)	\$ <b>131.5</b>	\$ 132.1	(0.5)
Funds from operations <sup>(2)</sup>	\$ <b>158.5</b>	\$ 157.8	0.4	\$ <b>581.6</b>	\$ 569.1	2.2
Capital expenditures <sup>(2)</sup>						
Growth <sup>(3)</sup>	\$ <b>5.7</b>	\$ 19.6		\$ <b>17.3</b>	\$ 146.4	
Sustaining <sup>(3)</sup>	<b>0.2</b>	0.3		<b>1.0</b>	1.1	
	\$ <b>5.9</b>	\$ 19.9		\$ <b>18.3</b>	\$ 147.5	

(1) Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

(2) For the three month period and year ended December 31, 2016, Cold Lake pipeline system includes the following amounts relating to non-controlling interest: revenue - \$3.9 million and \$41.6 million (\$12.8 million and \$51.5 million in 2015), respectively; operating expenses - \$0.4 million and \$8.9 million (\$2.8 million and \$9.8 million in 2015), respectively; FFO - \$3.5 million and \$32.0 million (\$9.8 million and \$41.0 million in 2015), respectively; and capital expenditures - \$0.1 million and \$1.1 million (\$1.0 million and \$8.3 million in 2015), respectively.

(3) Please refer to the NON-GAAP FINANCIAL MEASURES section.

The oil sands transportation business segment is comprised of the Cold Lake, Corridor and Polaris pipeline systems that transport petroleum products and provide related blending and handling services in Alberta.

The Cold Lake pipeline system is a bitumen blend and diluent pipeline system that transports diluted bitumen from the Cold Lake oil sands area of Alberta to delivery points in Hardisty and Edmonton, Alberta. Inter Pipeline owned an 85% interest in the Cold Lake pipeline system, however, effective November 1, 2016, Inter Pipeline acquired the remaining 15% interest, bringing its ownership interest to 100%.

The Corridor pipeline system is comprised of a bitumen blend pipeline, a diluent delivery pipeline, a feedstock pipeline and two products pipelines. It transports diluent from the Scotford upgrader located northeast of Edmonton, Alberta to the Muskeg River and Jackpine mines near Fort McMurray, Alberta and diluted bitumen produced from the mines back to the Scotford upgrader. In addition, feedstock and upgraded products are shipped between the Scotford upgrader and certain pipeline terminals in Edmonton. Corridor is the sole transporter of diluted bitumen produced by the Athabasca Oil Sands Project.

The Polaris pipeline system is a diluent pipeline system which provides diluent transportation service from the Edmonton area to the Athabasca and Cold Lake areas of Alberta.

See the **Description of the Business** section of the **Annual Information Form** for further information about the oil sands transportation business.

## Volumes

The oil sands transportation business transported average volumes of 1,172,500 b/d in the current quarter, an increase of 60,700 b/d or 5.5% from the same period in 2015 and average annual volumes of 1,095,900 b/d in 2016, an increase of 49,800 b/d or 4.8% over 2015.

On the Cold Lake pipeline system average volumes increased 46,200 b/d in the fourth quarter over the same period in 2015, largely due to higher volumes from FCCL Partnership's (FCCL), a business venture between Cenovus Energy and ConocoPhillips, Foster Creek oil sands project. In 2016, annual volumes on the Cold Lake pipeline system were fairly consistent with 2015, decreasing by 2,900 b/d. Volumes typically fluctuate on the Cold Lake pipeline system with the timing of steam injection cycles associated with certain shippers' production processes, however volume growth is anticipated over the long-term, which is consistent with shippers' published forecasts.

In the three months and year ended December 31, 2016, average volumes on the Corridor pipeline system increased 15,100 b/d and 32,800 b/d, respectively, from the same periods in 2015, largely due to higher volumes from the Jackpine mine. Wildfires in the Fort McMurray region in the second quarter of 2016 resulted in a temporary shut down for precautionary measures on a portion of the Corridor pipeline system but did not materially impact producers' transportation volumes.

Average volumes on the Polaris pipeline system in the fourth quarter of 2016 and 2015 were consistent, decreasing slightly by 600 b/d. Average annual volumes in 2016 increased 19,900 b/d from 2015, due to additional deliveries to Suncor's oil sands facilities, Husky's Sunrise, Canadian Natural's Kirby South and Athabasca Oil Corporation's (AOC) Hangingstone oil sands projects, as well as incremental diluent deliveries for Imperial's Kearn expansion which began in the third quarter of 2015. Wildfires in the Fort McMurray region in the second quarter of 2016 caused portions of the Polaris pipeline system to temporarily shut down for precautionary measures which impacted various producers' demand for diluent volumes.

## Revenue

The oil sands transportation business earns revenue for the transportation of petroleum products which are underpinned by a range of long-term cost-of-service contracts as defined in the adjusted EBITDA by contract type disclosure in the **NON-GAAP FINANCIAL MEASURES** section.

Oil sands transportation revenue decreased \$12.6 million in the current quarter and increased \$9.9 million for the full year in 2016, compared to the same periods in 2015. Revenue in the three months and year ended December 31, 2015, were

favourably impacted by one-time revenue adjustments of \$21 million and \$11 million, respectively, primarily related to capital fee payments on the Polaris and Cold Lake pipeline systems and a change in accounting policy. These adjustments were partially offset in the current quarter and more than offset in the full year of 2016 by incremental fees on the Polaris pipeline system from deliveries to Suncor's, AOC's Hangingstone and JACOS-Nexen Hangingstone oil sands projects. Annual revenues in 2016 also increased from higher capital fee revenue on the Polaris pipeline system from Imperial's Kearn expansion service which began in June 2015.

### **Operating Expenses**

Operating expenses in the oil sands transportation business segment typically have a limited impact on Inter Pipeline's FFO, as substantially all operating expenditures are recovered from shippers on the Cold Lake, Corridor and Polaris pipeline systems. Operating expenses in the oil sands transportation business decreased \$1.5 million and \$0.6 million in the three months and year ended December 31, 2016, respectively, from the same periods in 2015. This is largely due to lower property taxes, power costs and remediation costs.

### **Capital Expenditures**

In 2016, the oil sands transportation business incurred total growth capital expenditures\* of \$17.3 million. Approximately \$3 million relates to a new pipeline lateral and associated facilities connecting the Polaris pipeline system to the JACOS-Nexen Hangingstone project which was completed in the first quarter of 2016. The remaining growth capital expenditures\* relate to various system and facility upgrades and enhancements.

### **Acquisition of Cold Lake Non-Controlling Interest**

Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system from Canadian Natural. The acquisition was valued at \$527.5 million plus closing adjustments for working capital, resulting in total consideration transferred of \$532.6 million. Funding for the acquisition was partially provided through the issuance of 6,417,740 common shares of Inter Pipeline, for total proceeds of \$177.5 million, and the remaining balance of \$355.1 million was funded from the proceeds of the \$450 million Series 9 medium-term notes issuance.

Operating results for the acquired 15% interest in the Cold Lake pipeline system have been included in Inter Pipeline's consolidated net income attributable to shareholders since November 1, 2016, contributing an additional \$6.2 million to net income attributable to shareholders from the effective date of the acquisition to December 31, 2016. If the acquisition had taken place at January 1, 2016, for the year ended December 31, 2016, management estimates that the 15% interest in the Cold Lake pipeline system would have contributed an incremental \$34.1 million to pro forma net income attributable to shareholders. The pro forma information is not necessarily indicative of the results of operations that would have resulted had the acquisition been effective on the date indicated, or of future results.

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

The acquisition did not result in a change of control and therefore the transaction has been accounted for as an equity transaction with non-controlling interest, resulting in the following:

Consideration paid	\$	532.6
Items recognized directly in retained earnings:		
Long-term payable		21.0
Deferred tax liability on acquired assets and liabilities		26.2
Accounts receivable write-off		8.6
Reduction in net assets attributable to non-controlling interest		(332.3)
Decrease in equity attributable to shareholders of Inter Pipeline Ltd.	\$	256.1

## Conventional Oil Pipelines Business Segment

Volumes (000s b/d)	Three Months Ended December 31			Years Ended December 31		
	2016	2015	% change	2016	2015	% change
Bow River	89.2	96.3	(7.4)	90.2	99.5	(9.3)
Central Alberta	26.8	33.8	(20.7)	28.6	34.1	(16.1)
Mid-Saskatchewan	84.3	84.7	(0.5)	81.9	78.1	4.9
	<b>200.3</b>	214.8	(6.8)	<b>200.7</b>	211.7	(5.2)

  

(millions, except per barrel amount)

Revenue	\$ 111.0	\$ 89.0	24.7	\$ 365.0	\$ 322.4	13.2
Midstream product purchases	\$ 44.3	\$ 20.6	115.0	\$ 103.3	\$ 62.6	65.0
Operating expenses	\$ 14.3	\$ 17.0	(15.9)	\$ 62.9	\$ 65.2	(3.5)
Funds from operations	\$ 52.4	\$ 51.5	1.7	\$ 198.6	\$ 194.6	2.1
Revenue per barrel <sup>(2)</sup>	\$ 2.89	\$ 2.90	(0.3)	\$ 2.93	\$ 2.94	(0.3)
Capital expenditures						
Growth <sup>(1)</sup>	\$ 4.0	\$ 22.1		\$ 51.5	\$ 123.4	
Sustaining <sup>(1)</sup>	2.5	3.1		5.7	7.1	
	<b>\$ 6.5</b>	\$ 25.2		<b>\$ 57.2</b>	\$ 130.5	

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(2) Revenue per barrel represents total revenue of the conventional oil pipelines business segment less midstream marketing revenue, revenue from take-or-pay contracts for volume shortfalls and revenue/expense from over/short volumes, divided by actual volumes.

Inter Pipeline's conventional oil pipelines business is comprised of the Bow River, Central Alberta and Mid-Saskatchewan pipeline systems, located in Alberta and Saskatchewan. These pipeline systems provide for the transportation of petroleum products and related blending and handling services.

See the **Description of the Business** section of the **Annual Information Form** for further information about the conventional oil pipelines business.

## Volumes

Average volumes transported on the conventional oil pipelines decreased 14,500 b/d in the fourth quarter of 2016 and 11,000 b/d for the year, from the same periods in 2015. On the Bow River pipeline system volumes decreased 7,100 b/d and 9,300 b/d in the three months and year ended December 31, 2016, respectively, compared to the same periods in 2015. A reduction in producer activity levels arising from low commodity prices, natural production declines, weather related issues and third party refinery issues impacting first quarter south bound volumes were the primary drivers for the decrease. Volumes on the Central Alberta pipeline system decreased in the three months and year ended December 31, 2016 by 7,000 b/d and 5,500 b/d, respectively, from the comparable periods in 2015, due to a reduction in producer

activity and lower volumes at third party truck terminals. Mid-Saskatchewan pipeline system volumes decreased 400 b/d in the fourth quarter largely due to weather related issues. Volumes increased 3,800 b/d for the full year in 2016 due to increased volumes on the heavy oil system and the completion of several expansion projects in mid-2015 along with the Kerrobert terminal storage expansion project in mid-2016 to accommodate regional production increases from the Viking light oil play.

## Revenue

The conventional oil pipelines business earns revenue for the transportation of petroleum products in accordance with a number of fee-based contracts, while its midstream marketing activities generate revenue under a number of short-term commodity-based contracts. Please refer to the adjusted EBITDA by contract type disclosure in the **NON-GAAP FINANCIAL MEASURES** section for further information.

Revenue from conventional oil pipelines increased \$22.0 million and \$42.6 million in the three months and year ended December 31, 2016, respectively, from the same periods in 2015. Midstream marketing revenue increased \$25.8 million in the current quarter and \$53.3 million in the full year of 2016, over the same periods in 2015, largely due to increased blending activity. Transportation revenue decreased \$3.8 million and \$10.7 million in the fourth quarter and full year of 2016, from the same periods in 2015, primarily due to lower overall pipeline system volumes.

## Midstream Product Purchases

In the three months and year ended December 31, 2016, midstream product purchases increased \$23.7 million and \$40.7 million, respectively, over the same periods in 2015, due to higher product purchase volumes arising from increased blending activity, offset in part by lower product pricing.

## Operating Expenses

Operating expenses in the conventional oil pipelines business decreased \$2.7 million in the fourth quarter largely due to lower integrity and remediation costs, offset in part by higher employee related costs. Annual operating costs decreased \$2.3 million in 2016, from 2015, due to lower remediation and fuel and power costs, which were somewhat offset by higher employee and non-routine maintenance costs.

## Capital Expenditures

The conventional oil pipelines business incurred growth capital expenditures\* of \$51.5 million in 2016. Growth capital expenditures\* incurred on the recently completed 400,000 barrel crude oil storage expansion project at the Kerrobert Terminal on the Mid-Saskatchewan pipeline system were approximately \$40.0 million in 2016. The remaining 2016 growth capital expenditures\* of \$11.5 million relate to various pipeline system initiatives, enhancements and facility upgrades.

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

## NGL Processing Business Segment

### Natural gas processing

								Three Months Ended December 31	
2016				2015					
<i>mmcf/d</i>		<i>(000s b/d)</i>		<i>mmcf/d</i>		<i>(000s b/d)</i>			
Straddle plant	Throughput	Ethane	Propane-plus	Total	Throughput	Ethane	Propane-plus	Total	
Cochrane	2,084	47.1	31.4	78.5	1,853	38.4	30.0	68.4	
Empress V (100% basis)	970	22.8	12.4	35.2	837	20.7	11.3	32.0	
Empress II	-	-	-	-	-	-	-	-	
	3,054	69.9	43.8	113.7	2,690	59.1	41.3	100.4	

  

								Years Ended December 31	
2016				2015					
<i>mmcf/d</i>		<i>(000s b/d)</i>		<i>mmcf/d</i>		<i>(000s b/d)</i>			
Straddle plant	Throughput	Ethane	Propane-plus	Total	Throughput	Ethane	Propane-plus	Total	
Cochrane	1,954	38.1	30.9	69.0	1,799	39.8	28.4	68.2	
Empress V (100% basis)	966	22.1	12.5	34.6	878	22.3	11.2	33.5	
Empress II	-	-	-	-	-	-	-	-	
	2,920	60.2	43.4	103.6	2,677	62.1	39.6	101.7	

### Offgas processing

	Three Months Ended December 31	Year Ended December 31
	2016	2016
<i>(mmcf/d)</i>		
Offgas plants throughput volume <sup>(1)</sup>	145	40
<i>(000s b/d)</i>		
Offgas plants production volume <sup>(1)</sup>	27.6	7.7
Redwater Olefinic Fractionator sales volume <sup>(1)</sup>	29.9	8.1
Redwater Olefinic Fractionator volume composition <sup>(2)</sup>		
Ethane-ethylene	37%	38%
Paraffinic NGL		
Propane	30%	30%
Normal butane	8%	7%
Olefinic NGL		
Polymer grade propylene	13%	13%
Alky feed	8%	8%
Olefinic condensate	4%	4%

(1) Average volumes from offgas processing for the year ended December 31, 2016 is calculated by taking total volumes for 100 days of operations from the closing date of the acquisition on September 23, 2016 to December 31, 2016 divided by 366 days in 2016.

(2) Composition is based on production volumes, which may differ from sales volumes.

## NGL processing financial results

<i>(millions)</i>	Three Months Ended December 31			Years Ended December 31		
	2016	2015	% change	2016	2015	% change
Revenue <sup>(1)</sup>	\$ 191.1	\$ 88.5	115.9	\$ 435.1	\$ 370.8	17.3
Shrinkage gas <sup>(1)</sup>	\$ 88.5	\$ 43.4	103.9	\$ 194.1	\$ 183.1	6.0
Operating expenses <sup>(1)</sup>	\$ 37.7	\$ 19.9	89.4	\$ 93.3	\$ 86.8	7.5
Funds from operations <sup>(1)</sup>	\$ 65.0	\$ 25.2	157.9	\$ 147.8	\$ 100.8	46.6
Capital expenditures <sup>(1)</sup>						
Growth <sup>(2)</sup>	\$ 24.2	\$ 0.9		\$ 26.0	\$ 1.5	
Sustaining <sup>(2)</sup>	4.1	0.4		12.6	6.2	
	\$ 28.3	\$ 1.3		\$ 38.6	\$ 7.7	

(1) Revenue, shrinkage gas, operating expenses, FFO and capital expenditures for the Empress V straddle plant are recorded based on Inter Pipeline's 50% ownership.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section.

Inter Pipeline's NGL processing business extracts NGL from natural gas and oil sands upgrader offgas. The natural gas processing facilities consist of a 100% ownership interest in the Cochrane and Empress II straddle plants and a 50% ownership interest in the Empress V straddle plant. The Empress and Cochrane plants are located on the eastern and western legs, respectively, of the TransCanada Alberta System near export points from Alberta. The offgas processing facilities consist of two offgas plants located near Fort McMurray, Alberta, a fractionator near Redwater, Alberta, and the Boreal pipeline system that connects these facilities.

See the **Description of the Business** section of the **Annual Information Form** for further information about the NGL processing business.

## Volumes

For the three months and year ended December 31, 2016, Inter Pipeline's straddle plants processed natural gas throughput volumes of 3,054 million cubic feet per day (mmcf/d) and 2,920 mmcf/d, an increase of 364 mmcf/d and 243 mmcf/d, respectively, over the same periods in 2015.

At the Cochrane straddle plant average throughput volumes increased 231 mmcf/d in the current quarter and 155 mmcf/d for the full year in 2016, compared to the same periods in 2015. Throughput volumes at the Cochrane straddle plant are largely impacted by, and fluctuate with, demand for Canadian natural gas in the United States (US) west-coast region.

Average throughput volumes at the Empress V straddle plant increased 133 mmcf/d and 88 mmcf/d in the three months and year ended December 31, 2016, respectively, compared to the same periods in 2015. The Empress II straddle plant did not receive throughput volumes in the three months and years ended December 31, 2016 and 2015, which does not impact operating results due to cost-of-service commercial arrangements in place. Natural gas throughput volumes at the Empress straddle plants are dependent on the level of natural gas exported from Alberta's eastern border and are reliant on successfully attracting border gas flows to the straddle plants.

Total NGL production from the straddle plants increased in the fourth quarter from 100,400 b/d in 2015 to 113,700 b/d in 2016 and annually from 101,700 b/d in 2015 to 103,600 b/d in 2016. NGL production from the Cochrane and Empress V straddle plants is driven by changing throughput levels, composition of the natural gas, operating conditions and third party downstream facility constraints which can result in partial reinjection of volumes. Partial reinjection of ethane volumes occurred in 2016 due to third party downstream facility constraints.

Inter Pipeline's offgas plants in the Fort McMurray area processed average throughput volumes of 145 mmcf/d and 40 mmcf/d for the three months and year ended December 31, 2016. Production of ethane-plus volumes from the offgas plants averaged 27,600 b/d in the current quarter, with annualized volumes since Inter Pipeline has owned the assets of 7,700 b/d in 2016. Oil sands upgrader offgas processed in the current quarter was approximately 5.0 times more liquids rich than the natural gas processed at Inter Pipeline's Cochrane straddle plant. Offgas processing throughput volumes to Inter Pipeline's offgas plants can be impacted by the operations associated with connected third party oil sands upgraders in the Fort McMurray area, as well as various downstream issues.

Average NGL sales volumes from the Redwater Olefinic Fractionator was 29,900 b/d in the current quarter, with annualized volumes since Inter Pipeline has owned the assets of 8,100 b/d for the full year in 2016. Sales from the Redwater Olefinic Fractionator can be impacted by the volumes and composition of the ethane-plus production from the offgas plants, cavern storage levels, operational and commercial matters, and various downstream related issues. Production from the offgas plants and sales volumes at the Redwater Olefinic Fractionator can differ due to varying inventory levels associated with the cavern storage facilities at the Redwater Olefinic Fractionator, operational and commercial matters, and other downstream issues.

## Revenue

The NGL processing business earns revenue from the recovery of certain higher value hydrocarbon liquids from export-destined natural gas streams and offgas streams pursuant to a combination of commodity-based, fee-based and cost-of-service contracts. Please refer to the adjusted EBITDA by contract type disclosure in the **NON-GAAP FINANCIAL MEASURES** section for further information.

NGL processing revenue increased \$102.6 million and \$64.3 million for the three months and year ended December 31, 2016, respectively, over the same periods in 2015. Offgas processing contributed revenue of \$75.9 million in the current quarter and \$81.7 million for the year, from the date of acquisition in 2016. Revenue from Inter Pipeline's straddle plants increased \$26.7 million in the fourth quarter of 2016 largely due to higher propane-plus pricing, ethane volumes and propane-plus volumes from the Cochrane straddle plant. Annual revenue from the straddle plants decreased \$17.4 million in 2016 largely due to lower ethane pricing and volumes, offset in part by increased revenue from higher propane-plus pricing and volumes from the Cochrane straddle plant.



## Frac-spread

Three Months Ended December 31						
<i>(dollars)</i>	<b>2016</b>				<b>2015</b>	
	<i>USD/USG<sup>(1)</sup></i>	<i>CAD/USG<sup>(1)</sup></i>	<i>USD/USG<sup>(1)</sup></i>	<i>CAD/USG<sup>(1)</sup></i>		
Cochrane propane-plus market frac-spread	\$ 0.484	\$ 0.645	\$ 0.310	\$ 0.414		
Cochrane propane-plus realized frac-spread	\$ 0.468	\$ 0.624	\$ 0.317	\$ 0.423		
Offgas olefinic market frac-spread	\$ 0.922	\$ 1.228	-	-		
Offgas olefinic realized frac-spread	\$ 0.885	\$ 1.172	-	-		
Offgas paraffinic market frac-spread	\$ 0.221	\$ 0.293	-	-		
Offgas paraffinic realized frac-spread	\$ 0.182	\$ 0.241	-	-		

Years Ended December 31						
<i>(dollars)</i>	<b>2016</b>				<b>2015</b>	
	<i>USD/USG<sup>(1)</sup></i>	<i>CAD/USG<sup>(1)</sup></i>	<i>USD/USG<sup>(1)</sup></i>	<i>CAD/USG<sup>(1)</sup></i>		
Cochrane propane-plus market frac-spread	\$ 0.405	\$ 0.535	\$ 0.327	\$ 0.417		
Cochrane propane-plus realized frac-spread	\$ 0.400	\$ 0.528	\$ 0.329	\$ 0.420		

(1) The differential between USD/USG and CAD/USG frac-spreads is due to fluctuations in exchange rates between US and Canadian dollars. This conversion is calculated based on Bank of Canada exchange rates.

Frac-spread is the difference between the selling prices for certain NGL and the input cost of the natural gas required to produce the respective products, including shrinkage gas.

The market frac-spread for propane-plus from the Cochrane straddle plant is defined as the difference between the weighted average propane-plus price at Mont Belvieu, Texas and the monthly index price of AECO natural gas purchased for shrinkage calculated in US dollars per US gallon (USD/USG). Cochrane propane-plus realized frac-spread is defined in a similar manner and is calculated on a weighted average basis using market frac-spread for unhedged production and fixed-price frac-spread prices for any hedged production. Natural gas purchased for shrinkage is based on the actual combination of the monthly index and daily price of AECO paid. The Cochrane propane-plus realized frac-spread does not include market price differentials or extraction premiums.

In the fourth quarter, the Cochrane propane-plus realized frac-spread increased from \$0.32 USD/USG in 2015 to \$0.47 USD/USG in 2016 and annually from \$0.33 USD/USG in 2015 to \$0.40 USD/USG in 2016. The 5-year and 15-year simple average Cochrane propane-plus market frac-spread at December 31, 2016 were \$0.68 USD/USG and \$0.61 USD/USG, respectively.

Offgas processing produces both olefinic and paraffinic NGL which are sold under multiple shorter term, individually negotiated contracts with unique pricing benchmarks. As a result, market and realized olefinic and paraffinic frac-spreads may change period over period.

Olefins are typically higher value petrochemicals that do not naturally exist and consist of polymer grade propylene, alky feed and olefinic condensate. Paraffins are generally lower value NGL consisting of propane and normal butane. The olefinic market frac-spread for offgas processing is defined as the difference between the weighted average prices of propylene, alky feed and olefinic condensate products sold less applicable differentials and the daily index price of AECO natural gas purchased for shrinkage calculated in USD/USG. Propylene pricing is based on a North American Gulf Coast benchmark price, while alky feed and olefinic condensate are currently priced on a differential to West Texas Intermediate light sweet crude. The olefinic realized frac-spread for offgas processing is defined as the difference between the realized price of the propylene, alky feed and olefinic condensate products sold for unhedged production and fixed price frac-

spread prices for any hedged production, and the realized cost of shrinkage gas purchased, including natural gas transportation, extraction premiums and associated costs, calculated in USD/USG. Natural gas purchased for shrinkage is based on a combination of AECO daily index and monthly index natural gas prices. The offgas olefinic realized frac-spread does not include product transportation or marketing fees.

The paraffinic market frac-spread for offgas processing is defined as the difference between the weighted average prices of the propane and butane products less applicable differentials and the daily index price of AECO natural gas purchased for shrinkage calculated in USD/USG. Propane is currently based on a Conway monthly posting less a weighted average differential. Butane is currently priced based on a differential to West Texas Intermediate light sweet crude. The paraffinic realized frac-spread for offgas processing is defined as the difference between the realized price of the propane and butane products sold for unhedged production and fixed price frac-spread prices for any hedged production and the realized cost of shrinkage gas purchased, including natural gas transportation, extraction premiums and associated costs, calculated in USD/USG. Natural gas purchased for shrinkage is based on a combination of AECO daily index and monthly index natural gas prices. The offgas paraffinic realized frac-spread does not include product transportation or marketing fees.

In the current quarter, the offgas olefinic realized frac-spread was \$0.89 USD/USG and the offgas paraffinic realized frac-spread was \$0.18 USD/USG. The offgas olefinic market frac-spread was \$0.92 USD/USG and the offgas paraffinic market frac-spread was \$0.22 USD/USG for the current quarter.

See the **RISK MANAGEMENT AND FINANCIAL INSTRUMENTS** section for further discussion of frac-spread hedges.

## Shrinkage Gas

Shrinkage gas represents natural gas bought by Inter Pipeline to replace the heat content of liquids extracted from natural gas processed at the straddle plants and offgas processed at the offgas plants. The price for shrinkage gas is based on a combination of AECO daily spot prices and monthly index natural gas prices. In the three months and year ended December 31, 2016, shrinkage gas expense increased \$45.1 million and \$11.0 million, respectively, compared to the same periods in 2015. Shrinkage gas expense from offgas processing was \$33.7 million and \$36.1 million in the fourth quarter and year ended December 31, 2016, respectively, from the date of acquisition. Shrinkage gas expense from Inter Pipeline's straddle plants increased \$11.4 million in the current quarter due to higher propane-plus volumes at the Cochrane straddle plant, higher ethane volumes at the Empress V straddle plant and an increase in AECO natural gas prices, from the same period in 2015. Annual shrinkage gas expense from the straddle plants decreased \$25.1 million for the full year in 2016 largely due to a decline in AECO natural gas prices, offset in part by higher propane-plus volumes from the Cochrane straddle plant. The weighted average monthly AECO prices\* increased in the fourth quarter from \$2.51 per gigajoule (GJ) in 2015 to \$2.67/GJ in 2016 and decreased year to date from \$2.62/GJ in 2015 to \$1.98/GJ in 2016.

## Operating Expenses

In the three months and year ended December 31, 2016, operating expenses in the NGL processing business increased \$17.8 million and \$6.5 million, respectively, compared to the same periods in 2015. The increase largely results from the inclusion of operating expenses from offgas processing from the date of acquisition in 2016 of \$16.2 million in the fourth quarter and \$18.2 million for the year. Operating expenses from Inter Pipeline's straddle plants increased \$1.6 million in

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\* Weighted average price calculated from one-month spot prices at AECO as reported in the *Canadian Gas Price Reporter*.

the current quarter due to higher employee, general operating and maintenance costs, as well as increased fuel and power costs. Annual operating expenses from the straddle plants decreased \$11.7 million in 2016 largely due to lower fuel and power costs arising from lower pricing, as well as a reduction in general operating and maintenance costs. Average Alberta power pool prices increased in the fourth quarter from \$21.19/MWh in 2015 to \$22.03/MWh in 2016 and decreased year to date from \$33.34/MWh in 2015 to \$18.28/MWh in 2016.

### **Capital Expenditures**

The NGL processing business incurred growth capital expenditures\* of \$26.0 million in 2016, of which \$23.6 million relates primarily to front-end engineering and design costs on the proposed \$1.85 billion PDH facility and the proposed \$1.3 billion PP facility. The remaining growth capital expenditures\* largely relate to equipment upgrades at the Cochrane straddle plant. Sustaining capital expenditures\* of \$12.6 million incurred in 2016 largely relate to various processing system upgrades at the Cochrane straddle plant.

### **Acquisition of Williams Canada**

On September 23, 2016, Inter Pipeline acquired the outstanding shares of Williams Energy Canada Development ULC, Williams Horizon Offgas ULC, Williams Canada Employee Services Inc., Williams Canada Propylene ULC and Williams Energy Canada ULC, from The Williams Companies International Holdings B.V. and Williams Energy Canada LP (together, the Sellers) pursuant to two share purchase agreements (together, the Acquisition Agreement) dated August 8, 2016. The Williams Canada acquisition was valued at \$1.35 billion, plus closing adjustments for working capital, for total cash consideration of \$1.38 billion and was funded by the net proceeds of a \$600 million subscription receipt equity issuance, \$350 million of senior unsecured medium-term notes, and the remaining balance drawn under Inter Pipeline's increased syndicated credit facility.

The offgas plants process offgas from oil sands production into an ethane-plus mix that is transported through the Boreal pipeline system to the Redwater Olefinic Fractionator where it is further separated into marketable NGL products and sold across North America.

Operating results from offgas processing have been included in the consolidated financial statements since September 23, 2016, contributing \$81.7 million to revenue and \$13.1 million to net income to December 31, 2016. If the Williams Canada acquisition had taken place on January 1, 2016, for the year ended December 31, 2016, management estimates that offgas processing would have contributed an incremental \$204.6 million to pro forma revenue and a \$20.3 million loss to pro forma net income. The pro forma information is not necessarily indicative of the results of operations that would have resulted had the Williams Canada acquisition been effective on the date indicated, or of future results.

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

The Williams Canada acquisition was accounted for by the acquisition method as at the closing date of September 23, 2016. Determinations of fair value often require management to make assumptions and estimates about future events. Changes in any of the assumptions or estimates used in determining the fair values of the acquired assets and liabilities could impact the carrying amounts assigned. Inter Pipeline has provisionally allocated the consideration paid, subject to changes in estimates, as follows:

Cash	\$ 46.9
Property, plant and equipment	1,084.2
Intangible asset <sup>(1)</sup>	139.0
Deferred tax asset	173.1
Non-cash working capital	(12.8)
Decommissioning obligation	(47.4)
	<b>\$ 1,383.0</b>

(1) A customer contract intangible asset has been recorded due to the off-market nature of the economic terms of an agreement for a sustained period of time. The intangible asset will be amortized over the life of the contract.

On December 5, 2016, Inter Pipeline was approved to receive up to \$200 million in royalty credits from the Government of Alberta's Petrochemical Diversification Program. The royalty credits were awarded in support of Inter Pipeline's proposed PDH facility, and the credits will be available once the PDH facility is in operation. The royalty credits can then be sold to oil or natural gas producers which use the credits to reduce their royalty payments. Inter Pipeline anticipates making a final investment decision on the PDH facility by mid-2017 and the facility is expected to be operational by mid-2021. The royalty credits will not be recognized on Inter Pipeline's consolidated balance sheet until the final investment decision is made and Inter Pipeline has reasonable assurance that the conditions attached to the grant will be fulfilled.

## Bulk Liquid Storage Business Segment

	Three Months Ended December 31			Years Ended December 31		
	2016	2015	% change	2016	2015	% change
Utilization	<b>99%</b>	97%	2.1	<b>98%</b>	94%	4.3
<i>(millions)</i>						
Revenue	<b>\$ 57.8</b>	\$ 64.8	<i>(10.8)</i>	<b>\$ 245.9</b>	\$ 214.4	14.7
Operating expenses	<b>\$ 20.2</b>	\$ 26.4	<i>(23.5)</i>	<b>\$ 93.4</b>	\$ 84.0	11.2
Funds from operations	<b>\$ 28.9</b>	\$ 28.2	2.5	<b>\$ 120.0</b>	\$ 98.3	22.1
Capital expenditures						
Growth <sup>(1)</sup>	<b>\$ 16.0</b>	\$ 10.0		<b>\$ 55.8</b>	\$ 25.0	
Sustaining <sup>(1)</sup>	<b>6.1</b>	5.4		<b>12.2</b>	15.3	
	<b>\$ 22.1</b>	\$ 15.4		<b>\$ 68.0</b>	\$ 40.3	

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section.

Inter Pipeline operates a bulk liquid storage business branded as Inter Terminals with operations in the UK, Germany, Ireland, Denmark and Sweden. Inter Terminals is one of the largest independent bulk liquid storage businesses in Europe, with a combined storage capacity of approximately 27 million barrels across 16 terminals. These terminals are strategically located with five terminals at the ports of Immingham, Teesside and Tyneside in the UK, one terminal on the Shannon estuary in Ireland, two terminals on the River Rhine at Mannheim, Germany, four terminals in Denmark located on the Danish Straits and four terminals in Sweden located along the Baltic Sea and Danish Straits.

See the **Description of the Business** section of the **Annual Information Form** for further information about the bulk liquid storage business.

## Utilization

Average utilization rates in the bulk liquid storage business increased in the fourth quarter from 97% in 2015 to 99% in 2016 and for the full year from 94% in 2015 to 98% in 2016, reflecting higher demand across Inter Terminals' business.

## Revenue

The bulk liquid storage business earns revenue for bulk liquid storage and handling services that are underpinned by a range of long-term and short-term fee-based contracts. Please refer to the adjusted EBITDA by contract type disclosure in the **NON-GAAP FINANCIAL MEASURES** section for further information.

Revenue from the bulk liquid storage business decreased \$7.0 million in the fourth quarter primarily due to unfavourable foreign exchange translation adjustments of \$6.0 million, compared to the same period in 2015. For the full year in 2016, revenue increased \$31.5 million over 2015, largely due to inclusion of revenue from Inter Terminals Sweden for the entire year in 2016, as opposed to from the acquisition date of June 10, 2015, as well as incremental revenue from the Denmark terminals as a result of higher utilization, storage rates and activity levels. Partially offsetting these annual revenue increases was unfavourable foreign currency translation adjustments of \$4.2 million in 2016.

See the **Foreign Exchange Rates** section below for further information on changes in rates.

## Foreign Exchange Rates

<i>(dollars)</i>	Three Months Ended December 31			Years Ended December 31		
	2016	2015	% change	2016	2015	% change
Euro/CAD	\$ 1.4380	\$ 1.4609	(1.6)	\$ 1.4663	\$ 1.4185	3.4
Pound Sterling/CAD	\$ 1.6564	\$ 2.0253	(18.2)	\$ 1.7963	\$ 1.9542	(8.1)

## Operating Expenses

Operating expenses in the bulk liquid storage business decreased \$6.2 million in the current quarter compared to the same period in 2015, largely due to favourable foreign currency translation adjustments of \$2.2 million, and a \$2.0 million partial reimbursement of a customs duty claim in Sweden, which was previously recognized as an expense in third quarter of 2016. Annual operating expenses in 2016 increased \$9.4 million over 2015, primarily due to the inclusion of operating expenses from Inter Terminals Sweden for the full year, compared to a partial year in 2015, offset in part by favourable foreign currency translation adjustments of \$1.7 million in 2016.

## Capital Expenditures

In 2016, the bulk liquid storage business incurred total growth capital expenditures\* of \$55.8 million, which largely relate to a number of tank life extensions and tank modification projects. Approximately \$9.3 million of the growth capital expenditures\* in 2016 related to the initial spend to date on a project to build five new tanks with aggregate capacity of 175,000 barrels at Seal Sands terminal in the UK, for a total estimated project cost of \$25 million. In addition, approximately \$2.0 million of the 2016 growth capital expenditures\* relate to the construction of six new tanks at a German terminal which was completed earlier in the year.

\* Please refer to the NON-GAAP FINANCIAL MEASURES section

The bulk liquid storage business incurred total sustaining capital expenditures\* of \$12.2 million in 2016. These expenditures primarily relate to terminal infrastructure, safety improvement projects and environmental performance enhancement initiatives.

## Other Expenses

<i>(millions)</i>	Three Months Ended December 31		Years Ended December 31	
	2016	2015	2016	2015
Income tax expense	\$ 47.4	\$ 43.0	\$ 151.4	\$ 187.4
Depreciation and amortization	64.8	52.6	229.7	188.4
Financing charges	40.8	38.5	147.0	142.1
General and administrative	35.8	20.5	133.9	76.2
Loss on disposal of assets	4.3	0.6	6.5	5.6
Unrealized change in fair value of derivative financial instruments	-	(0.1)	-	(0.2)

## Income Tax Expense

Consolidated income tax expense increased \$4.4 million and decreased \$36.0 million in the three months and year ended December 31, 2016, respectively, compared to the same periods in 2015. Consolidated income tax expense is the sum of current income tax expense and deferred income tax expense.

Current income tax expense decreased \$31.0 million and \$19.0 million in the three months and year ended December 31, 2016, respectively, compared to the same periods in 2015. The decrease for the three months ended December 31, 2016 is due to a \$31.0 million current tax recovery which was a result of the utilization of tax assets acquired from Williams Canada. The decrease for the year ended December 31, 2016 is due to the same reason above offset by increased current tax expense of \$12.0 which was a result of higher taxable income recognized in 2016 compared to 2015.

Deferred income tax expense increased \$35.4 million and decreased \$17.0 million in the three months and year ended December 31, 2016, respectively, compared to the same periods in 2015. The increase for the three months ended December 31, 2016 is primarily due to the utilization of tax assets to lower current income tax expense in the quarter. The decrease for the year ended December 31, 2016 is primarily due to a one-time deferred income tax expense of \$35.9 million recognized in the second quarter of 2015 for the Alberta provincial corporate tax rate increase from 10% to 12%. This is partially offset by increased deferred tax expense of approximately \$18.9 million which was a result of the utilization of tax assets to lower current income tax expense in 2016.

## Depreciation and Amortization

Depreciation and amortization of tangible and intangible assets increased \$12.2 million and \$41.3 million in the three months and year ended December 31, 2016, respectively, over the same periods in 2015. This increase is primarily due to depreciation of new assets now in service, assets acquired with Williams Canada and accelerated amortization of certain intangible assets in the NGL processing business. The annual increase is also due to depreciation of assets acquired with Inter Terminals Sweden for the entire year in 2016, as opposed to a partial year in 2015.

\* Please refer to the NON-GAAP FINANCIAL MEASURES section

## Financing Charges

<i>(millions)</i>	Three Months Ended		Years Ended	
	December 31		December 31	
	2016	2015	2016	2015
Interest on credit facilities	\$ 11.8	\$ 8.4	\$ 37.1	\$ 35.0
Interest on Corridor Debentures	1.9	1.9	7.4	7.6
Interest on Medium-Term Notes Series 1 to 9	26.6	23.5	97.8	92.3
Total interest	40.3	33.8	142.3	134.9
Capitalized interest	(2.0)	2.6	(2.4)	0.7
Amortization of transaction costs on financial debt	0.9	0.9	3.4	3.3
Accretion of provisions and pension plan funding charges	1.6	1.2	3.7	3.2
Total financing charges	\$ 40.8	\$ 38.5	\$ 147.0	\$ 142.1

Total financing charges in the three months and year ended December 31, 2016, increased \$2.3 million and \$4.9 million, respectively, over the same periods in 2015.

In the current quarter, interest on credit facilities increased \$3.4 million due to higher weighted average credit facility debt outstanding and short-term interest rates, as well as interest costs related to the acquisition of the remaining 15% ownership interest in the Cold Lake pipeline system. This was also the primary driver for the annual increase of \$2.1 million, over the same periods in 2015.

Interest on medium-term notes increased \$3.1 million and \$5.5 million in the three months and year ended December 31, 2016, compared to the same periods in 2015, due to the timing of issuance of Series 7 on March 23, 2015, Series 8 on September 13, 2016 and Series 9 on December 16, 2016.

Capitalized interest increased \$4.6 million in the current quarter and \$3.1 million for the full year of 2016, over the comparable periods in 2015. Capitalized interest in 2016 largely relates to the proposed \$1.85 billion PDH facility.

In the three months and year ended December 31, 2015, accretion of provisions and pension plan funding charges increased \$0.4 million and \$0.5 million, respectively, over the same periods in 2014, as a result of changes in discount rates for environmental provisions.

See the **LIQUIDITY AND CAPITAL RESOURCES** section for further information about Inter Pipeline's debt facilities.

## General and Administrative

<i>(millions)</i>	Three Months Ended		Years Ended	
	December 31		December 31	
	2016	2015	2016	2015
Canada	\$ 27.7	\$ 12.8	\$ 103.6	\$ 52.4
Europe	8.1	7.7	30.3	23.8
	\$ 35.8	\$ 20.5	\$ 133.9	\$ 76.2

Canadian general and administrative expenses increased \$14.9 million and \$51.2 million in the three months and year ended December 31, 2016, respectively, over the same periods in 2015. The increase is largely due to higher employee costs, rent expense and external services costs relating to Williams Canada transition and integration. Employee costs rose largely due to an increase in long-term incentive plan expense due to a greater increase in Inter Pipeline's share price during the fourth quarter and year in 2016, over the same periods in 2015, in addition to the increased number of

employees from the acquisition of Williams Canada. Rent expense increased as Inter Pipeline's head office was relocated to new premises in the first quarter of 2016, as well as the inclusion of Williams Canada's leased premises. Rent expense was also impacted on a year to date basis by a one-time adjustment in rent expense of \$14.9 million in the first quarter of 2016, for the difference between future lease obligations and the estimated sublease recoveries as the previous non-cancellable office leases were deemed to be onerous contracts.

In the three months and year ended December 31, 2016, European general and administrative costs increased \$0.4 million and \$6.5 million, respectively, over the same periods in 2015. The increase is largely due to higher employee costs and professional fees. The annual increase is also attributable to the inclusion of general and administrative costs from Inter Terminals Sweden for the full year, as opposed to a partial year in 2015. Foreign currency translation adjustments resulted in lower general and administrative costs of \$1.4 million in the fourth quarter and \$1.5 million for the full year in 2016.

### **Loss on Disposal of Assets**

In the three months and year ended December 31, 2016, Inter Pipeline incurred a loss on disposal of assets of \$4.3 million and \$6.5 million, respectively, largely due to the disposal and de-recognition of certain assets in the bulk liquid storage business, as well as a turbine exchange in the NGL processing business in the second quarter of 2016.



## SUMMARY OF QUARTERLY RESULTS

(millions, except volume, per share and % amounts)	2015				2016			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
<b>Pipeline volumes (000s b/d)<sup>(1)</sup></b>								
Oil sands transportation	1,097.7	853.9	1,119.9	1,111.8	1,104.2	1,012.6	1,093.3	1,172.5
Conventional oil pipelines	214.2	208.5	209.4	214.8	208.5	201.3	192.8	200.3
<b>Total pipeline volumes</b>	<b>1,311.9</b>	<b>1,062.4</b>	<b>1,329.3</b>	<b>1,326.6</b>	<b>1,312.7</b>	<b>1,213.9</b>	<b>1,286.1</b>	<b>1,372.8</b>
<b>NGL processing volumes (000s b/d)<sup>(1)(2)</sup></b>								
Natural gas processing - Ethane	71.0	56.3	62.0	59.1	60.9	51.9	58.0	69.9
Natural gas processing - Propane-plus	42.0	34.1	40.8	41.3	44.9	42.2	42.5	43.8
Redwater Olefinic Fractionator sales volume <sup>(2)</sup>	-	-	-	-	-	-	-	29.9
<b>Total NGL processing volumes</b>	<b>113.0</b>	<b>90.4</b>	<b>102.8</b>	<b>100.4</b>	<b>105.8</b>	<b>94.1</b>	<b>100.5</b>	<b>143.6</b>
<b>Utilization</b>								
Bulk liquid storage	90%	93%	93%	97%	98%	97%	98%	99%
<b>Revenue</b>								
Oil sands transportation	\$ 177.4	\$ 182.7	\$ 195.2	\$ 213.4	\$ 191.6	\$ 193.3	\$ 192.9	\$ 200.8
Conventional oil pipelines	77.8	74.7	80.9	89.0	81.5	85.6	86.9	111.0
NGL processing	102.5	88.8	91.0	88.5	77.5	72.8	93.7	191.1
Bulk liquid storage	48.1	44.4	57.1	64.8	65.8	61.3	61.0	57.8
	\$ 405.8	\$ 390.6	\$ 424.2	\$ 455.7	\$ 416.4	\$ 413.0	\$ 434.5	\$ 560.7
<b>Funds from operations</b>								
Oil sands transportation	\$ 130.2	\$ 135.0	\$ 146.1	\$ 157.8	\$ 139.4	\$ 141.4	\$ 142.3	\$ 158.5
Conventional oil pipelines	46.8	46.5	49.8	51.5	50.0	47.1	49.1	52.4
NGL processing	28.7	23.3	23.6	25.2	23.6	30.5	28.7	65.0
Bulk liquid storage	20.5	20.6	29.0	28.2	31.3	29.6	30.2	28.9
Corporate costs	(49.7)	(44.4)	(43.3)	(51.3)	(58.3)	(51.9)	(38.9)	(50.1)
	\$ 176.5	\$ 181.0	\$ 205.2	\$ 211.4	\$ 186.0	\$ 196.7	\$ 211.4	\$ 254.7
<b>Per share<sup>(3)</sup></b>	\$ 0.53	\$ 0.54	\$ 0.61	\$ 0.63	\$ 0.55	\$ 0.58	\$ 0.62	\$ 0.71
Net income	\$ 122.8	\$ 73.8	\$ 128.4	\$ 138.0	\$ 104.6	\$ 122.9	\$ 121.3	\$ 128.8
Net income attributable to shareholders	\$ 113.7	\$ 65.3	\$ 118.7	\$ 129.7	\$ 95.8	\$ 114.4	\$ 113.7	\$ 125.8
Per share – basic and diluted	\$ 0.34	\$ 0.19	\$ 0.35	\$ 0.39	\$ 0.28	\$ 0.34	\$ 0.34	\$ 0.35
Dividends to shareholders <sup>(4)</sup>	\$ 121.8	\$ 123.1	\$ 123.5	\$ 128.7	\$ 131.3	\$ 131.4	\$ 131.4	\$ 145.1
Per share <sup>(4)</sup>	\$ 0.3675	\$ 0.3675	\$ 0.3675	\$ 0.3825	\$ 0.3900	\$ 0.3900	\$ 0.3900	\$ 0.4000
Shares outstanding (basic)								
Weighted average	331.5	334.8	335.8	336.3	336.6	336.8	338.7	361.2
End of period	334.2	335.3	336.2	336.4	336.7	336.9	359.5	367.9
Capital expenditures <sup>(5)</sup>								
Growth <sup>(3)</sup>	\$ 132.5	\$ 67.8	\$ 43.4	\$ 52.6	\$ 32.2	\$ 27.7	\$ 40.8	\$ 49.9
Sustaining <sup>(3)</sup>	9.5	10.0	12.3	27.8	18.0	10.0	8.1	22.3
	\$ 142.0	\$ 77.8	\$ 55.7	\$ 80.4	\$ 50.2	\$ 37.7	\$ 48.9	\$ 72.2
Payout ratio <sup>(3)</sup>	73.3%	71.9%	63.6%	63.8%	74.6%	70.3%	64.8%	57.8%
Total assets	\$ 8,733.8	\$ 8,955.5	\$ 9,010.4	\$ 9,029.4	\$ 8,921.9	\$ 8,869.7	\$ 10,141.0	\$ 10,151.6
Total debt <sup>(6)</sup>	\$ 4,680.7	\$ 4,865.1	\$ 4,876.2	\$ 4,851.7	\$ 4,850.2	\$ 4,832.7	\$ 5,596.6	\$ 5,828.6
Total shareholders' equity	\$ 2,737.6	\$ 2,732.2	\$ 2,805.4	\$ 2,821.1	\$ 2,752.9	\$ 2,692.8	\$ 3,269.9	\$ 3,187.9
Enterprise value <sup>(3)</sup>	\$ 15,590.4	\$ 14,487.4	\$ 13,153.2	\$ 12,323.7	\$ 13,857.0	\$ 14,064.4	\$ 15,555.0	\$ 16,732.5
Consolidated Net Debt to Total Capitalization <sup>(3)</sup>	51.4%	52.8%	52.7%	52.8%	53.8%	54.2%	54.5%	57.2%

(1) Cold Lake volumes and Empress V NGL production reported on a 100% basis. Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

(2) Average quarterly throughput volumes from the recently acquired Williams Canada offgas processing have not been included for the third quarter of 2016 in the table above as only eight days of operations from the closing date of the acquisition are included in Inter Pipeline's September 30, 2016 results and therefore would not contain any meaningful information.

(3) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(4) Dividends to shareholders are calculated based on the number of common shares outstanding at each record date.

(5) Amounts reported on a 100% basis that includes non-controlling interest. Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

(6) Total debt includes long-term debt, short-term debt and commercial paper before discounts and debt transaction costs.

## LIQUIDITY AND CAPITAL RESOURCES

Inter Pipeline's capital management objectives are aligned with its commercial growth strategies and long-term outlook for the business. The primary objectives are to maintain:

- (i) stable dividends to shareholders over economic and industry cycles;
- (ii) a flexible capital structure which optimizes the cost of capital within an acceptable level of risk; and
- (iii) an investment grade credit rating.

Inter Pipeline's capital under management includes financial debt and shareholders' equity. Management may make adjustments to the capital structure for changes in economic conditions or the risk characteristics of the underlying assets. To maintain or modify the capital structure, Inter Pipeline may adjust the level of cash dividends paid to shareholders, issue new common or preferred shares, issue new debt, renegotiate existing debt terms or repay existing debt.

Inter Pipeline maintains flexibility in its capital structure to fund growth capital<sup>\*</sup> and acquisitions through market and industry cycles. Funding requirements are projected to ensure appropriate sources of financing are available to meet future financial obligations and capital expenditure programs. Inter Pipeline generally relies on committed credit facilities and FFO in excess of dividends to fund capital requirements. At December 31, 2016, Inter Pipeline had access to committed credit facilities totaling \$3.05 billion, of which \$796.4 million remained unutilized, and demand facilities totaling \$98.1 million of which \$95.3 million remained unutilized. Certain facilities are available to specific subsidiaries of Inter Pipeline.

Inter Pipeline may also issue equity capital to ensure its balance sheet remains well prepared for expected growth. During the three months and year ended December 31, 2016, approximately \$52.5 million and \$68.8 million, respectively, of equity was issued through the dividend reinvestment plan. Effective with the October dividend announced on October 5, 2016, Inter Pipeline re-instated the premium component of its Premium Dividend<sup>TM</sup> and Dividend Reinvestment Plan.

On August 17, 2016, Inter Pipeline completed an offering of 22.4 million subscription receipts at a price of \$26.75 per subscription receipt for total gross proceeds of \$600 million. Each subscription receipt entitled the holder to receive one common share of Inter Pipeline upon closing of the Williams Canada acquisition. Subscription Receipt holders received dividend equivalent payments per subscription receipt equal to dividends declared on each common share. On September 23, 2016 the subscription receipts were exchanged for common shares of Inter Pipeline in accordance with the terms of the subscription receipt agreement and were delisted from the Toronto Stock Exchange. Net proceeds from the equity offering were used to partially fund the Williams Canada acquisition.

On August 30, 2016 Inter Pipeline increased its syndicated credit facility by \$250 million, from \$1.25 billion to \$1.5 billion. Inter Pipeline amended its \$1.5 billion syndicated credit facility on December 5, 2016, extending the term for one year with

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

<sup>TM</sup> denotes trademark of Canaccord Genuity Corp.

a revised maturity date of December 3, 2021. On December 14, 2016, Corridor extended the maturity date of its \$1.55 billion syndicated credit facility by one year to December 14, 2020.

On September 13, 2016, Inter Pipeline issued \$350 million of senior unsecured medium-term notes Series 8 due September 13, 2023, in the Canadian public debt market. The medium-term notes Series 8 bear interest at a fixed rate of 2.608% per annum, payable semi-annually. Net proceeds from the offering were used to partially fund the Williams Canada acquisition.

On December 16, 2016, Inter Pipeline issued \$450 million of senior unsecured medium-term notes Series 9 due December 16, 2026, in the Canadian public debt market. The medium-term notes Series 9 bear interest at a fixed rate of 3.484% per annum, payable semi-annually. Net proceeds from the offering were used to partially fund the acquisition of Canadian Natural's 15% interest in the Cold Lake pipeline system and to repay existing bank indebtedness.

Inter Pipeline has a current short form base shelf prospectus with Canadian regulatory authorities that was filed in December 2015. Under provisions detailed in the short form base shelf prospectus, Inter Pipeline may offer and issue, from time to time: (i) common shares; (ii) preferred shares; (iii) debt securities; and (iv) subscription receipts (collectively, the "Securities") of up to \$3.0 billion aggregate of Securities during the 25 month period that the short form base shelf prospectus is valid. Securities may be offered separately or together, in amounts, at prices and on terms to be determined based on market conditions at the time of sale and set forth in one or more prospectus supplements. As a result of the subscription receipt offering in August 2016 and the medium-term note offerings in September and December 2016, the amount of Securities that can be issued under the shelf prospectus and related prospectus supplements has been reduced to \$1.6 billion.

Inter Pipeline may utilize derivative financial instruments to minimize exposure to fluctuating commodity prices, foreign exchange and interest rates. Inter Pipeline's market risk management policy defines and specifies the controls and responsibilities to manage market exposure to changing commodity prices (crude oil, natural gas, NGL and power) and changes within financial markets relating to interest rates and foreign exchange exposure. Further details of the risk management program are discussed in the **RISK MANAGEMENT AND FINANCIAL INSTRUMENTS** section.

## Credit Facilities and Debt Outstanding

<i>(millions)</i>			December 31	
	Recourse	Non-recourse	2016	2015
<b>Credit facilities available</b>				
Corridor syndicated credit facility	\$ -	\$ 1,550.0	\$ 1,550.0	\$ 1,550.0
Inter Pipeline syndicated credit facility <sup>(1)</sup>	1,500.0	-	1,500.0	1,250.0
	1,500.0	1,550.0	3,050.0	2,800.0
Demand facilities <sup>(2)</sup>	73.1	25.0	98.1	105.8
	\$ 1,573.1	\$ 1,575.0	\$ 3,148.1	\$ 2,905.8
<b>Total debt outstanding</b>				
Inter Pipeline Ltd.				
Inter Pipeline syndicated credit facility			\$ 913.0	\$ 664.0
Medium-Term Notes Series 1 to 9 <sup>(4)</sup>			3,425.0	2,625.0
Inter Terminals demand facility <sup>(1)</sup>			-	26.5
Inter Pipeline (Corridor) Inc.				
Corridor syndicated credit facility			1,340.6	1,386.2
Corridor Debentures			150.0	150.0
<b>Total debt outstanding<sup>(3)(5)</sup></b>			<b>\$ 5,828.6</b>	<b>\$ 4,851.7</b>

(1) On August 30, 2016 Inter Pipeline increased the size of its syndicated credit facility from \$1.25 billion to \$1.5 billion.

(2) Demand facilities consist of: Inter Pipeline's \$40 million demand facility; Corridor's \$25 million demand facility; and Inter Terminals Limited and Inter Terminals EOT ApS Pound Sterling 20 million demand facility which was converted at a Pound Sterling/CAD rate of 1.6564 at December 31, 2016.

(3) At December 31, 2016, outstanding Inter Pipeline letters of credit of approximately \$2.8 million were not included in total debt outstanding.

(4) Inter Pipeline issued \$350 million of medium-term notes Series 8 on September 13, 2016 and issued \$450 million of medium-term notes Series 9 on December 16, 2016.

(5) Financial debt reported in the December 31, 2016 consolidated financial statements of \$5,806.3 million, includes long-term debt, short-term debt and commercial paper outstanding of 5,828.6 million less discounts and debt transaction costs of \$22.3 million.

Inter Pipeline's debt outstanding at December 31, 2016, matures at various dates up to May 2044 as follows:

<i>(millions)</i>	Amount	Rate	Maturity date
<b>Inter Pipeline Ltd.</b>			
Inter Pipeline syndicated credit facility	\$ 913.0	Variable	December 3, 2021
Medium-Term Notes			
Series 1	325.0	4.967%	February 2, 2021
Series 2	200.0	3.839%	July 30, 2018
Series 3	400.0	3.776%	May 30, 2022
Series 4	500.0	3.448%	July 20, 2020
Series 5	500.0	4.637%	May 30, 2044
Series 6	400.0	CDOR plus 49 bps	May 30, 2017
Series 7	300.0	3.173%	March 24, 2025
Series 8	350.0	2.608%	September 13, 2023
Series 9	450.0	3.484%	December 16, 2026
<b>Inter Pipeline (Corridor) Inc.</b>			
Corridor syndicated credit facility	1,340.6	Variable	December 14, 2020
Corridor Debentures	150.0	4.897%	February 3, 2020

## Financial Covenants

Inter Pipeline was in compliance with all covenants under its credit facilities and medium-term notes as at December 31, 2016.

The following table provides a listing of the key financial covenants as at December 31, 2016:

	Maximum Ratio	December 31 2016
<b>Inter Pipeline Ltd.</b>		
Inter Pipeline syndicated credit facility		
Consolidated Net Debt to Total Capitalization <sup>(1)(2)(3)(4)</sup>	65%	57.2%
Medium-Term Notes Series 1 to 9		
Funded Debt to Total Capitalization <sup>(2)(5)(6)</sup>	70%	55.1%
<b>Inter Pipeline (Corridor) Inc.</b>		
Corridor syndicated credit facility		
Corridor Debentures		
Rate Base Debt to Rate Base <sup>(7)(8)</sup>	75%	73.5%

- (1) "Consolidated Net Debt" includes the aggregate amount of all debt of the borrower and its restricted subsidiaries, but excludes debt of any unrestricted subsidiary which is not guaranteed by the borrower or any restricted subsidiary, subordinated debt, non-recourse debt and debt attributable to any non-controlling interest, less cash and cash equivalents owned by the borrower and its restricted subsidiaries, but excluding any such cash or cash equivalents owned by an unrestricted subsidiary or attributable to any non-controlling interest, provided that the use or application of such cash and cash equivalents is not encumbered or restricted by contract or regulatory requirements.
- (2) Inter Pipeline (Corridor) Inc. is not considered a restricted subsidiary under Inter Pipeline's syndicated credit facility or medium-term note indenture and, as a result, its debt and assets are excluded from all financial covenant calculations under those agreements.
- (3) "Total Capitalization" for Inter Pipeline's syndicated credit facility covenant is the sum of debt, but excluding non-recourse debt, debt attributable to unrestricted subsidiaries or any non-controlling interest, plus convertible debentures, plus consolidated shareholders' equity of the borrower, but excluding any shareholders' equity from or attributable to non-recourse assets, unrestricted subsidiaries or any non-controlling interest, plus a \$243.8 million adjustment related to Canadian SIFT legislation.
- (4) Please refer to the NON-GAAP FINANCIAL MEASURES section.
- (5) "Funded Debt" includes long-term debt of the issuer and its restricted subsidiaries, but excluding non-recourse debt, subordinated debt and any obligations of the issuer to a restricted subsidiary or of a restricted subsidiary to the issuer or another restricted subsidiary.
- (6) "Total Capitalization" for Inter Pipeline's medium-term notes covenant is the sum of Funded Debt plus subordinated debt, plus consolidated equity, plus the amount of any minority interests in restricted subsidiaries, plus a \$243.8 million adjustment related to Canadian SIFT legislation.
- (7) "Rate Base Debt" includes all Corridor debt excluding debt incurred in connection with financing additions to the rate base prior to the time those additions form part of the rate base, debt incurred to fund recoverable expenditures under the Corridor Firm Service Agreement (FSA) and subordinated debt.
- (8) "Rate Base" includes the invested capital to bring the asset to service pursuant to the Corridor FSA.

The Corridor pipeline system is operated under the Corridor FSA, which is a long-term cost-of-service contract that provides for the recovery of debt financing costs, substantially all operating costs, rate base depreciation and taxes, in addition to providing a return on equity. As a result, Corridor's FFO is not impacted by throughput volumes or commodity price fluctuations. Inter Pipeline actively manages Corridor's debt level to ensure the actual rate base debt to rate base ratio is very close to the benchmark criteria (i.e. not more than 75%) to optimize its defined capital structure.

At December 31, 2016, approximately \$2,653.6 million or 45.5% of Inter Pipeline's total debt outstanding was exposed to variable interest rates. Of this amount \$1,340.6 million or 50.5% relates to Corridor debt outstanding and its financing costs are directly recoverable through the terms of the Corridor FSA. When deemed appropriate, Inter Pipeline may enter into interest rate swap agreements to manage its interest rate risk exposure.

The following interest coverage\* ratio is calculated on a consolidated basis for the twelve month periods ended December 31, 2016 and 2015.

<i>(times)</i>	Twelve Months Ended	
	December 31	
	2016	2015
Interest coverage <sup>(1)(2)</sup>	5.1	5.4

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(2) Net income attributable to shareholders plus income taxes and borrowing costs, divided by the sum of borrowing costs, capitalized borrowing costs and any retirement of obligations.

## Credit Ratings

The following investment grade, long-term corporate credit ratings or senior unsecured debt ratings are maintained by Inter Pipeline and by Inter Pipeline (Corridor) Inc.

	Credit Rating	Trend/Outlook
<b>Inter Pipeline Ltd.</b>		
S&P	BBB+	Stable
DBRS	BBB (high)	Stable
<b>Inter Pipeline (Corridor) Inc.</b>		
S&P	A	Stable
DBRS	A	Stable
Moody's	A2	Stable

\* Please refer to the NON-GAAP FINANCIAL MEASURES section

## Contractual Obligations, Commitments and Guarantees

The following table summarizes Inter Pipeline's expected capital spending profile and future contractual obligations at December 31, 2016. Management intends to finance short-term commitments either through existing or renegotiated credit facilities and FFO in excess of dividends. Longer term commitments will be funded through Inter Pipeline's capital management policies as discussed earlier in the **LIQUIDITY AND CAPITAL RESOURCES** section.

<i>(millions)</i>	Total	Less than one year	One to five years	After five years
Capital expenditure projects <sup>(1)</sup>				
Oil sands transportation	\$ 436.0	\$ 113.4	\$ 322.6	\$ -
Conventional oil pipelines	34.3	34.3	-	-
NGL processing	165.1	165.1	-	-
Bulk liquid storage	40.3	40.3	-	-
Growth capital funded by Inter Pipeline <sup>(2)</sup>	675.7	353.1	322.6	-
Sustaining capital funded by Inter Pipeline <sup>(2)</sup>	78.2	78.2	-	-
	753.9	431.3	322.6	-
Total debt <sup>(3)(4)</sup>				
Corridor syndicated credit facility <sup>(4)</sup>	1,340.6	1,340.6	-	-
Inter Pipeline syndicated credit facility	913.0	-	913.0	-
Corridor Debentures	150.0	-	150.0	-
Medium-Term Notes Series 1 to 9	3,425.0	400.0	1,025.0	2,000.0
	5,828.6	1,740.6	2,088.0	2,000.0
Other obligations				
Operating leases	342.2	29.3	104.8	208.1
Purchase obligations	231.7	33.8	81.2	116.7
Long-term portion of incentive plan	12.5	-	12.5	-
Adjusted working capital deficit <sup>(2)</sup>	74.9	74.9	-	-
	\$ 7,243.8	\$ 2,309.9	\$ 2,609.1	\$ 2,324.8

(1) Capital expenditures classified as "less than one year" represent expected spending in 2017.

(2) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(3) At December 31, 2016, outstanding Inter Pipeline letters of credit of approximately \$2.8 million were not included in total debt outstanding. Financial debt reported in the December 31, 2016 consolidated financial statements of \$5,806.3 million, includes long-term debt, short-term debt and commercial paper of \$5,828.6 million less discounts and debt transaction costs of \$22.3 million.

(4) Principal obligations are related to commercial paper. This amount is fully supported and management expects that it will continue to be supported by Corridor's fully committed syndicated credit facility that has no repayment requirements until December 2020.

The following future obligations resulting from the normal course of operations will be primarily funded from FFO in the respective periods that they become due or may be funded through debt:

- (i) Operating leases and purchase obligations represent minimum payment obligations associated with leases and normal operating agreements for periods up to 2094.
- (ii) Working capital deficiencies\* arise primarily from capital expenditures outstanding in accounts payable and accrued liabilities at the end of a period.
- (iii) Inter Pipeline has obligations of \$28.9 million under its employee long-term incentive plan, of which \$16.4 million is included in the working capital deficit\*.

\* Please refer to the NON-GAAP FINANCIAL MEASURES section

- (iv) Present value of estimated expenditures expected to be incurred in the longer term on decommissioning of active pipeline systems, NGL processing facilities and leased bulk liquid storage sites and remediation of known environmental liabilities is \$154.2 million at December 31, 2016. Due to the uncertainty of timing for payment of these obligations, they were excluded from the table above.

## DIVIDENDS TO SHAREHOLDERS

	Three Months Ended December 31		Years Ended December 31	
<i>(millions, except per share and % amounts)</i>	2016	2015	2016	2015
Cash provided by operating activities	\$ 199.5	\$ 233.9	\$ 805.9	\$ 760.5
Net change in non-cash operating working capital	55.2	(22.5)	42.9	13.6
Less funds from operations attributable to non-controlling interest <sup>(2)</sup>	(3.5)	(9.8)	(32.0)	(41.0)
Funds from operations attributable to shareholders	\$ 251.2	\$ 201.6	\$ 816.8	\$ 733.1
Dividends to shareholders	\$ 145.1	\$ 128.7	\$ 539.2	\$ 497.1
Dividends per share <sup>(3)</sup>	\$ 0.4000	\$ 0.3825	\$ 1.5700	\$ 1.4850
Payout ratio <sup>(1)</sup>	57.8%	63.8%	66.0%	67.8%

(1) Please refer to the NON-GAAP FINANCIAL MEASURES section.

(2) Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

(3) Dividends to shareholders are calculated based on the number of common shares outstanding at each record date.

Inter Pipeline's objective is to provide shareholders with stable dividends over economic and industry cycles. As a result, not all FFO attributable to shareholders are distributed to shareholders. A portion is withheld and reinvested in the business to effectively manage its capital structure, and in particular, debt levels. Inter Pipeline sets dividend levels based on the underlying assumptions in each year's annual operating and capital budget and long-term forecast, consistent with its goal to provide shareholders with stable dividends. Dividends are determined at the discretion of Inter Pipeline's Board of Directors, subject to certain legal requirements, and are payable when declared.

FFO is a financial measure that Inter Pipeline uses in managing its business and in assessing future cash requirements that impact the determination of future dividends to shareholders. Inter Pipeline expresses FFO attributable to shareholders as cash provided by operating activities less net changes in non-cash working capital and FFO attributable to non-controlling interest. The impact of net change in non-cash working capital is excluded in the calculation of FFO primarily to compensate for the seasonality of working capital throughout the year. Certain Inter Pipeline revenue contracts dictate an exchange of cash that differs, on a monthly basis, from the recognition of revenue. Within a 12-month calendar year, there is minimal variation between revenue recognized and cash exchanged. Inter Pipeline therefore excludes the net change in non-cash working capital in its calculation of FFO to mitigate its quarterly impact. The intent is to not skew the results of Inter Pipeline in any quarter for exchanges of cash, but to focus the results on cash that is generated in any reporting period.

The tables below show Inter Pipeline's dividends declared relative to cash provided by operating activities and net income attributable to shareholders for the periods indicated. See the **OUTLOOK** section of this report and **RISK FACTORS** section for further information regarding the sustainability of dividends.



<i>(millions)</i>	Three Months Ended		Years Ended	
	December 31		December 31	
	2016	2015	2016	2015
Cash provided by operating activities	\$ 199.5	\$ 233.9	\$ 805.9	\$ 760.5
Less cash provided by operating activities attributable to non-controlling interest <sup>(1)</sup>	(3.3)	(10.0)	(31.6)	(39.4)
Dividends to shareholders	(145.1)	(128.7)	(539.2)	(497.1)
Excess	\$ 51.1	\$ 95.2	\$ 235.1	\$ 224.0

(1) Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

<i>(millions)</i>	Three Months Ended		Years Ended	
	December 31		December 31	
	2016	2015	2016	2015
Net income attributable to shareholders	\$ 125.8	\$ 129.7	\$ 449.7	\$ 427.4
Dividends to shareholders	(145.1)	(128.7)	(539.2)	(497.1)
(Shortfall) excess	\$ (19.3)	\$ 1.0	\$ (89.5)	\$ (69.7)

Cash provided by operating activities in all periods was greater than dividends to shareholders plus cash provided by operating activities attributable to non-controlling interest. Dividends were greater than net income attributable to shareholders, except for the three months ended December 31, 2015, as net income also includes certain non-cash expenses such as depreciation and amortization, deferred income taxes and unrealized changes in the fair value of derivative financial instruments.

## OUTSTANDING SHARE DATA

Inter Pipeline's outstanding common shares at December 31, 2016 are as follows:

<i>(millions)</i>	Total
Common shares outstanding	367.9

At February 14, 2017, Inter Pipeline had 368.8 million common shares outstanding.

## RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

### Market Risk Management

Inter Pipeline may utilize derivative financial instruments to manage liquidity and market risk exposure to changes in commodity prices, foreign exchange and interest rates. Market risk management strategies are intended to minimize the volatility of Inter Pipeline's exposure to commodity price, foreign exchange and interest rate risk to assist with stabilizing FFO. Inter Pipeline prohibits the use of derivative financial instruments for speculative purposes. All hedging policies are authorized and approved by the Board of Directors through Inter Pipeline's market risk management policy.

Inter Pipeline may enter into the following types of derivative financial instruments: commodity price swap agreements, foreign currency exchange contracts, power price hedges and heat rate and interest rate swap agreements. The mark-to-market or fair value of these financial instruments is recorded as an asset or liability and any change in the fair value recognized as an unrealized change in fair value of these derivative financial instruments in the calculation of net income. When the financial instrument matures, any realized gain or loss is recorded in net income.

In the following sections, sensitivity analyses are presented to provide an indication of the amount that an isolated change in one variable may have on net income and are based on long-term debt, short-term debt and commercial paper outstanding at December 31, 2016. The analyses are hypothetical and should not be considered to be predictive of future performance. Changes in fair value generally cannot be extrapolated based on one variable because the relationship with other variables may not be linear. In reality, changes in one variable may magnify or counteract the impact of another variable which may result in a significantly different conclusion.

#### **FRAC-SPREAD RISK MANAGEMENT**

Inter Pipeline is exposed to frac-spread risk being the difference between the selling prices for certain NGL products and the input cost of the natural gas required to produce the respective products, including shrinkage gas. Various frac-spreads are as defined in the **Frac-spread** section of the **NGL Processing Business Segment**. Inter Pipeline may enter into natural gas liquids, AECO natural gas and foreign exchange swap contracts to manage frac-spread risk exposure in the NGL processing business. As at December 31, 2016, there were no frac-spread hedges outstanding.

#### **POWER PRICE RISK MANAGEMENT**

Inter Pipeline may use derivative financial instruments to manage power price risk in its NGL processing and conventional oil pipelines business segments. When deemed appropriate, Inter Pipeline enters into financial heat rate swap and power price swap contracts to manage power price risk exposure in these businesses. As at December 31, 2016, there were no electricity price swap or heat rate price swap agreements outstanding.

#### **FOREIGN EXCHANGE RISK MANAGEMENT**

Inter Pipeline is exposed to currency risk resulting from the translation of assets and liabilities of its European bulk liquid storage operations and transactional currency exposures arising from purchases in currencies other than Inter Pipeline's functional currency, the Canadian dollar. Transactional foreign currency risk exposures have not been significant historically, therefore are generally not hedged; however, Inter Pipeline may decide to hedge this risk in the future. As at December 31, 2016, there were no foreign currency exchange hedges outstanding.

### **Corporate**

#### **INTEREST RATE RISK MANAGEMENT**

Inter Pipeline's exposure to interest rate risk primarily relates to its long-term debt obligations. Inter Pipeline manages its interest rate risk by balancing its exposure to fixed and variable rates while minimizing interest costs. When deemed appropriate, Inter Pipeline may enter into interest rate or cross-currency swap agreements to manage its interest rate price risk exposure. As at December 31, 2016, there were no interest rate hedges outstanding.

Based on the variable rate obligations outstanding at December 31, 2016, a 1% change in interest rates at this date would have changed interest expense for the three months and year ended December 31, 2016, by approximately \$6.7 million and \$26.5 million, respectively, assuming all other variables remain constant. Of this amount, \$3.4 million and \$13.4 million for the three months and year ended December 31, 2016, respectively, relate to Corridor's syndicated credit facility and is recoverable through the terms of the Corridor FSA. The after-tax income impact for the three months and year ended December 31, 2016 would be \$2.4 million and \$9.6 million, respectively.

## Credit Risk

Inter Pipeline's credit risk exposure relates primarily to the non-performance of its customers and financial counterparties holding cash, accounts receivable, and prepaid expenses and other deposits. Credit risk is managed through Inter Pipeline's credit management policy, which establishes guidelines for defining and measuring credit risk, determining credit risk thresholds and monitoring credit risk exposures to counterparties and vendors. The creditworthiness assessment takes into account available qualitative and quantitative information about the counterparty including, but not limited to, business performance, financial status and external credit ratings. Depending on the outcome of each assessment, guarantees, letters of credit, prepayments or some other form of credit enhancement may be requested as security. Inter Pipeline attempts to mitigate its exposure by entering into contracts with customers that may permit netting or entitle Inter Pipeline to rely on indemnification provisions, a lien or take product in kind and/or allow for termination of the contract on the occurrence of certain events of default. Each business segment monitors outstanding accounts receivable on an ongoing basis.

Concentrations of credit risk associated with accounts receivable relate to a limited number of principal customers in the oil sands transportation and NGL processing business segments, the majority of which are affiliated with investment grade corporations in the energy and chemical industry sectors. At December 31, 2016, accounts receivable associated with these two business segments were \$152.4 million or 67.4% of total accounts receivable outstanding. Inter Pipeline believes the credit risk associated with the remainder of accounts receivable is minimized due to diversity across business segments and customers.

With respect to credit risk arising from cash and cash equivalents, deposits and derivative financial instruments, Inter Pipeline believes the risk of non-performance of counterparties is minimal as cash and deposits outstanding are predominantly held with major financial institutions or investment grade corporations.

Inter Pipeline actively monitors the risk of non-performance of its customers and financial counterparties. Accounts receivable are deemed past due if they are aged greater than 60 days and are considered to be impaired if one or more events have occurred that would impact the estimated future cash flows of that asset. At December 31, 2016, accounts receivable outstanding meeting the definition of either past due or impaired are insignificant.

## TRANSACTIONS WITH RELATED PARTIES

No revenue was earned from related parties in the three months and years ended December 31, 2016 or 2015.

## CONTROLS AND PROCEDURES

Disclosure controls and procedures (DC&P) are designed to provide reasonable assurance that all relevant information is gathered and reported to senior management, including the President and Chief Executive Officer and the Chief Financial Officer, on a timely basis so that appropriate decisions can be made regarding public disclosure.

Internal controls over financial reporting (ICFR) are a process designed to provide reasonable assurance regarding the reliability of financial reporting and compliance with GAAP in Inter Pipeline's consolidated financial statements.

No changes in Inter Pipeline's ICFR occurred during the period beginning on January 1, 2016 and ended on December 31, 2016 that has materially affected, or is reasonably likely to materially affect, Inter Pipeline's ICFR.

Management has limited the scope of their design of DC&P and ICFR to exclude controls, policies and procedures of the recently acquired Williams Canada, the results of which are consolidated in Inter Pipeline's interim financial statements at September 30, 2016 and the audited consolidated financial statements at December 31, 2016.

In September 2016, Inter Pipeline acquired Williams Canada. Where possible, Williams Canada has adopted Inter Pipeline's DC&P and ICFR. For business processes unique to Williams Canada, management is committed to completing DC&P and ICFR before the end of the third quarter of the 2017 fiscal year.

At December 31, 2016, Inter Pipeline's management, including the President and Chief Executive Officer and the Chief Financial Officer, conducted an evaluation of the effectiveness of Inter Pipeline's disclosure controls and procedures and internal control over financial reporting as defined under *National Instrument 52-109 Certification of Disclosure in Issuers' Annual and Interim Filings*. Based on that evaluation, the President and Chief Executive Officer and Chief Financial Officer concluded that the design and operation of Inter Pipeline's disclosure controls and procedures and internal control over financial reporting excluding Williams Canada were effective as of December 31, 2016.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of the annual consolidated financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future years could be material. Information about critical judgments, estimates and assumptions in applying accounting policies for these areas is included in the relevant sections of the notes to the financial statements. Estimates and underlying assumptions are reviewed on an ongoing basis and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Readers should refer to note 3 Summary of Significant Accounting Policies of the December 31, 2016 annual consolidated financial statements for a list of Inter Pipeline's significant accounting policies.

### Financial Instruments

Inter Pipeline may utilize derivative financial instruments to manage its exposure to market risk relating to commodity prices, foreign exchange and interest rates. Inter Pipeline has a market risk management policy that defines and specifies the controls and responsibilities associated with those activities managing market exposure to changing commodity prices (power, crude oil, natural gas, NGLs and olefins) as well as changes within the financial market relating to interest rates and foreign exchange exposure for Inter Pipeline. Inter Pipeline's market risk management policy prohibits the use of derivative financial instruments for speculative purposes. Inter Pipeline also reviews all significant agreements acquired, substantially modified or entered into for embedded derivatives.

Inter Pipeline has classified its financial instruments as follows: Cash and cash equivalents and the majority of accounts receivable are classified as cash, loans and receivables; dividends payable, the majority of accounts payable, accrued

liabilities and provisions, and long-term debt, short-term debt and commercial paper are classified as other financial liabilities.

For further discussion on Inter Pipeline's derivative financial instruments, see the **RISK MANAGEMENT AND FINANCIAL RESULTS** section.

## Intangible Assets

Inter Pipeline's intangible assets are amortized using an amortization method and term based on estimates of the useful lives of these assets. The carrying values of Inter Pipeline's intangible assets are periodically reviewed for impairment or whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. This review requires an estimate of future cash flows to be derived from the utilization of these assets based on assumptions about future events which may be subject to change depending on future economic or technical developments. A significant change in these assumptions or unanticipated future events could require a provision for impairment in the future which would be recorded as a charge against net income.

The Cold Lake Transportation Service Agreement (TSA) intangible asset is the estimated value, using a discounted cash flow analysis, of the shipping agreement entered into with the Cold Lake founding shippers on the Cold Lake pipeline system as valued on January 2, 2003. The term of the Cold Lake TSA extends until Cold Lake LP gives notice that it forecasts it will earn less than \$1.0 million of capital fees in the year. This intangible asset is being amortized on a straight-line basis over 30 years. The remaining amortization period of the Cold Lake TSA is approximately 16 years.

The NGL processing business' intangible assets consist of customer contracts for the sales of ethane, ethane-ethylene and propane-plus and a patented operational process utilized in one of the straddle plants. Contracts include fee-based contracts, cost-of-service contracts and commodity-based arrangements. On November 1, 2015, Inter Pipeline revised the estimated useful life of the NGL processing business' customer contract intangible assets from 30 years to a useful life that matches the term of the existing customer contracts. The revised estimate is more reflective of the evolving industry and economic environment. The value of these contracts is realized over the term of the agreement, which is the period over which amortization is being charged using the straight-line method. Should the useful life of a customer contract change, the amortization of the remaining balance would change accordingly. The average remaining amortization period of the NGL processing customer contracts is approximately 8 years. The patent is being amortized on a straight-line basis over the 14 years from the acquisition of the NGL processing business on July 28, 2004. The remaining amortization period of the patent is approximately two years.

In the bulk liquid storage business, Inter Terminals UK's intangible assets consist of a customer contract for the storage and handling of bulk liquid products. The value of this contract is being realized over the term of the agreement, which is the period over which amortization is being charged using the straight-line method. Should the term of the contract change, the amortization of the remaining balance would change prospectively. The remaining amortization period of the customer contract is approximately 10 years.

## Business Combinations

Business acquisitions are accounted for using the acquisition method of accounting at the date control of a business is obtained. The cost of an acquisition is measured as the aggregate of the fair values of the assets given or equity instruments issued, net of liabilities incurred or assumed. Costs directly associated with the acquisition are expensed. The consideration transferred of an acquired business is allocated to the identifiable assets acquired and liabilities assumed at

their estimated fair values on the acquisition date. The excess of the consideration transferred over the amount allocated to net assets is recorded as goodwill. All available information is used to estimate fair values. External consultants are typically engaged to assist in the fair value determination of identifiable intangible assets and other significant assets or liabilities. The preliminary allocation of consideration transferred may be adjusted, as necessary, up to one year after the acquisition closing date due to additional information impacting asset valuation and liabilities assumed.

The allocation process of the consideration transferred involves uncertainty as management is required to make assumptions and apply judgment to estimates of the fair value of the acquired assets and liabilities, including highest and best use of assets. Quoted market prices and widely accepted valuation techniques, including discounted cash flows and market multiple analyses are used to estimate the fair market value of the assets and liabilities, and depreciated replacement costs are used for the valuation of tangible assets. These estimates include assumptions on inputs within the discounted cash flow calculations related to forecasted revenues, cash flows, contract renewals, asset lives, industry economic factors and business strategies.

In certain circumstances Inter Pipeline may also be required to consider the differences between the acquisition of a business and the purchase of assets depending on the terms of an acquisition contract. Certain judgments can be made in this determination which could impact the valuation and recognition of assets acquired and liabilities assumed. When an asset acquisition occurs, the identifiable assets acquired and liabilities assumed are allocated based on the cost of the acquisition and no goodwill or gain on a bargain purchase is recognized.

## **Goodwill**

Inter Pipeline has goodwill in four of its cash generating units (CGU's): the Corridor and Polaris pipeline systems in the oil sands transportation business; Inter Terminals UK, Germany and Ireland; and Inter Terminals Denmark in the bulk liquid storage business. Assets are grouped in CGU's which are the lowest levels for which there are separately identifiable cash inflows. Goodwill represents the excess of the consideration transferred over the fair value of the net identifiable assets of the Corridor; Polaris; Inter Terminals UK, Germany and Ireland; and Inter Terminals Denmark CGU's. After initial recognition, goodwill is carried at cost less any write downs for impairment. During each fiscal year and as economic events dictate, management conducts an impairment test taking into consideration any events or circumstances which might have impaired the recoverable amount. Inter Pipeline assesses the recoverable amount of the goodwill for impairment on a fair value less costs of disposal basis by discounting projected future cash flows generated by these assets at a weighted average cost of capital that reflects the relative risk of the asset. If it is determined that the recoverable amount of the future cash flows is less than the carrying amount of the assets at the time of assessment, an impairment loss would be determined by deducting the fair value less costs of disposal on a discounted cash flow basis from the carrying amount. The recoverable amount of the underlying assets and liabilities were assessed and it was determined that there was no impairment of goodwill in 2016. Projected future cash flows used in the goodwill assessment represented management's best estimate of the future operating performance of these businesses at the current time. A significant change in these assumptions or unanticipated future events could require a provision for impairment in the future which would be recorded as a reduction of the carrying value of goodwill with a charge against net income.

## **Property, Plant and Equipment**

Calculation of the net book value of property, plant and equipment requires estimates of the useful life of the assets, residual value at the end of the asset's useful life, method of depreciation and whether impairment in value has occurred.

A change in any of the estimates would result in a change in the amount of depreciation and a charge to net income recorded in a period in which the change occurs, with a similar change in the carrying value of the asset on the consolidated balance sheet.

Property, plant and equipment in the oil sands transportation business consists of pipelines and related facilities. Depreciation of capital costs is calculated on a straight-line basis over the estimated service life of the assets, which is 80 years. The cost of pipelines and facilities includes all expenditures directly attributable to bringing the pipeline to the location and condition necessary for its intended use, including costs incurred for system construction, expansion and betterments until the assets are available for use. Pipeline system costs also include an allocation of directly attributable overhead costs and capitalized borrowing costs. Capitalization of borrowing costs ceases when the related property, plant and equipment are substantially complete and ready for its intended productive use.

Pipeline line fill and tank working inventory for the Cold Lake and Corridor pipeline systems represent petroleum based product purchased for the purpose of charging the pipeline system and partially filling the petroleum product storage tanks with an appropriate volume of petroleum products to enable a commercial operation of the facilities and pipeline. The majority of pipeline line fill for the Cold Lake and Polaris pipeline systems is owned by the shippers directly. The cost of line fill owned by Inter Pipeline includes all direct expenditures for acquiring the petroleum based products. Any line fill that Inter Pipeline continues to own upon the ultimate retirement and decommissioning of the pipeline systems will be recovered under the terms of the agreements. Cold Lake and Polaris line fill is carried at cost and Corridor line fill is carried at cost less accumulated depreciation. Proceeds from the sale of Cold Lake and Polaris line fill will be fully available to Inter Pipeline, whereas proceeds from the sale of Corridor's line fill will be used to fund the cost of any decommissioning obligations and to the extent Corridor's decommissioning obligations exceed the value of the line fill, Inter Pipeline will be obligated to fund the excess. To the extent the value of the line fill exceeds the decommissioning obligation; the excess funds will be refunded to the Corridor shippers. Depreciation of Corridor line fill is calculated on the same basis as the related property, plant and equipment.

On conventional oil pipeline systems expenditures for expansions and betterments are capitalized. Maintenance, pipeline integrity verification and repair costs are expensed as incurred. Depreciation of pipeline facilities and equipment commences when the pipelines are available for use. Depreciation of the capital costs is calculated on a straight-line basis over the estimated 80 year service life of the Bow River pipeline system assets and 30 year service life of the Central Alberta and Mid-Saskatchewan pipeline system assets. These estimates are connected to the estimated remaining life of the crude oil reserves expected to be gathered and shipped on these pipeline systems. Pipeline line fill and tank working inventory for the conventional oil pipeline systems represents petroleum based product purchased for the purpose of charging the pipeline systems and partially filling the petroleum product storage tanks with an appropriate volume of petroleum products to enable a commercial operation of the facilities and pipelines. The cost of line fill includes all direct expenditures for acquiring the petroleum based products. These product volumes will be recovered upon the ultimate retirement and decommissioning of the pipeline systems and are carried at cost.

Property, plant and equipment of the NGL processing business are comprised primarily of three straddle plants, two offgas plants, an olefinic fractionator, and the Boreal pipeline system. Expenditures on plant expansions, major repairs and maintenance, or betterments are capitalized, while routine maintenance and repair costs are expensed as incurred. Depreciation of the property, plant and equipment and additions thereto is charged once the assets are ready for their

intended use, and is calculated on a straight-line basis over the estimated useful life of the assets which ranges from 25 to 30 years.

The bulk liquid storage business' property, plant and equipment consist of storage facilities and associated equipment. Expenditures on expansion and betterments are capitalized, while maintenance and repair costs are expensed as incurred. Depreciation of the property, plant and equipment is calculated on a straight-line basis over the estimated service life of the assets, the majority of which ranges from four to 100 years.

## Inventory

Inventory is measured at the lower of cost and net realizable value and consists primarily of NGLs and olefins. The cost of inventories is determined using the weighted average costing method and includes direct purchase costs and when applicable, costs of production, extraction, fractionation, and transportation. Net realizable value is the estimated selling price in the ordinary course of business less the estimated selling costs. The reversal of previous net realizable value write-downs is recorded when there is a subsequent increase in the value of inventories.

## Provisions

A provision is recognized when it is determined that an obligation has arisen as a result of a past event, the obligation can be reliably estimated and it is probable that an outflow of economic benefits will be required to settle the obligation. Inter Pipeline's provisions represent legal or constructive obligations associated with decommissioning tangible long-lived assets at the end of their useful lives and loss contingencies, including environmental remediation costs arising from claims, assessments, litigation, fines and penalties, and other sources.

Decommissioning obligations and environmental liabilities are calculated based on current price estimates using current technologies in accordance with current legal or constructive requirements and are adjusted for inflation to when the decommissioning or remediation activity is anticipated. Where a range of estimates exists, the possible outcomes are weighted to determine a probable settlement value or the midpoint is used where all outcomes are equally likely. Inter Pipeline's decommissioning obligations are expected to occur when the assets are no longer economically viable. The economic lives of these assets are estimated based on future expectations involving the supply of petroleum, chemical and other products and demand for certain services and therefore the timing of decommissioning may change significantly in the future. Actual costs and cash outflows may differ from these estimates due to changes in laws or regulations, timing of projects, costs and technology. As a result, there could be material adjustments to the provisions established. If the effect of the time value of money is material, provisions are discounted to their present value using a pre-tax risk-free rate. The provision will accrete to its full value over time through charges to income, or until Inter Pipeline settles the obligation. Recoveries from third parties which are virtually certain to be realized are recorded separately and are not offset against the related provision.

On initial recognition of a decommissioning obligation, an amount equal to the estimated present value of the obligation is capitalized as part of the cost of the related long-lived asset and depreciated over the asset's estimated useful life. Any subsequent changes to the decommissioning cost estimate or discount rate will result in a similar adjustment to the cost of the related long-lived asset.

Property, plant and equipment related to the oil sands transportation and conventional oil pipelines businesses consist primarily of underground pipelines and above ground equipment and facilities. The potential cost of future decommissioning activities is a function of several factors, including regulatory requirements at the time of pipeline



abandonment, the diameter and length of the pipeline and the pipeline's location. Decommissioning requirements can vary considerably, ranging from purging product from the pipeline, refilling with inert gas and capping all open ends to removal of the pipeline and reclamation of the right-of-way. Under current regulations, the estimated cost for the decommissioning obligation include: such activities as purging product from the pipeline, refilling with inert gas and capping all open ends; and removal of surface facilities and reclamation of the surface facility sites. Decommissioning obligations for the oil sands transportation and conventional oil pipelines business assets are being accreted over a period of 40 to 290 years at a rate of 3.1% per annum, based on an estimated discounted value at December 31, 2016 of \$14.3 million.

NGL processing and the bulk liquid storage businesses consist mainly of three straddle plants, two offgas plants, one olefinic fractionator, the Boreal pipeline system and sixteen bulk liquid storage facilities, respectively. Inter Pipeline's decommissioning obligation represents the present value of the expected cost to be incurred upon the termination of operations and closure of the extraction plants, olefinic fractionator and leased bulk liquid storage sites. The estimated costs for decommissioning obligations include such activities as dismantling, demolition and disposal of the facilities and equipment, as well as remediation and restoration of the sites. Decommissioning obligations for the NGL processing business assets are being accreted over a period of 25 to 40 years at rates of 3.1% per annum based on the estimated discount value of \$57.8 million at December 31, 2016. The decommissioning obligation for the bulk liquid storage business assets are being accreted over a range of 30 to 40 years at rates of 2.5% to 3.7% per annum based on the estimated discounted value at December 31, 2016 of \$62.5 million.

Inter Pipeline's environmental remediation obligation relates to a number of projects which have been identified that Inter Pipeline is obligated to remediate in future periods. Based on management's current knowledge of regulations, technology and current plans to remediate these sites, an estimated discounted liability of \$19.6 million has been recognized at December 31, 2016. Environmental obligations for the conventional oil pipelines and bulk liquid storage businesses are being accreted over a period of five to ten years at rates of 1.35% to 2.5% and 0.1% to 1.85% per annum, respectively.

## **Obligations Relating to Employee Pension Plans**

Inter Pipeline provides retirement benefits for its UK, German and Irish employees under three separate defined benefit pension plans. These plans provide benefits based primarily on a combination of years of service and an estimate of final pensionable salary. Inter Pipeline's policy is to fund the amount of benefit as required by governing legislation. Independent actuaries perform the required calculations to determine the pension expense in accordance with GAAP. The most recent actuarial valuations of both the UK and German plans were carried out in 2016, while the Ireland plan was carried out in 2013.

The cost of pension benefits earned by certain employees in the UK, Germany and Ireland covered by the defined benefit pension plans is actuarially determined using the projected unit credit method. The determination of benefit expense requires assumptions such as the expected return on assets available to fund pension obligations, the discount rate used to measure obligations, expected mortality and the expected rate of future compensation. There is measurement uncertainty inherent in the actuarial valuation process because the determination of the cost and obligations associated with employee future benefits requires the use of various assumptions. Actual results will differ from results which are estimated based on assumptions.

Plan assets are measured at fair value for the purpose of determining the expected return on plan assets. Adjustments for plan amendments are expensed over the vesting period of the employee benefits. The expected return on Inter Pipeline's pension plan assets is calculated using the same interest rate as applied for the purpose of discounting the benefit obligation. Actuarial gains and losses arise from changes in assumptions and differences between assumptions and the actual experience of the pension plans. Actuarial gains and losses are recognized in full in the period in which they occur in other comprehensive income. Past service costs are recognized as an expense on a straight-line basis over the average period until the benefits become vested. If the benefits have already vested, immediately following the introduction of, or changes to, a pension plan, past service costs are recognized.

## Long-Term Incentive Plans

Awards are paid in cash under Inter Pipeline's Restricted Share Unit Plan (RSUP) and Performance Share Unit Plan (PSUP). The fair value basis of accounting is used for both plans whereby changes in the liability are recorded in each period based on the number of awards outstanding and the current market price of Inter Pipeline's shares plus an amount equivalent to cash dividends declared to date. Additionally, the valuation of the Performance Share Units (PSUs) incorporates the use of a performance multiplier, which is determined based on the achievement of two equally weighted, pre-determined, Board approved performance criteria. The expense is recognized over the vesting periods of the respective awards. Compensation expense and the long-term incentive liability are adjusted to reflect the use of actual historical forfeiture rates as well as estimated future forfeiture rates. The market-based value of the award approximates the intrinsic value as the awards have no exercise price.

## Government Grants

Government grants are initially recognized as deferred income at fair value when there is reasonable assurance that the grant will be received and any conditions attached to the grant will be fulfilled. Grants that compensate Inter Pipeline for expenses incurred are recognised as other income in the same periods in which the expenses are incurred. Grants that compensate Inter Pipeline for the acquisition or construction of an asset are recognised as other income over the periods necessary to match the related depreciation charges, or other expenses of the asset, as they are incurred.

## Income Taxes

### Current Income Taxes

Certain of Inter Pipeline's subsidiaries are taxable corporations in Canada and Europe.

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to taxation authorities. The tax rates and laws used to compute the amount are those that are enacted or substantively enacted, by the reporting date, in countries where Inter Pipeline and its subsidiaries operate and generate taxable income. The actual amount of income tax expense is final only when the tax return is filed and accepted by relevant tax authorities, which occurs subsequent to the issuance of the annual consolidated financial statements.

Management periodically evaluates positions taken in Inter Pipeline's entity tax returns with respect to situations in which applicable tax regulations are subject to interpretation. Provisions are established if appropriate.

Current income tax relating to items recognized directly in shareholders' equity is recognized in equity and not the income statement.

## Deferred Income Taxes

Inter Pipeline uses the liability method where deferred income taxes are recognized based on temporary differences between the carrying amounts of assets and liabilities recorded for financial reporting purposes and their tax bases.

Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and carried forward tax losses can be utilized. Assessing the recoverability of deferred taxes requires management to make significant estimates related to expectations of future taxable income. Estimates of future taxable income are based on forecast FFO and the application of existing tax laws.

The carrying amount of deferred tax assets is reviewed each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred income taxes contain uncertainties because of the assumptions made about when deferred tax assets are likely to reverse, and a judgment as to whether or not there will be sufficient taxable profits available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain.

Deferred tax assets and liabilities are measured using the tax rates that have been enacted or substantively enacted at the reporting date. The tax rates are those that are expected to apply in the year the asset is to be realized or the liability is to be settled. Future changes in tax laws affecting existing tax rates could limit the ability of Inter Pipeline to obtain tax deductions in future periods.

Deferred tax relating to items recognized outside net income is recognized outside net income. Deferred tax items are recognized in correlation to the underlying transaction either in comprehensive income or directly in shareholders' equity.

Deferred tax assets and liabilities have been offset if a legally enforceable right exists to offset current income tax assets against current income tax liabilities and the deferred taxes are related to the same taxable entity and the same taxation authority.

## Revenue Recognition

Revenue is recorded when services have been performed, the amount of revenue and associated costs can be reliably measured and when it is probable that consideration will be collected.

The Cold Lake and Polaris pipeline systems revenue is determined by the nature of the contract and is either recognized ratably over the term of fixed fee arrangements, or as volumes are transported and services are provided to each shipper. Where transportation agreements involve separately identifiable services, consideration is allocated amongst the services based on their relative estimated stand-alone selling prices. Long term ship-or-pay agreements, under which shippers are obligated to pay fixed amounts ratably over the life of the agreement regardless of volumes shipped, may contain make-up rights. Make-up rights are earned by the shippers when minimum volume commitments are not utilized during the period but under certain circumstances can be used to offset excess volumes in future periods, subject to expiry periods. Inter Pipeline recognizes revenues associated with make-up rights at the earlier of when the make-up volume is shipped, the make-up right expires, or when it is determined that the likelihood that the shipper will utilize the make-up rights is remote.

Revenue on the Corridor pipeline system is recognized as services are provided in accordance with terms prescribed by the Corridor FSA with the shippers. Under the terms of the Corridor FSA, revenues are determined by an agreed upon annual revenue requirement formula which allows for the recovery of prescribed expenditures and costs associated with the operation of the Corridor pipeline system, including debt financing costs, operating costs, Rate Base (as defined in the Corridor FSA) depreciation and taxes, as well as a rate of return on the equity component of the Rate Base determined with reference to a spread over a long-term bond yield reported by the Bank of Canada.

Revenues associated with the transportation, storage and processing of hydrocarbons on the conventional oil pipelines gathering systems, namely trunk line tariffs and gathering tariffs are recognized as the services are provided. The majority of volumes are transported on the conventional oil pipelines gathering systems under short-term contracts with a fixed tolling arrangement and no volume commitment made by the shipper.

Volumes purchased by Inter Pipeline to be used in the blending process that are then resold to the same party at a pre-arranged differential are recognized on a net basis. Sales of additional volumes created through the blending process, and volumes purchased from and sold to different parties, are recognized on a gross basis with corresponding product purchases. Revenue is recognized when title is transferred.

Revenue from the NGL processing business is recognized when the service is provided or when products are shipped to the customer in accordance with the terms of the sales contract, title or risk of loss has been transferred and pricing is either fixed or determinable. Revenue recognition is based on three methodologies: according to the terms of the commodity based arrangements which may include an annualized adjustment; fee based revenue which is recognized when volumes are produced; and cost-of-service revenue, which is predominantly based on a fixed monthly fee.

Revenues are derived from the storage and handling of bulk liquid products and provision of complementary services and are recognized as the services are provided. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates and sales taxes or duties. Revenue received in advance is recognized over the duration of the contract to which it applies.

## **Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset that takes a substantial period of time to get ready for its intended use are capitalized as part of the cost of the related assets, until such time as the assets are substantially ready for their intended productive use. All other borrowing costs are expensed in the period in which they are incurred. Borrowing costs include interest and other costs incurred in connection with the borrowing of funds. Borrowing costs are amortized over the estimated service life of the assets to which the borrowings relate.

## **Consolidation of Non-Controlling Interest**

Prior to November 1, 2016, when Inter Pipeline effectively acquired the remaining 15% interest in the Cold Lake pipeline system, management was required to exercise significant judgment in its assessment of control including, but not limited to, the determination of the activities of the investee that significantly affect the investee's returns, the investor's ability to direct those activities, the investor's exposure to returns of the investee, as well as the rights of other parties.

Cold Lake's USA established the decision-making abilities of Cold Lake's shareholders in relation to the Cold Lake pipeline system. Inter Pipeline had the ability to unilaterally approve those activities determined by management to most

significantly impact Cold Lake's returns and to proceed with significant capital projects, on a negotiated basis, without the approval or consent of the other third party owner. As a result, Inter Pipeline had control during the period where there was a non-controlling interest in Cold Lake.

Inter Pipeline had an indirect 85% ownership interest in the Cold Lake Pipeline Limited Partnership (Cold Lake LP) and an 85% ownership interest in its general partner, Cold Lake Pipeline Ltd. (collectively Cold Lake) until November 1, 2016, when Inter Pipeline effectively purchased the remaining 15% ownership interest.

Prior to November 1, 2016, non-controlling interest represented a 15% ownership interest in the Cold Lake pipeline system attributable to an unrelated third party. Cold Lake is governed by a Unanimous Shareholder Agreement (USA) which established the decision making abilities of the Cold Lake shareholders in relation to the Cold Lake pipeline system. Inter Pipeline had the ability to unilaterally approve those activities determined by management to most significantly impact returns without the consent of the unrelated third party, such as the identification of expansion and other transportation service opportunities, performance of due diligence, undertaking economic feasibility studies and managing decisions to undergo non-Cold Lake Transportation Service Agreement (TSA) capital projects, where a feasibility study has been undertaken. Accordingly, the results of Cold Lake were fully consolidated by Inter Pipeline and the portion of equity in entities not owned by Inter Pipeline was reflected as non-controlling interest within total equity on the consolidated balance sheets.

Transactions that result in changes in ownership interest while retaining control are accounted for as transactions with equity holders in their capacity as equity holders. As a result, no change in the carrying amount of assets or liabilities is recognized as a result of such transaction, and any gain or loss on such change of control is recognized in retained earnings. Costs directly associated with the change in ownership interest are also recognized in retained earnings.

## FUTURE ACCOUNTING PRONOUNCEMENTS

Certain new standards, interpretations and amendments to existing standards were issued by the IASB that are mandatory for accounting periods beginning on or after January 1, 2017 or later periods with early adoption permitted. The standards impacted are as follows:

### **IFRS 15 Revenue from Contracts with Customers (IFRS 15)**

IFRS 15 replaces IAS 18 *Revenue*, IAS 11 *Construction Contracts* and related interpretations and will be applied to annual periods beginning on January 1, 2018. IFRS 15 establishes a control based revenue recognition model under which revenue is recognized when control of the underlying goods or services for the particular performance obligation is transferred to the customer. This is achieved by applying the following five steps:

1. Identify the contract with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when, or as, the entity satisfies a performance obligation.

IFRS 15 will primarily affect the timing of revenue recognition under multiple element arrangements. Under multiple element arrangements, although the total revenue recognized during the term of a contract will be largely unaffected, the allocation of the transaction price to the delivered goods or services may result in revenue being deferred or accelerated from its associated cash flows. For short-term commodity based arrangements, no significant changes are expected on adoption of IFRS 15.

Inter Pipeline is currently assessing the impact of IFRS 15; however it is not possible to make a reliable estimate of the impact of the new standard at this time. Further analysis needs to be completed and changes to processes and systems will be required to collect the new data requirements and compile the historical comparatives.

### **IFRS 9 Financial Instruments (IFRS 9)**

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* and shall be applied to annual periods beginning on or after January 1, 2018, with early adoption permitted. IFRS 9 establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of financial statements for their assessment of the amounts, timing and uncertainty of an entity's future cash flows. Inter Pipeline is currently assessing the impact of IFRS 9; however the extent of the impact has not yet been determined.

### **IFRS 16 Leases (IFRS 16)**

IFRS 16 replaces IAS 17 *Leases* and shall be applied to annual periods beginning on or after January 1, 2019, with early adoption permitted. IFRS 16 establishes a single, on-balance sheet accounting model for lessees which will result in the recognition of a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Inter Pipeline is currently assessing the impact of IFRS 16; however, the extent of the impact has not yet been determined.

## **RISK FACTORS**

The risks summarized in the following sections may require Inter Pipeline to invest additional capital, pursue alternative business plans, or could have a material adverse effect on the business, financial condition, results of operations, funds from operations and future prospects of Inter Pipeline and its future ability to make cash dividends to shareholders. Readers are cautioned that this summary of risks may not be exhaustive, as there may be risks that are unknown and other risks that may pose unexpected consequences. Further, many of the risks are beyond Inter Pipeline's control and, despite Inter Pipeline's active management of its risk exposure, there is no guarantee that risk management activities will successfully mitigate such exposure.

### **Risks Associated with the Pipelines – The Oil Sands Transportation and Conventional Oil Pipelines Businesses**

#### **Throughput and Demand Risks**

Over the long term, Inter Pipeline's business will depend, in part, on the level of demand for petroleum in the geographic areas in which deliveries are made by the pipelines and the ability and willingness of shippers having access or rights to utilize the pipelines to supply such demand. Inter Pipeline cannot predict the impact of future economic conditions, fuel conservation measures, increasing demand for alternative fuel requirements, government regulation (including those resulting from the ratification of greenhouse gas legislation, including the initiatives discussed below) or technological

advances in fuel economy and energy generation devices, all of which could reduce the demand for petroleum, and major changes may have a material adverse effect on its business, financial condition, results of operations, cash flows and future prospects.

### **Supply Risks and Commodity Prices**

Future throughput on the pipelines and replacement of petroleum reserves in the pipelines' service areas are dependent upon the success of producers operating in those areas in exploiting their existing reserve bases and exploring for, developing and acquiring additional reserves. Reserve bases necessary to maintain long-term supply cannot be assured, and petroleum price declines, without corresponding reductions in costs of production, may reduce or eliminate the profitability of production and therefore the supply of petroleum for the pipelines. While reserve additions and increased recovery rates can offset natural declines in petroleum production in the areas serviced by the pipelines, reserve additions tend to not be sufficient to offset natural declines in produced volumes in certain service areas over the long term, which reduces the likelihood that reserve additions and increased recovery rates will offset natural declines in petroleum production in the future. Sustained low petroleum prices could lead to a decline in drilling or mining activity and production levels or the shutting-in or abandonment of wells or oil sands operations. Drilling and mining activity, production levels and shut-in or abandonment decisions may also be affected by the availability of capital to producers for drilling, allocation by producers of available capital to produce oil as compared to natural gas, current or projected petroleum price volatility, overall supply and demand expectations and light crude oil to heavy crude oil price differentials. The pipelines are dependent on producers' continuing petroleum exploration and development activity and on technological improvements leading to increased recovery rates in order to offset natural declines in petroleum production in the areas serviced by the pipelines. Absent the continuation of such activities and improvements, the volumes of petroleum transported on the pipelines will decline over time as reserves are depleted.

The Cold Lake, Polaris and Corridor pipeline systems service the Cold Lake and Athabasca oil sands regions of Alberta. Both areas contain substantial oil sands deposits. Bitumen is produced in the Athabasca region using an open-pit mine operation. In addition, in-situ recovery techniques such as cyclic steam stimulation (CSS) and steam-assisted gravity drainage (SAGD) are utilized in the Cold Lake and Athabasca regions. These techniques require higher levels of capital investment and, as a result, bitumen production in these areas is more sensitive to lower producer net-back prices than crude oil production in the conventional oil pipeline business segment. Producer net-back prices are affected by several factors, including bitumen prices, natural gas and diluent costs, light crude oil to heavy crude oil price differentials and government royalties. Natural gas is required to either heat water or generate steam in order to extract bitumen from the oil sands deposits. As well, the viscosity of bitumen requires diluent, a light petroleum product, to be blended with the bitumen to allow it to be transported through the pipeline. High natural gas prices or a shortage of diluent supply may increase the overall costs of producing bitumen, which may reduce production and/or delay development of new production in the Cold Lake and Athabasca oil sands regions.

The revenue generated from Inter Pipeline's midstream marketing activities relies on the availability and pricing of different crude oil streams and other commodities. The variability of supply, or an increase or decrease in the price of such crude oil or commodities, could reduce the financial results from these activities.

### **Competition and Contracts**

The majority of transportation revenue associated with Inter Pipeline's conventional pipeline business has been and is currently derived primarily from contracts or arrangements of 30 days duration or less with producers in the geographic

areas served by its pipelines. While Inter Pipeline attempts to renew contracts on the same or similar terms and conditions, there can be no assurance that such contracts will continue to be renewed or, if renewed, will be renewed upon terms favourable to Inter Pipeline. Inter Pipeline's transportation contracts with producers in the areas serviced by the conventional oil pipelines business are based on market-based toll structures negotiated from time to time with individual producers, rather than the cost-of-service recovery or fixed rate of return structures applicable to certain other pipelines. The conventional oil pipelines business is, and will continue to be, subject to market competitive factors.

The pipelines are subject to competition for volumes transported by rail, trucking, or by other pipelines near the areas serviced by the pipelines. Competing pipelines could be constructed in areas serviced by Inter Pipeline's pipelines and rail has emerged as a transportation option as producers seek to access higher value markets due to capacity constraints on downstream pipelines.

The Cold Lake pipeline system is operated pursuant to long-term contracts with shippers (including the Cold Lake pipeline system's founding shippers) who have committed to utilizing the Cold Lake pipeline system and who pay for such usage over the term of their contracts. Pursuant to the Cold Lake Transportation Service Agreement, the capital fee paid by the Cold Lake pipeline system's founding shippers is not subject to a minimum ship-or-pay threshold. Although volumes that are shipped by the Cold Lake pipeline system's founding shippers from the reserves dedication area while under the Cold Lake Transportation Service Agreement are generally committed to the Cold Lake pipeline system, the Cold Lake founding shippers may utilize alternative transportation methods (if certain minimum volume levels are maintained) subject to Inter Pipeline's right to match the alternative proposal. Consequently, there is no assurance that the level of volumes or revenues received from the Cold Lake founding shippers will be sustained.

The bitumen blend pipeline system that Inter Pipeline constructed pursuant to contracts with FCCL Partnership commenced operations in January, 2015, and the FCCL Partnership is obligated to transport bitumen blend under a long-term ship-or-pay agreement that has an initial term of 20 years, with options to extend up to an additional 30 years. However, there is no assurance that FCCL Partnership will be able to perform its obligations under the contract with Inter Pipeline, or that revenues received from FCCL Partnership following the expiry of the term of the contract will be sustained.

The Corridor pipeline system is operated pursuant to a long-term ship-or-pay contract with the Corridor shippers, who are contractually obligated to utilize the Corridor pipeline system for the transportation of all bitumen and diluent used or produced from the Athabasca oil sands project. There are 12 years remaining in the initial term of the agreement, extending through 2028 with options for further extensions. However, there is no assurance that the Corridor shippers will be able to perform their obligations under the contract with Inter Pipeline, or that revenues received from the Corridor shippers following the expiry of the term of the contract will be sustained.

The Polaris pipeline system is operated pursuant to long-term ship-or-pay contracts with various counterparties that are contractually obligated to utilize the Polaris pipeline system. However, there is no assurance that these counterparties will be able to perform their obligations under the contracts with Inter Pipeline, or that revenues received from the counterparties following the expiry of the term of each contract will be sustained.

Inter Pipeline can supplement revenues by marketing excess capacity on all three oil sands pipeline systems, including the excess capacity installed as part of the Cold Lake and Polaris pipeline system expansions for the FCCL Partnership, to third



parties, but there can be no assurance that they will be successful in doing so. Furthermore, any potential third party capacity rights on the Corridor pipeline system are also subject to the approval of the current Corridor shippers.

### **Operational Factors**

The pipelines are connected to various third party mainline systems such as the Enbridge system, Express pipeline, Trans Mountain pipeline, and the Milk River pipeline, as well as refineries and third party storage terminals in those areas where deliveries are made by the pipelines. Operational disruptions, apportionment, or changes to operating parameters on third party systems or refineries may prevent the full utilization of the pipelines, and could have an otherwise adverse effect on Inter Pipeline's overall operating results. The pipelines are reliant on electrical power for their operations. A failure or disruption within the local or regional electrical power supply or distribution or transmission systems could significantly affect ongoing pipeline operations. In addition, a significant increase in the cost of power, fuel or other operating costs in relation to the pipelines could have a materially negative effect on the financial results realized by the pipeline business in certain cases where the relevant contracts do not provide for recovery of such costs.

In the event of a major pipeline or facility incident resulting in the release of large quantities of product, dependent on the location and applicable insurance coverage, there could be a significant impact to the financial results and continuing operation of the impacted pipeline.

### **Rights-of-Way and Access**

Successful development of the pipelines through construction of new pipelines or extensions to existing pipelines depends in part on securing leases, easements, rights-of-way, permits and/or licenses from landowners or governmental authorities allowing access for such purposes. In general, the process of securing rights-of-way or similar access is becoming more complex, particularly in more densely populated, environmentally sensitive and other areas. The Cold Lake, Corridor, Polaris and Central Alberta pipeline systems have portions of their operations in the Edmonton area, with the Cold Lake pipeline system also having operations in the Hardisty area and within the Cold Lake air weapons range. Although pipelines have been constructed in these areas in recent years, these are three of the more complicated areas in which to secure pipeline rights-of-way in the Province of Alberta.

### **Regulatory Factors**

The pipelines are subject to intra-provincial and multi-jurisdictional regulation, including regulation by the Alberta Energy Regulator (AER) in Alberta, and the Ministry of the Economy in Saskatchewan. As a result, Inter Pipeline's operations may be affected by changes implemented by such regulatory authorities or in the legislation governing such authorities.

The Bow River, Central Alberta, Cold Lake, Corridor and Polaris pipeline systems are wholly within the boundaries of the Province of Alberta and are primarily subject to regulation under the *Pipeline Act* (Alberta) and *Pipeline Regulation* (Alberta), and by the AER. The Mid-Saskatchewan pipeline system is wholly within the boundaries of the Province of Saskatchewan and is subject to regulation under the *Pipelines Act* (Saskatchewan) and the *Pipelines Regulation* (Saskatchewan) and by the Ministry of the Economy in Saskatchewan. None of the pipelines are subject to regulation by the National Energy Board (NEB).

Oil pipelines in Alberta may be subject to rate regulation pursuant to the *Public Utilities Act* (Alberta). In Saskatchewan, oil pipelines may similarly be subject to rate regulation under the *Pipelines Act* (Saskatchewan).

Legislation in the Province of Alberta exists to ensure that shippers and producers have fair and reasonable opportunities to produce, transport, process, and market their reserves. Under the *Oil and Gas Conservation Act* (Alberta), the AER may,

on application, declare the proprietor of a pipeline to be a common carrier of oil or natural gas such that the proprietor must not discriminate among shippers and producers who seek access to the pipeline. If a pipeline is designated a common carrier and agreement cannot be reached between a proprietor and a shipper as to the tariff to be charged, then either party may apply to the Alberta Utilities Commission. Transportation service on the pipelines has been made available on an open access, non-discriminatory basis and the pipelines' tolls have not been set or restricted by any regulatory agency. Should an order for access or for the setting of tolls be made, it could result in a toll reduction and decreased revenue for Inter Pipeline.

## **Risks Associated with the NGL Processing Business**

### **Natural Gas Availability and Composition**

The volumes of natural gas processed by the straddle plants depend on the throughput of the TransCanada Alberta System from which the straddle plants source their natural gas supply. Without reserve additions, other new sources of natural gas supply, and associated investments in infrastructure to connect those supplies, throughputs will decline over time as reserves are depleted in the areas these pipeline systems currently service. Natural gas producers in these service areas may not be successful in exploring for and developing additional reserves or commodity prices may not remain at a level that encourages gas producers to explore for and develop additional reserves or to produce existing marginally economic reserves. Also, to continue to have the right to reprocess natural gas for the purpose of NGL processing from gas being transported on the TransCanada Alberta System, Inter Pipeline will be required to continue to negotiate processing agreements with the various natural gas shippers and there is no assurance that Inter Pipeline will be able to renew contracts related to the NGL processing business to extract NGL on terms favourable to Inter Pipeline.

The production of NGL from the straddle plants is largely dependent on the quantity and composition of the NGL within the natural gas streams that supply the straddle plants. The quantity and composition of NGL may vary over time. Also, marketable natural gas on the TransCanada Alberta System contains contaminants such as carbon dioxide and various sulphur compounds that are concentrated in the NGL products through the processing process. Increased content of these contaminants in the natural gas supply may require incurring additional capital and operating costs at the straddle plants. Other factors, such as an increased level of NGL recovery conducted at field processing plants upstream of or in parallel to the straddle plants (including the Harmattan co-stream facility described below), increased intra-Alberta consumption of natural gas or processing completed at any new processing plants constructed upstream of or in parallel to the straddle plants, or changes in the quantity and composition of the natural gas produced from the reservoirs that supply the straddle plants, could have a materially negative effect on NGL production from the straddle plants.

### **Offgas Availability and Composition**

The volumes of offgas supply processed by the offgas plants depend on volumes available from the Suncor Energy Oil Sands Limited Partnership's (Suncor) oil sands upgrader and the Canadian Natural Horizon oil sands upgrader from which the offgas plants source their offgas supply. These upgraders process bitumen that has been produced locally through mining or in-situ operations, also owned by Canadian Natural and Suncor. Combined, these capital intensive oil sands production and upgrader facilities have been built based on long-term economic outlooks with a stable and long-term proven supply of bitumen, with minimal decline risk. These facilities can be affected by the demand for their products, material changes in their key cost drivers, regulatory changes, and various other factors that may be outside the control of Canadian Natural and Suncor, all of which have the potential to reduce production and/or delay development of new production thereby impacting offgas supply available for processing at the offgas plants.

In addition, the volumes of offgas supply available to be processed by the offgas plants can be directly impacted by the reliability of the Suncor and Canadian Natural upgraders, or their related mining or in-situ operations and downstream transportation options for the products they produce. These are complex operations and any number of operational related issues may cause a material disruption to the supply of offgas available for processing at the offgas plants.

The production of ethane-plus from the offgas plants is largely dependent on the quantity and composition of the offgas supply produced by Canadian Natural and Suncor. The quantity and composition may vary over time as a result of changing bitumen quality, production issues, and/or process changes by Canadian Natural and Suncor, which could have a materially negative effect on production from the offgas plants and the Redwater Olefinic Fractionator.

### **Operational Factors**

The straddle plants, offgas plants, Redwater Olefinic Fractionator and Boreal pipeline system (collectively, the NGL Processing Facilities) are directly or indirectly connected to various third party systems, including the TransCanada Alberta System, Kerrobert Pipeline, Co-Ed Pipeline, the Alberta Ethane Gathering System, and the Joffre Feedstock Pipeline. Operational disruptions or apportionment on these third party systems and/or disruptions at the other facilities in the Empress, Redwater or Joffre areas may prevent the full utilization of the NGL Processing Facilities. In addition, various products produced at the Redwater Olefinic Fractionator are transported by rail or tank truck to end use customers in Canada and the United States. Any disruption to the operations, including labour disputes, infrastructure issues, or potential regulatory changes to the rail or trucking industry, could also impact the utilization of the offgas plants, Redwater Olefinic Fractionator and Boreal pipeline system.

The Redwater Olefinic Fractionator is also dependent on ethane-plus supplied by the Boreal pipeline system, which along with the offgas plants, are dependent on the reliable operation of the pipeline system. Any failure or disruption associated with the pipeline system could prevent the full utilization of the Redwater Olefinic Fractionator and the offgas plants, although this risk is partially mitigated through cavern storage for ethane-plus at the Redwater Olefinic Fractionator. The risks associated with this pipeline operated by Inter Pipeline are similar in nature to the Operational Factors, Rights-of-Way and Access, and Regulatory Factors as noted above in the Pipeline risk section.

The NGL Processing Facilities are reliant on electrical power for their operations. A failure or disruption within the local or regional electrical power supply or distribution or transmission systems could significantly affect ongoing NGL processing operations. In addition, a significant increase in the cost of power, fuel or other operating costs in relation to the NGL Processing Facilities could have a materially negative effect on the financial results realized by the NGL processing business in certain cases where the relevant contracts do not provide for recovery of such costs.

In the event of a major facility incident, such as a fire, major equipment damage or serious safety incident, there could be a significant impact to the financial results and continuing operation of the impacted NGL Processing Facilities should insurance not cover the incident.

### **Competition**

The straddle plants are subject to natural gas markets and, as such, are subject to competition for gas supply from all natural gas markets served by the TransCanada Alberta System. The straddle plants are subject to competition from other straddle plants that are in the general vicinity of the straddle plants or that may be constructed upstream of or in parallel to the straddle plants, including the Harmattan co-stream facility, described below. The straddle plants are also subject to competition from field processing facilities that extract NGL from the natural gas streams before injection into the

TransCanada Alberta System. Offgas plants are not subject to this type of competition as the offgas supply is received directly from the Suncor and Canadian Natural upgraders.

The Harmattan co-stream project, which became operational in late 2012, consisted of modifications to the Harmattan facility and a new bypass pipeline around the Cochrane plant for the purpose of extracting NGL from up to 490 mmcf/d of natural gas on the TransCanada Alberta System directly upstream of and in parallel to the Cochrane plant. This project has caused, and has further potential to cause, a significant reduction in volumes available for processing at the Cochrane plant. The Harmattan co-stream facility competes directly with the Cochrane plant for the right to reprocess gas volumes on the TransCanada Alberta System.

To the extent that: (i) other gas market participants are willing to pay for gas supply; (ii) existing or newly constructed straddle plants or field processing plants are successful in securing natural gas supply currently processed at the straddle plants or are successful in removing significant amounts of NGL from the gas supply upstream of the straddle plants; or (iii) products derived from the production at the straddle plants cannot be priced competitively, Inter Pipeline will be adversely affected.

Similarly, there is no assurance that new sources of natural gas supply that may be developed in areas such as the Montney and Duvernay in Northwest Alberta and Northeast British Columbia will be transported via the natural gas transmission systems connected to the straddle plants, or that new processing plants will not be constructed upstream of or in parallel to the straddle plants to process that natural gas.

Volumes of natural gas processed by the straddle plants are also dependent on commodity pricing competition between the Western Canadian Sedimentary Basin (WCSB) natural gas and other recently developed natural gas basins such as Marcellus. A growing supply of North American natural gas from such developments will compete with historical supplies and may significantly change traditional natural gas flow patterns. Such natural gas flow patterns may also be impacted by the development of Liquefied Natural Gas (LNG) export facilities competing for volumes, potentially adversely affecting natural gas to the straddle plants.

The products produced at the NGL Processing Facilities or derivatives produced at downstream customer facilities must compete with similar products from other facilities on a local, regional or continental scale. The markets in which Inter Pipeline sells its production are exposed to new infrastructure additions, repurposing of existing infrastructure, and significant changes in supply and demand associated with development of shale resources.

### **Commodity Price; Frac-spread**

At the Cochrane plant, Inter Pipeline is exposed to frac-spread risk or the relative price differential between the propane-plus produced and the natural gas used to replace the heat content removed during processing of the NGL from the natural gas stream. Financial results obtained from this portion of the NGL processing business will increase or decrease as the difference between the price of the applicable NGL and the price of natural gas varies. Propane-plus produced at the Cochrane plant is based on NGL sales at Sarnia linked to Mont Belvieu rather than Edmonton prices and is also sold in US currency, exposing Inter Pipeline's frac-spread margin to currency risk.

At the Redwater Olefinic Fractionator, Inter Pipeline can be exposed to possible price fluctuations between the time it stores ethane-plus from the Boreal pipeline system in local storage caverns, and the time it processes the ethane-plus. This can vary depending on the amount of inventory and price fluctuations. Inter Pipeline is also exposed to possible price fluctuations between the time it processes the ethane-plus and when it sells the NGL products. Inter Pipeline is exposed to

frac-spread risk being the difference between the selling prices for certain NGL products and the input cost of the natural gas required to produce the respective products, including shrinkage gas. Various frac-spreads are as defined in the **Frac-spread** section of the **NGL Processing Business Segment**.

### **Extraction Premiums**

Further influencing the financial results of the NGL processing business is the cost of natural gas feedstock in excess of the market price of natural gas. Currently, extraction premiums for the straddle plants are paid to export shippers in exchange for the ability to reprocess their natural gas for the purpose of NGL processing. Historically, these premiums have been moderate relative to the selling price of NGL, but it is possible that they could increase, which would adversely affect the NGL processing business.

Extraction rights for the offgas plants are granted pursuant to long-term contracts with the owners of oil sands upgrading facilities. Such contracts provide compensation through both fixed premium and profit sharing arrangements with minimal risk exposure to Inter Pipeline.

### **Contractual Risks**

NOVA Chemicals, Dow Chemical, and Plains Midstream are the principal customers of the NGL processing business and represent the majority of the revenue from this business. Plains Midstream also operates the Empress II and Empress V straddle plants. If, for any reason, any of these parties are unable to perform their obligations under the various agreements with Inter Pipeline, the financial results of the NGL processing business or the operations of the Empress II and Empress V straddle plants could be negatively impacted.

Inter Pipeline relies on NOVA Chemicals to purchase ethane-ethylene mix produced at the Redwater Olefinic Fractionator which is operated by Pembina NGL Corporation (Pembina). If, for any reason, Nova or Pembina is unable to perform their obligations under the agreements, the revenue and the operations of the offgas plants and Redwater Olefinic Fractionator could be negatively impacted. Various other products produced at the Redwater Olefinic Fractionator are sold under shorter term agreements to a variety of customers. Failure of these customers to accept the products, perform their obligations under the agreements, or the failure of Inter Pipeline to renew these agreements and/or find suitable alternative customers under similar terms and conditions could also negatively impact the revenue and operations of the offgas plants and Redwater Olefinic Fractionator.

Inter Pipeline has contractual relationships with Suncor and Canadian Natural for the delivery of offgas supply. If Suncor and Canadian Natural do not fulfill their contractual obligations, Inter Pipeline may not be able to source offgas supply and may therefore not be able to operate the offgas plants, Redwater Olefinic Fractionator and/or Boreal pipeline system, causing Inter Pipeline to suffer financial losses. Inter Pipeline is subject to re-contracting risk upon the expiry of long-term offgas supply contracts. The ability to re-contract economic volumes of offgas supply will be dependent on the viable production and upgrading of bitumen at the Suncor and Canadian Natural oil sands sites.

### **Regulatory Factors**

Straddle plants in Alberta are not commercially regulated and all such facilities secure extraction rights for the processing of natural gas from shippers on the TransCanada Alberta System under proprietary commercial arrangements known as the "NGL Extraction Convention". If an alternative model for contracting for extraction rights was to be implemented it would require changes to contracting counterparties and commercial arrangements, and potentially business process changes to the NGL Processing Facilities, which changes could adversely affect the NGL processing business.

The offgas plants, Redwater Olefinic Fractionator and Boreal pipeline system are not commercially regulated either; however, all NGL Processing Facilities are regulated by the AER and various legislation applicable to such facilities. As a result, Inter Pipeline's operations may be adversely affected by changes implemented by the AER or in the legislation governing the AER.

In addition to being regulated by the AER, the straddle plants and Redwater Olefinic Fractionator are subject to regulation under the *Oil and Gas Conservation Act* (Alberta), the *Oil and Gas Conservation Rules* (Alberta) and the *Environmental Protection and Enhancement Act* (Alberta); the offgas plants are subject to regulation under the *Oil Sands Conservation Act* (Alberta), the *Oil Sands Conservation Rules* (Alberta) and the *Environmental Protection and Enhancement Act* (Alberta); and the Boreal pipeline system is wholly within the boundaries of the Province of Alberta and is primarily subject to regulation under the *Pipeline Act* (Alberta) and *Pipeline Regulation* (Alberta).

### **Completion and Success of PDH and PP Opportunities**

There can be no assurance that Inter Pipeline will proceed to develop the PDH facility and PP facility; all necessary regulatory approvals can be obtained to develop and construct the PDH facility and PP facility; or the PDH facility or PP facility will achieve the anticipated benefits for Inter Pipeline. An inability to complete or realize the anticipated benefits of the PDH facility and PP facility could have an adverse effect on the financial results of Inter Pipeline.

## **Risks Associated with the Bulk Liquid Storage Business**

### **Demand for Bulk Liquid Storage**

The Inter Terminals business in the UK, Ireland and Germany is primarily involved in the storage and handling of liquids for local and regional petroleum refining and chemical businesses. The products stored and handled at these storage terminals are generally either feedstock for chemical plants and refineries or are products produced from those facilities. As a result, a sustained slowdown in either the petroleum refining, biofuels or chemical sectors serviced by the Inter Terminals business could adversely affect the bulk liquid storage business.

The Inter Terminals business in Denmark and Sweden is primarily involved in the storage and handling of liquids for the petroleum refining and general oil-trading business. Therefore, a sustained slowdown in the petroleum sector could adversely affect the Inter Terminals business. Sustained periods of backwardation in the oil products markets served by Inter Terminals Denmark and Sweden could also adversely affect the Inter Terminals business.

The bulk liquid storage business is highly integrated with local refineries in several areas where Inter Terminals operates. The financial results from the Inter Terminals business could be significantly reduced if there was a closure to one or more of these refineries, some of these refineries were owned by a single entity or if a refinery was converted into a competing storage facility.

### **Customs and Excise Warehouses**

The Inter Terminals business operates approved customs and excise warehouses, thereby permitting their respective customers to store products on a duty-suspended basis. Failure to comply with legal and regulatory requirements governing the operation of such warehouses could lead to liability for customs and excise duties, value added tax and penalties, including the withdrawal of the related authorizations, which in turn could result in a reduction in commercial activity at the facilities. Authorizations granted for both customs and excise warehouses gives rise to a risk that the Inter Terminals business could become jointly and severally liable with the product owner to any duties or taxes on products irrespective of compliance with legal and regulatory requirements by the Inter Terminals business.

The Inter Terminal business stores alcohol products at many warehouse locations. Failure to comply with regulatory measures to counteract fraudulent activity within the alcohol sector could result in the Inter Terminals business being held liable for duties or taxes in cases where it is evident that controls have not been sufficient to mitigate the risks.

### **Operational Factors**

In the event of a major facility incident resulting in a major fire or the release of large quantities of product, the location of the bulk liquid storage facilities adjacent to water courses and large bodies of water could result in a major environmental incident and significantly impact the financial results, reputation and continuing operation of the bulk liquid storage business.

### **Defined Benefit Pension Plan**

Defined benefit pension plans exist for certain employees and former employees of Inter Terminals' UK, Irish and German businesses. The UK and Irish plans hold interests in various securities invested in equities, fixed income instruments and real estate. Fluctuations in the value of the plans' assets and the factors which are applied to calculate the plans' liabilities could result in a requirement for additional cash contributions by Inter Terminals.

### **Competition**

The bulk liquid storage business faces competition from other independent bulk liquid terminals which operate in several of the regions serviced by Inter Terminals. Certain of the bulk liquid storage business' customers also have the option to store products at their own storage facilities or to adopt alternative logistics solutions. As a result, customers could elect in the future to make alternative arrangements for the storage and handling of their products resulting in a decline in the financial results of the bulk liquid storage business.

### **Land Lease Renewals**

Certain storage terminals and associated infrastructure are located on lands leased or licensed from third parties that must be renewed from time to time. Failure to renew the leases or licenses on terms acceptable to Inter Pipeline could significantly reduce the operations of the bulk liquid storage business, and could result in related decommissioning costs for Inter Pipeline, pursuant to the terms of such leases or licenses. Where there is such a legal obligation, decommissioning costs have been provided in the financial statements in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

### **Foreign Exchange Risk**

The bulk liquid storage business' earnings and cash flows are subject to foreign exchange rate variability, primarily arising from the denomination of such earnings and cash flows in British Pounds, Euros, Danish Kroner, Swedish Kronor and US dollars.

## **Risks Common to the Oil Sands Transportation, Conventional Oil Pipelines, NGL Processing and Bulk Liquid Storage Businesses**

### **Volatility in Commodity Prices**

Petroleum prices are determined by a wide range of political and economic factors external to Inter Pipeline and beyond its control. These factors include economic conditions in the US and Canada and worldwide, the actions of Organization of the Petroleum Exporting Countries (OPEC), governmental regulation, political stability in the Middle East and elsewhere, weather conditions, the foreign supply of oil and natural gas, risks of supply disruption, the price of foreign imports and

the availability of alternative fuel sources. Any substantial and extended decline in the prices of oil and natural gas liquids may have a material adverse effect on Inter Pipeline's business, borrowing capacity, financial condition, results of operations, financial results and future prospects. Lower commodity prices may render Inter Pipeline's development and expansion plans uneconomic.

Petroleum prices are expected to remain volatile as a result of market uncertainties over the supply and demand of these commodities that are caused by changing world economies, OPEC actions, credit and liquidity concerns, Middle East political unrest and a new government in the United States. Volatile commodity prices make it difficult to estimate the value of projects and often cause disruption in the market for oil and gas projects, as buyers and sellers have difficulty agreeing on such value. Price volatility also makes it difficult to budget for and project the return on acquisitions, and development and expansion projects.

### **Execution Risk**

Inter Pipeline's ability to successfully execute the development of its growth projects may be influenced by capital constraints, third party opposition, changes in customer support over time, delays in or changes to government and regulatory approvals, cost escalations, construction delays, labour and equipment shortages and in-service delays. Inter Pipeline's growth plans may strain its resources and may be subject to high cost pressures in the North American and European energy sectors. Early stage project risks include right-of-way procurement, special interest group opposition, Crown consultation, and environmental and regulatory permitting. Cost escalations may impact project economics. Construction delays due to slow delivery of materials, contractor non-performance, weather conditions and other shortages may impact project development and timing of related revenue. Labour shortages, inexperience and productivity issues may also affect the successful completion of projects.

### **Reputational Risk**

Reputational risk is the potential for negative impacts that could result from the deterioration of Inter Pipeline's reputation in the market or with key stakeholders. The potential for harming Inter Pipeline's reputation exists in every business decision and all risks can have an impact on reputation, which in turn can negatively impact Inter Pipeline's business and the value of common shares. Reputational risk cannot be managed in isolation from other forms of risk. Credit, market, investor relations, operational, third-party, insurance, liquidity, regulatory and legal risks must all be managed effectively to safeguard Inter Pipeline's reputation. Negative impacts from a compromised reputation could include reductions in cash flow and customer base, and a decrease in the value of common shares or debt securities.

Inter Pipeline's reputation as a reliable and responsible energy services provider with consistent financial performance and long-term financial stability is one of its most valuable assets. The key to effectively building and maintaining Inter Pipeline's reputation is fostering a culture that promotes integrity and ethical conduct. Ultimate responsibility for Inter Pipeline's reputation lies with Inter Pipeline's Board of Directors and executive team that examines reputational risk and issues as part of all business decisions. Nonetheless, every employee of Inter Pipeline and other representatives of Inter Pipeline have a responsibility to contribute in a positive way to Inter Pipeline's reputation. This means ensuring compliance with applicable policies, legislation and regulations, that ethical practices are followed at all times, and that interactions with our stakeholders are transparent. Reputational risk is most effectively managed when every individual works continuously to protect and enhance Inter Pipeline's reputation.



## **Credit Risk**

Inter Pipeline is subject to credit risk arising out of its operations. A majority of Inter Pipeline's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risk. Credit risk is managed through Inter Pipeline's credit management policy which sets out guidelines for defining and measuring credit risk, determining credit risk thresholds and monitoring credit risk exposures of counterparties and vendors. The credit worthiness assessment takes into account available qualitative and quantitative information about the counterparty, including, but not limited to, business performance, financial status and external credit ratings. Depending on the outcome of each assessment, guarantees, letters of credit, prepayments or some other form of credit enhancement may be requested as security; however, Inter Pipeline cannot be sure that counterparties are able to or will provide such requested security or that the amount of security provided will secure all obligations owing to Inter Pipeline. Inter Pipeline attempts to mitigate its exposure by entering into contracts with customers that may permit netting or entitle Inter Pipeline to rely on indemnification provisions, a lien or take product in kind, and/or allow for termination of the contract on the occurrence of certain events of default.

## **Royalty Regimes**

Inter Pipeline's pipeline and NGL processing business may be impacted by changes to the oil and gas royalty regime in effect in Alberta and Saskatchewan. Future royalty regime modifications could have adverse impacts on production of oil and gas volumes. Such changes may directly or indirectly impact Inter Pipeline in a materially different manner and/or in a manner that is more adverse to Inter Pipeline than the current royalty regime and regulatory framework.

## **Operational Factors**

Inter Pipeline's operations are subject to the customary hazards of the petroleum transportation, storage, marketing and processing business. Inter Pipeline's operations could be impacted by failures of pipelines (including pipeline leaks), storage tanks and caverns, power infrastructure, equipment, information systems, the performance of equipment at levels below those originally intended (whether due to misuse, unexpected degradation, design errors, or construction or manufacturing defects), failure to maintain an adequate inventory of supplies or spare parts, operator error, labour disputes, disputes with owners of interconnected facilities and carriers, and catastrophic events such as natural disasters, fires, flooding, explosions, chemical releases, fractures, or other events beyond Inter Pipeline's control, including acts of terrorists, eco-terrorists and saboteurs, and other third party damage to Inter Pipeline's assets. Operational errors could cause a process safety incident that additionally results in reputational damage to the business. The occurrence or continuance of any of these events could increase the cost of operating facilities and/or reduce their processing, throughput or storage capacity. An operational incident might result in the loss of life as well as injury and property damage. Inter Pipeline carries insurance with respect to some, but not all, casualty occurrences and disruptions. However, such coverage may not be sufficient to compensate for all casualty occurrences.

Insurance of Inter Pipeline's operations is susceptible to appetite for risk within the insurance market. Either general market conditions or a poor claims record could result in significantly increased premiums or the impossibility of obtaining coverage for certain risks. In the event that laws and regulations regarding minimum financial resources thresholds are established in jurisdictions in which Inter Pipeline carries on business, Inter Pipeline may incur increased costs to comply with such requirements.

Inter Pipeline has extensive integrity management programs in all of its business segments. While Inter Pipeline believes its programs are consistent with industry practice, increasingly strict operational regulations or new data on the condition

of Inter Pipeline's assets could result in repair or upgrading activities that are more extensive and costly than in the past. Such developments could contribute to higher operating costs for Inter Pipeline or the termination of operations on the affected portion of Inter Pipeline's assets.

A significant operating cost for Inter Pipeline is electrical power. Deregulation of the Alberta electrical power market has contributed to increased volatility in electrical power prices. Factors such as a shortage of electrical power supply or high natural gas prices could contribute to higher electrical power prices, which may result in higher operating costs for Inter Pipeline. In addition, Alberta's planned phase out of coal-fired electricity generation by 2030 and planned move to a "capacity market" for the purpose of pricing electricity could have an adverse effect on Inter Pipeline's business in Alberta.

Inter Pipeline continues to build on its business continuity planning, which involves analyzing critical activities, interdependencies and vulnerabilities to assist in prioritizing key functions and planning strategies and to recover or maintain them in the event of a significant business disruption. Critical infrastructure, personnel, supervisory control and data acquisition (SCADA) and information technology systems have redundancy established, which is intended to minimize both the probability and impact of disruptive events; however, there is no guarantee that such measures will be effective in the event of a worst case scenario.

### **Regulatory Intervention and Changes in Legislation**

Although fees charged to customers of the pipelines and the NGL processing business have not been set or restricted by any regulatory agency, an application to the Alberta or Saskatchewan regulators for the setting of fees could result in a reduction of fees and revenue for Inter Pipeline.

Income tax laws relating to the oil and natural gas industry or Inter Pipeline, environmental and applicable operating legislation, and the legislation and regulatory framework governing the oil and natural gas industry may be changed in a manner which adversely affects Inter Pipeline.

Failure of Inter Pipeline to comply with applicable regulations could result in sanctions, fines, litigation, or other adverse outcomes.

New regulations or legislation introduced may result in a significant increase in operating costs to ensure compliance. Such changes could have a materially negative effect on the financial results realized by Inter Pipeline in certain cases where the relevant contracts do not provide for recovery of such costs.

### **Decommissioning, Abandonment and Reclamation Costs**

Inter Pipeline is responsible for compliance with all laws, regulations and relevant agreements regarding the abandonment of its assets at the end of their economic lives and all associated costs, which costs may be substantial. Abandonment costs are a function of regulatory requirements at the time of abandonment, and the characteristics (such as diameter, length and location) of the pipeline or the size and complexity of the NGL processing or storage facility.

Abandonment requirements can vary considerably. For example, in the context of the pipelines, requirements can range from simply emptying the pipeline and capping all open ends, to the removal of the pipeline and reclamation of the related right-of-way. With respect to pipelines, the costs of abandonment have been limited primarily to the costs associated with the removal of petroleum from the lines, refilling with inert gas and capping all open ends, the removal of any associated surface facilities and surface reclamation of the disturbed site. However, future requirements are expected to be more stringent.

Abandonment and reclamation costs for the straddle plants and Redwater Olefinic Fractionator are regulated by the AER, pursuant to Directive 001 and, with respect to the straddle plants, Directive 024. The straddle plants and Redwater Olefinic Fractionator are included in the AER's *Large Facilities Liability and Reclamation Regulations* and have defined reclamation requirements and financial tests to ensure that end of life costs can be funded. However, future requirements may be more stringent.

In the future, Inter Pipeline may determine it prudent to establish and fund one or more reclamation trusts to address anticipated abandonment costs. The payment of the costs of abandonment of the pipelines, the NGL Processing Facilities, or the assets of the bulk liquid storage business, or the establishment of cash reserves for that purpose, could have a materially negative effect on the financial results realized by Inter Pipeline.

### **Environmental Costs and Liabilities**

Inter Pipeline's operations are subject to the laws and regulations of the European Union, UK, Germany, Ireland, Denmark, Sweden, Alberta and Saskatchewan, and the Canadian federal government relating to environmental protection and operational safety.

In order to continuously improve environmental performance and address regulatory requirements, Inter Pipeline routinely reviews systems, programs and processes critical to protecting the environment, including integrity programs, leak detection systems, air monitoring systems, contaminated sites program and maintenance standards. Improvement opportunities are implemented as deemed appropriate, with costs budgeted during Inter Pipeline's normal budget cycle in accordance with applicable accounting practices. Operation of certain of the pipelines, bulk liquid storage business assets and NGL Processing Facilities has spanned several decades. While the remediation of releases or contamination during such period may have met then-current environmental standards, such remediation may not meet current or future environmental standards and historical contamination may exist for which Inter Pipeline may be liable. Inter Pipeline has completed internal environmental reviews that have identified locations of historical contamination and several locations have been remediated. While Inter Pipeline believes such reviews have identified all locations of historical contamination, others may exist. The remaining identified, but unremediated, sites will be addressed in a prioritized manner, utilizing industry practices, with some locations being subject to multi-year reclamation plans.

It is possible that other developments, such as increasingly strict environmental and safety laws, regulations and enforcement policies thereunder, and claims for damages to property or persons resulting from Inter Pipeline's operations and previously undetected locations of historical contamination, could result in substantial costs and liabilities for Inter Pipeline. If, at any time, regulatory authorities deem any one of the NGL Processing Facilities, oil sands transportation, conventional oil pipelines or bulk liquid storage business assets unsafe or not in compliance with applicable laws, they may order it shut down. Inter Pipeline could be adversely affected if it was not able to recover such resulting costs through insurance or other means.

While Inter Pipeline maintains insurance in respect of damage caused by seepage or pollution in amounts it considers prudent and in accordance with industry standards, certain provisions of such insurance may limit the availability thereof in respect of certain occurrences unless such seepage or pollution is both sudden and unexpected, and discovered and reported within fixed time periods. If Inter Pipeline is unaware of a problem or is unable to locate the problem within the relevant time period, insurance coverage may not be available.

## Greenhouse Gas Regulations

Inter Pipeline's facilities and other operations and activities emit greenhouse gases (GHG) and require Inter Pipeline to comply with greenhouse gas emissions legislation in Alberta. Alberta facilities emitting more than 100,000 tonnes of GHGs a year are currently subject to compliance with the *Climate Change and Emissions Management Act* (CCEMA) which requires a reduction in emissions intensity over a period of years. The CCEMA and the associated *Specified Gas Emitters Regulation* require certain facilities to reduce their emissions intensity in: (i) 2016 to 85%; and (ii) 2017 80%, of their baseline for 2008 and subsequent years, with their baseline being established by the average of the ratio of the total annual emissions to production for the years 2003 to 2005. The Cochrane plant is the only asset of Inter Pipeline that is subject to provincial GHG regulations. Regulated emitters can meet their emissions intensity targets by contributing to the Climate Change and Emissions Management Fund or by purchasing emissions credits. The cost of credits were \$20 per tonne in 2016 and are \$30 per tonne in 2017. The *Specified Gas Emitters Regulation* is set to expire on December 31, 2017 and it is unclear when the amended regulations will be put in place and what the amended regulations will include.

On January 1, 2017, the *Climate Leadership Act* (Alberta) and the associated *Climate Leadership Regulation* (Alberta) came into force and created registration requirements for "direct remitters" and imposed a carbon levy on certain fuels used in Alberta. The carbon levy is in effect a tax on certain regulated fuels at a rate of \$20 per tonne of greenhouse gas emissions in 2017 and rising to \$30 per tonne in 2018. Inter Pipeline has completed an assessment of its businesses and obtained all required registrations and available exemptions from the carbon levy with the result that Inter Pipeline will only have non-material obligations. For example, that the carbon levy applies to fuels used by Inter Pipeline for vehicles, maintenance, heating and electricity generation. The carbon levy exemptions available to Inter Pipeline on fuels used in a production process expire January 1, 2023. It is unclear if any replacement exemptions will be put in place at that time.

In October 2016, the Canadian federal government announced a national carbon pricing floor. This pan-Canadian approach to pricing carbon will require all provincial jurisdictions to have carbon pricing in effect by 2018 with a minimum floor or \$50 per tonne by 2022, or Ottawa will impose a federal carbon tax. Alberta's Climate Leadership Plan is intended to meet the federal requirement for a provincial carbon price by 2018.

The Paris Climate Conference (COP) in 2015 resulted in the *Paris Agreement*, which expresses the long-term goal of signatories to keep the increase in global average temperature to well below 2°C above pre-industrial levels and the aim to limit the increase to 1.5°C. It also recognizes the need for global emissions to peak as soon as possible and to undertake rapid reductions following such peak. As Canada has become a signatory to and ratified the *Paris Agreement*, Inter Pipeline may be required to comply with the regulatory scheme for GHG emissions ultimately adopted by the federal government, which may or may not be consistent with the regulatory scheme for GHG emissions proposed for adoption in Alberta. The future implementation or modification of GHG regulations, whether to meet the limits regulated by the *Paris Agreement* or as otherwise determined, could have an adverse effect on Inter Pipeline's business, financial condition, results of operations and prospects.

The adoption of legislation or other regulatory initiatives designed to reduce GHG and air pollutants from oil and gas producers, refiners and chemical producers and electric generators in the geographic areas served by the pipelines, NGL Processing Facilities and bulk liquid storage business could result in, among other things, increased operating and capital expenditures for those operators. This may make certain production of petroleum and natural gas by those producers uneconomic, resulting in reduced or delayed production, or reduced scope in planned new development or expansion projects. The operation of certain refineries and chemical plants may also become uneconomic. In addition, the adoption

of new regulations concerning climate change and the reduction of GHG emissions and other air pollutants or other related federal or provincial legislation, may also result in higher operating and capital costs for the pipelines and NGL Processing Facilities. Given the evolving nature of the debate related to climate change and the control of GHG and resulting requirements, it is not possible to fully predict the impact on Inter Pipeline and its operations and financial condition.

### **Dependence on Key Personnel**

The success of Inter Pipeline is largely dependent on the skills and expertise of key personnel who manage Inter Pipeline's business. The continued success of Inter Pipeline will be dependent upon its ability to hire and retain such personnel. Inter Pipeline does not have any "key man" insurance.

### **International Operations**

A portion of Inter Pipeline's operations are conducted in the UK, Germany, Ireland, Denmark and Sweden. Operations outside of Canada are subject to various discrete risks, including: natural disasters; market downturn or failure; currency exchange rate fluctuations; foreign economic conditions; credit conditions; trade barriers; exchange controls; national and regional labour strikes; political risks and risks of increases in duties; taxes and changes in tax laws; and changes in laws and policies governing operations of foreign-based companies.

### **Possible Failure to Realize Anticipated Benefits of Acquisitions**

Inter Pipeline has completed a number of acquisitions and, as part of its business plan, anticipates making additional acquisitions in the future. There is a risk that some or all of the expected benefits of completed acquisitions may fail to materialize, or may not occur within the time periods Inter Pipeline anticipates. Achieving the benefits of completed and future acquisitions depends in part on successfully consolidating functions, and integrating operations, procedures and personnel in a timely and efficient manner, as well as Inter Pipeline's ability to realize the anticipated growth opportunities and synergies from combining the acquired businesses and operations with those of Inter Pipeline. The integration of acquired businesses requires the dedication of substantial management effort, time and resources, which may divert management's focus, and resources from other strategic opportunities and from operational matters. The integration process may also result in the loss of key employees and the disruption of ongoing business, customer and employee relationships that may adversely affect Inter Pipeline's ability to achieve the anticipated benefits of past and future acquisitions. Acquisitions may expose Inter Pipeline to additional risks, including entry into markets or businesses in which Inter Pipeline has little or no direct prior experience, increased credit risks through the assumption of additional debt, costs and contingent liabilities and exposure to known or unknown liabilities of the acquired business or assets.

### **Information provided by the Sellers**

All information relating to entities acquired through acquisitions is based on public filings and other information provided by the sellers. Although Inter Pipeline conducts what it believes to be a prudent and thorough level of investigation in connection with acquisitions, an unavoidable level of risk remains regarding the accuracy and completeness of such information.

### **Potential Undisclosed Liabilities Associated with Acquisitions**

In connection with an acquisition, there may be liabilities that Inter Pipeline failed to discover or were unable to quantify in Inter Pipeline's due diligence which Inter Pipeline conducted prior to an acquisition or which may have been worse than anticipated and Inter Pipeline may not be indemnified for some or all of these liabilities. The discovery or quantification of

any material liabilities could have a material adverse effect on Inter Pipeline's business, financial condition or future prospects. In addition, liabilities in respect of an acquired business may be greater than the amounts for which Inter Pipeline is indemnified under an acquisition agreement.

### **Capital Maintenance Levels**

Inter Pipeline maintains and periodically replaces portions of its assets to sustain facility performance, provide a high level of asset integrity and ensure reliable operations. The funds associated with these efforts may be in the form of sustaining capital\* or maintenance expenses. Maintenance expenses are a subset of "operating expenses" and are not reported separately.

Inter Pipeline typically maintains its assets with reasonable levels of sustaining capital\* and maintenance expenditures. However, both sustaining capital\* and maintenance expenditures may vary considerably from current and forecast amounts as a result of a number of factors, including high equipment failure rates, more stringent government regulations and any additional efforts deemed necessary by Inter Pipeline to improve the reliability of its assets. An increase in capital and/or maintenance expenditures could result in significant additional costs to Inter Pipeline.

### **Possible Downgrade of Investment Grade Credit Ratings**

Inter Pipeline and its unsecured medium-term notes have investment grade credit ratings of BBB+ and BBB (high), by S&P and DBRS, respectively. Corridor's debentures have been assigned investment grade credit ratings of A, A2 and A by DBRS, Moody's and S&P, respectively. Should these credit ratings fall below investment grade, Inter Pipeline or Inter Pipeline (Corridor) Inc. may have to provide security, pay additional interest or pay in advance for goods and services. The perceived creditworthiness of Inter Pipeline and changes in its credit ratings may also affect the value of Inter Pipeline's common shares or debt securities. There is no assurance that any credit rating assigned to Inter Pipeline or Inter Pipeline (Corridor) Inc. will remain in effect for any given period of time or that any rating will not be lowered or withdrawn entirely by the relevant rating agency. A lowering or withdrawal of such rating may have an adverse effect on the market value of Inter Pipeline's common shares or debt securities.

Inter Pipeline (Corridor) Inc.'s commercial paper is rated R-1 (low) by DBRS. If Inter Pipeline (Corridor) Inc.'s commercial paper rating falls below this level, Inter Pipeline (Corridor) Inc. may not be able to issue commercial paper and be required to use higher cost financing to fund its financial obligations.

### **Liquidity Risk**

Liquidity risk is the risk that Inter Pipeline will not be able to meet its financial obligations. To manage this risk, Inter Pipeline forecasts its cash requirements to determine whether sufficient funds will be available. Inter Pipeline's primary sources of liquidity and capital resources are FFO, draws under committed credit facilities and the issuance of new equity capital or debt securities. Inter Pipeline maintains a base shelf prospectus with Canadian securities regulators, which, subject to market conditions, enables it to readily access Canadian public capital markets.

### **Refinancing Risk**

Inter Pipeline's credit facilities, medium-term notes and other outstanding financing instruments or debt securities each have a maturity date, on which date, absent replacement, extension or renewal, the indebtedness under the respective loan agreement becomes repayable in its entirety. To the extent any of the loan agreements are not replaced or extended

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\* Please refer to the NON-GAAP FINANCIAL MEASURES section

on or before their respective maturity dates or are not replaced, extended or renewed for the same or similar amounts or on the same or similar terms, Inter Pipeline's ability to fund ongoing operations and pay dividends could be impaired.

Inter Pipeline's ability to refinance its indebtedness under its credit facilities, medium-term notes, and other outstanding financing instruments or debt securities will depend upon its future operating performance and FFO, which are subject to prevailing economic and credit conditions, prevailing interest rate levels and financial, competitive, business and other factors, many of which are beyond its control.

### **Litigation or Arbitration**

Due to the nature of Inter Pipeline's business, Inter Pipeline is subject to legal proceedings and claims. Although management of Inter Pipeline believes such claims would be without merit, litigation or arbitration is expensive, time consuming and may divert management's attention away from the operation of Inter Pipeline. If any legitimate cause of action or arbitral matter arose which was successfully prosecuted against Inter Pipeline, Inter Pipeline's financial position, operations or results of operations could be materially and adversely affected.

In certain instances third parties have agreed or will agree to indemnify, defend and hold Inter Pipeline harmless from and against various claims, litigation and liabilities arising in connection with certain transactions or business matters. There is no assurance that third parties will possess sufficient assets, income, access to financing and insurance coverage to enable them to satisfy their indemnification obligations in favour of Inter Pipeline. In addition, Inter Pipeline may not be able to successfully enforce such indemnities or such indemnities may not be sufficient to fully indemnify Inter Pipeline from third party claims. The inability to recover fully any significant liabilities through an indemnity may have adverse effects on Inter Pipeline's financial position, operations or results of operations.

### **Aboriginal Land Claims**

Aboriginal peoples have claimed aboriginal title and/or rights, whether established pursuant to treaty or otherwise, to a substantial portion of the lands in western Canada. Such claims and rights could have an impact on future access to public lands and thereby adversely affect Inter Pipeline's Canadian operations.

### **Crown Duty to Consult First Nations**

The federal and provincial governments in Canada have a duty to consult and, where appropriate, accommodate aboriginal people where the interests of the aboriginal peoples may be affected by a Crown action or decision. Accordingly, the Crown's duty may result in regulatory approvals being delayed or not being obtained in relation to Inter Pipeline's Canadian operations.

### **Weather Conditions**

Weather conditions can affect the demand for and price of natural gas and NGL. As a result, changes in weather patterns can affect throughput, as well as Inter Pipeline's NGL processing business. For instance, colder winter temperatures generally increase demand for natural gas and NGL used for heating which tends to result in increased throughput volumes at facilities and higher prices in the processing and storage businesses. In its NGL processing business, Inter Pipeline attempts to position itself to be able to handle increased volumes of throughput and storage at its facilities to meet changes in seasonal demand; however, at any given time, facility and storage capacity is finite.

Weather conditions may influence Inter Pipeline's ability to complete capital projects, repairs or facility turnarounds on time, potentially resulting in delays and increasing costs of such capital projects and turnarounds. Weather may also affect

the access to Inter Pipeline facilities, and operations and projects of Inter Pipeline's customers or shippers, thereby influencing the supply of transportation services and products.

With respect to construction activities, in areas where construction can be conducted in non-winter months, Inter Pipeline attempts to schedule its construction timetables so as to minimize delays due to cold winter weather.

### **Labour Relations**

Labour unions may from time to time be established in certain Inter Pipeline business segments. Unionized labour disruptions could restrict the ability of Inter Pipeline to carry out its business and therefore affect Inter Pipeline's financial results.

### **Policies and Procedures**

Inter Pipeline has a number of formal and informal policies and procedures in place to govern certain business and governance processes and the entering into and administration of contracts. Deviations from such policies and procedures, or a lack of certain policies and procedures, could result in negative impacts, including failure to realize all available revenue from contracts, inefficiencies and potential litigation.

### **Cyber-Security Threats and Reliance on Information Technology**

Inter Pipeline's operations are dependent on the functioning of several information technology systems. Exposure of Inter Pipeline's information technology systems to external threats poses a risk to the security of these systems. Such cyber-security threats include unauthorized access to information technology systems due to hacking, viruses and other causes that can result in service disruptions, system failures and the disclosure, deliberate or inadvertent, of confidential business information. Significant interruption or failure of any or all of these systems could result in operational outages, delays, lost profits, lost data, increased costs, and other adverse outcomes. These factors could include a loss of communication links or reliable information, security breaches by computer hackers and cyber terrorists, and the inability to automatically process commercial transactions or engage in similar automated or computerized business activities.

## **Risks Inherent in the Corporation**

### **Fluctuating Dividends; Dividends Are Not Guaranteed**

There is uncertainty with respect to future dividend payments by Inter Pipeline and the level thereof. Funds available for the payment of dividends will be dependent upon, among other things, FFO, the execution of its growth strategy, financial requirements for Inter Pipeline's operations and limitations under its credit facilities as well as the satisfaction of liquidity and solvency tests imposed by the *Business Corporations Act* (Alberta) (ABCA) on corporations for the declaration and payment of dividends.

### **Market Price of the Common Shares**

The prices at which Inter Pipeline's common shares will trade cannot be predicted. The annual yield on the common shares as compared to annual yield on other financial instruments may also influence the price of Inter Pipeline's common shares.

In addition, the market price for Inter Pipeline's common shares may be affected by changes in general market or economic conditions, legislative changes, fluctuations in the markets for equity securities, interest rates, commodity prices and numerous other factors to be within and beyond the control of Inter Pipeline, many of which are enumerated here.



## **Capital Resources**

Future expansions of Inter Pipeline's assets and other capital expenditures will be financed out of FFO, sales of additional equity or debt securities and borrowings. There can be no assurance that sufficient capital will be available to Inter Pipeline on acceptable terms, or in an amount sufficient, to fund expansion or other required capital expenditures.

## **Leverage**

Borrowings made by Inter Pipeline (including, for clarity, various subsidiaries thereof) introduce leverage into Inter Pipeline's business which increases the level of financial risk in the operations of Inter Pipeline. To the extent interest rates are not fixed, interest rate variations will increase the sensitivity of interest payments made by Inter Pipeline.

## **Debt Restrictive Covenants**

The credit facilities, medium-term notes and the Corridor debentures described in the **LIQUIDITY AND CAPITAL RESOURCES** section contain numerous restrictive covenants that limit the discretion of Inter Pipeline's management with respect to certain business matters. These loan agreements may contain covenants that place restrictions on, among other things, the ability of Inter Pipeline to create liens or other encumbrances, to pay dividends or make certain other payments, loans and guarantees, and to sell or otherwise dispose of assets and merge or consolidate with another entity. In addition, the loan agreements contain various financial covenants that require Inter Pipeline to meet certain financial ratios and financial condition tests. A failure to comply with these obligations could result in a default which, if not cured or waived, could result in a reduction or termination of dividends by Inter Pipeline and permit acceleration of the relevant indebtedness. In the event of certain Inter Pipeline (Corridor) Inc. bankruptcy or insolvency events, Inter Pipeline lenders have certain rights to accelerate Inter Pipeline's debt. In addition, in some circumstances, it may become necessary to restrict or terminate dividends by Inter Pipeline in order to avoid a default of such obligations.

## **Issues of Additional Common Shares; Dilution**

Inter Pipeline may issue additional common shares in the future to finance capital expenditures, including acquisitions. Any issuance of common shares may have a dilutive effect to existing shareholders.

## **Foreign Exchange Risk on Dividends**

Inter Pipeline's cash dividends will be declared and paid in Canadian dollars. As a consequence, non-resident shareholders, and shareholders who calculate their income in currencies other than the Canadian dollar, will be subject to foreign exchange risk. To the extent that the Canadian dollar strengthens with respect to the reporting currency of a shareholder, the amount of the dividend will be reduced when converted to that currency.

## **Conflicts of Interest**

Certain directors of Inter Pipeline are also directors of other entities engaged in the energy business generally. As a result, situations may arise where the interest of such directors conflict with their interests as directors of other companies. The resolution of such conflicts is governed by applicable corporate laws, which require that directors act honestly, in good faith and with a view to the best interests of the company. Conflicts, if any, will be handled in a manner consistent with the procedures and remedies set forth in the ABCA. The ABCA provides that in the event that a director has an interest in a contract or proposed contract or agreement, the director shall disclose his interest in such contract or agreement and shall refrain from voting on any matter in respect of such contract or agreement unless otherwise provided by the ABCA.

## Anti-Corruption Violations

The Canadian *Corruption of Foreign Public Officials Act*, the *US Foreign Corrupt Practices Act* and similar anti-bribery laws generally prohibit companies from making improper payments to foreign officials for the purpose of obtaining or retaining business. Given the nature of Inter Pipeline's business and international operations, Inter Pipeline has from time to time regulatory and business interaction with governments and government-owned entities and contact with persons who may be considered foreign officials. Inter Pipeline cannot guarantee that its employees, officers, directors, agents, or business partners have not in the past or will not in the future engage in conduct undetected by Inter Pipeline's processes and procedures and for which Inter Pipeline might be held liable under applicable anti-corruption laws. Violations of these laws, or allegations or investigations of allegations of such violations, could harm Inter Pipeline's reputation, disrupt its business and result in a material adverse effect on the business, results of operations, and financial condition of Inter Pipeline.

## NON-GAAP FINANCIAL MEASURES

Certain non-GAAP financial measures referred to in this MD&A, namely "adjusted working capital deficiency", "EBITDA", "adjusted EBITDA", "Consolidated Net Debt to Total Capitalization", "enterprise value", "funds from operations per share", "growth capital expenditures", "sustaining capital expenditures", "interest coverage", and "payout ratio" are not measures recognized by GAAP. These non-GAAP financial measures do not have standardized meanings prescribed by GAAP and therefore may not be comparable to similar measures presented by other entities. Investors are cautioned that non-GAAP financial measures should not be construed as alternatives to other measures of financial performance calculated in accordance with GAAP.

The following non-GAAP financial measures are provided to assist investors with their evaluation of Inter Pipeline, including their assessment of its ability to generate cash and fund monthly dividends. Management considers these non-GAAP financial measures to be important indicators in assessing its performance.

**Adjusted working capital deficiency** is calculated by subtracting current liabilities from current assets including cash and excluding the fair value of derivative financial instruments, commercial paper and current portion of long-term debt. This financial measure is used by Inter Pipeline in the Contractual Obligations, Commitments and Guarantees table in the **LIQUIDITY AND CAPITAL RESOURCES** section of this MD&A to capture other working capital items not specifically included in the table.

	December 31	
<i>(millions)</i>	2016	2015
Current assets		
Cash and cash equivalents	\$ 21.4	\$ 40.3
Accounts receivable	226.1	183.1
Prepaid expenses and other deposits	20.1	26.3
Inventory	13.3	0.6
Current liabilities		
Dividends payable	(49.7)	(43.8)
Accounts payable, accrued liabilities and provisions	(277.3)	(220.6)
Current income taxes payable	(18.7)	(29.6)
Deferred revenue	(10.1)	(7.5)
Adjusted working capital deficiency	\$ (74.9)	\$ (51.2)

**EBITDA and adjusted EBITDA** are reconciled from the components of net income as noted below. EBITDA is expressed as net income before total interest less capitalized interest, income taxes, depreciation and amortization; adjusted EBITDA also includes additional adjustments for loss (gain) on disposal of assets, non-cash expense (recovery), non-cash financing charges and unrealized change in fair value of derivative financial instruments. These additional adjustments are made to exclude various non-cash items, or items of an unusual nature that are not reflective of ongoing operations. These adjustments are also made to better reflect the historical measurement of EBITDA used in the investment community as an approximate measure of an entity's operating cash flow based on data from its income statement.

<i>(millions)</i>	Three Months Ended December 31		Years Ended December 31	
	2016	2015	2016	2015
Net income	\$ 128.8	\$ 138.0	\$ 477.6	\$ 463.0
Financing charges	40.8	38.5	147.0	142.1
Current income tax (recovery) expense	(5.7)	25.3	51.0	70.0
Deferred income tax expense	53.1	17.7	100.4	117.4
Depreciation and amortization	64.8	52.6	229.7	188.4
EBITDA	\$ 281.8	\$ 272.1	\$ 1,005.7	\$ 980.9
Loss on disposal of assets	4.3	0.6	6.5	5.6
Non-cash financing charges	(2.4)	(2.1)	(7.0)	(6.5)
Non-cash expense (recovery)	3.7	2.7	20.0	(0.1)
Unrealized change in fair value of derivative financial instruments	-	(0.1)	-	(0.2)
Proceeds from long-term lease inducements	-	-	14.6	-
Adjusted EBITDA	\$ 287.4	\$ 273.2	\$ 1,039.8	\$ 979.7
Less adjusted EBITDA attributable to non-controlling interest <sup>(1)</sup>	(3.5)	(9.8)	(32.1)	(41.0)
Adjusted EBITDA attributable to shareholders	\$ 283.9	\$ 263.4	\$ 1,007.7	\$ 938.7

(1) Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

<i>(millions)</i>	Three Months Ended December 31		Years Ended December 31	
	2016	2015	2016	2015
Funds from Operations	\$ 254.7	\$ 211.4	\$ 848.8	\$ 774.1
Total interest less capitalized interest	38.4	36.5	140.0	135.6
Current income tax (recovery) expense	(5.7)	25.3	51.0	70.0
Adjusted EBITDA	\$ 287.4	\$ 273.2	\$ 1,039.8	\$ 979.7
Less adjusted EBITDA attributable to non-controlling interest <sup>(1)</sup>	(3.5)	(9.8)	(32.1)	(41.0)
Adjusted EBITDA attributable to shareholders	\$ 283.9	\$ 263.4	\$ 1,007.7	\$ 938.7

(1) Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

**Adjusted EBITDA by contract type** is a percentage of adjusted EBITDA, reconciled in the table above, based on (i) cost-of-service contracts which generally provide for a return on invested capital and recovery of substantially all operating costs. This includes both cost-of-service contracts (agreements that are not impacted by throughput volume or commodity price fluctuations) and modified cost-of-service contracts (agreements that may have throughput volume exposure in certain circumstances) collectively referred to as cost-of-service contracts, (ii) fee-based contracts are generally subject to throughput volume and operating cost exposure, but not commodity price fluctuations, and (iii) commodity-based contracts are generally subject to throughput volume, operating cost and commodity price fluctuations. This measure, in

combination with other measures, is used by the investment community to assess the overall stability and predictability of the business.

	Years Ended December 31	
	2016	2015
<b>Adjusted EBITDA by contract type</b>		
Cost-of-service	59%	63%
Fee-based	29%	30%
Commodity-based	12%	7%

	Cost-of- service	Fee-based	Commodity- based
<b>Contract type by business segment</b>			
Oil sands transportation	√	-	-
Conventional oil pipelines	-	√	√
NGL processing	√	√	√
Bulk liquid storage	-	√	-

**Consolidated Net Debt to Total Capitalization** is disclosed and discussed in the Financial Covenant table of the **LIQUIDITY AND CAPITAL RESOURCES** section of this report. This measure in combination with other measures, are used by the investment community to assess the financial strength of the business.

**Enterprise value** is calculated by multiplying the period-end closing common share price by the total number of common shares outstanding and adding total debt (excluding discounts and debt transaction costs). This measure, in combination with other measures, is used by the investment community to assess the overall market value of the business. Enterprise value is calculated as follows:

	December 31	
<i>(millions, except per share amounts)</i>	2016	2015
Closing share price	\$ 29.64	\$ 22.21
Total closing number of common shares outstanding	367.9	336.4
	10,903.9	7,472.0
Total debt	5,828.6	4,851.7
Enterprise value	\$ 16,732.5	\$ 12,323.7

**Funds from operations per share** are calculated on a weighted average basis using basic common shares outstanding during the period. This measure together with other measures, are used by the investment community to assess the source, sustainability and cash available for dividends.

**Growth capital expenditures** are generally defined as expenditures which are recoverable or incrementally increase cash flow or earnings potential of assets, expand the capacity of current operations or significantly extend the life of existing assets. This measure is used by the investment community to assess the extent of discretionary capital spending.

**Sustaining capital expenditures** are generally defined as expenditures which support and/or maintain the current capacity, cash flow or earnings potential of existing assets without the associated benefits characteristic of growth capital expenditures. This measure is used by the investment community to assess the extent of non-discretionary capital spending.

					Three Months Ended December 31	
					2016	2015
<i>(millions)</i>	Growth	Sustaining		Total	Total	
Oil sands transportation	\$ 5.7	\$ 0.2	\$ 5.9	\$ 19.9		
Conventional oil pipelines	4.0	2.5	6.5	25.2		
NGL processing	24.2	4.1	28.3	1.3		
Bulk liquid storage	16.0	6.1	22.1	15.4		
Corporate	-	9.4	9.4	18.6		
Capital expenditures	\$ 49.9	\$ 22.3	\$ 72.2	\$ 80.4		
Capital expenditures funded by Inter Pipeline <sup>(1)</sup>	\$ 49.8	\$ 22.3	\$ 72.1	\$ 79.4		

					Years Ended December 31	
					2016	2015
<i>(millions)</i>	Growth	Sustaining		Total	Total	
Oil sands transportation	\$ 17.3	\$ 1.0	\$ 18.3	\$ 147.5		
Conventional oil pipelines	51.5	5.7	57.2	130.5		
NGL processing	26.0	12.6	38.6	7.7		
Bulk liquid storage	55.8	12.2	68.0	40.3		
Corporate <sup>(2)</sup>	-	26.9	26.9	29.9		
Capital expenditures	\$ 150.6	\$ 58.4	\$ 209.0	\$ 355.9		
Capital expenditures funded by Inter Pipeline <sup>(1)</sup>	\$ 149.6	\$ 58.3	\$ 207.9	\$ 347.6		

(1) Capital expenditures funded by Inter Pipeline exclude the 15% non-controlling interest in the Cold Lake pipeline system. Effective November 1, 2016, Inter Pipeline acquired the remaining 15% ownership interest in the Cold Lake pipeline system.

(2) Corporate sustaining capital, in 2016, predominately relates to leasehold improvement costs for the new office space and upgrades to Inter Pipeline's financial systems.

**Interest coverage** is calculated as net income attributable to shareholders plus income taxes, and borrowing costs, divided by the sum of borrowing costs, capitalized borrowing costs and any retirement of obligations. This measure is used by the investment community to determine the ease with which borrowing costs are satisfied.

**Payout ratio** is calculated by expressing dividends declared to shareholders for the period as a percentage of funds from operations attributable to shareholders. This measure, in combination with other measures, is used by the investment community to assess the sustainability of the current dividends.

## ADDITIONAL INFORMATION

Additional information relating to Inter Pipeline, including Inter Pipeline's **Annual Information Form** is available on SEDAR at [www.sedar.com](http://www.sedar.com)

The MD&A has been reviewed and approved by the Audit Committee and the Board of Directors of Inter Pipeline.

**Dated at Calgary, Alberta this 16th day of February, 2017**