

QUESTIONS AND ANSWERS

The following Questions and Answers are intended to address some of the key aspects of the Meetings and the Arrangement. This section is a summary only and is qualified in its entirety by the more detailed information appearing elsewhere in the Information Circular, including the Appendices thereto. Preferred Shareholders are encouraged to read the Information Circular in its entirety and to consult with their own legal, tax, financial and other professional advisors with respect to the matters to be acted on at the Meetings. Capitalized terms used but not otherwise defined in the Questions and Answers have the meanings set forth under the heading "Glossary of Terms" in the Information Circular.

Process

1. When is the vote?

- The Meetings will be held on February 16, 2017 at BMO Centre, 20 Roundup Way S.W., Calgary, Alberta, Room 100B, at the following times:
 - Series A Meeting: 9:30 a.m. (Calgary time)
 - Series B Meeting: 10:15 a.m. (Calgary time)
 - Series C Meeting: 11:00 a.m. (Calgary time)
 - Series E Meeting: 11:45 a.m. (Calgary time)
 - Series G Meeting: 12:30 p.m. (Calgary time)

See "General Information for the Special Meetings" in this Information Circular.

2. How do I vote?

- **Option 1:** Vote through your Intermediary
 - Beneficial Preferred Shareholders must comply with the instructions on the voting instructions or proxy form well in advance of the applicable Meeting in order to ensure their Preferred Shares can be voted at the applicable Meeting.
 - If you are a non-objecting beneficial owner (and have permitted the disclosure of your ownership information to the Corporation) you will receive voting instruction forms or a proxy which include a 16-digit control number that allows you to provide your voting instructions by telephone, on the Internet, by mail or by fax. If you want to provide your voting instructions:
 - on the Internet, go to Broadridge's website at www.proxyvote.com and follow the instructions. You will need your 16-digit control number, which you will find on your voting instruction or proxy form; or
 - by telephone, call 1-800-474-7493 (English) or 1-800-474-7501 (French).
 - If you are an objecting beneficial owner (and have not permitted the disclosure of your ownership information to the Corporation), you may be a non-registered Preferred Shareholder who will receive from your Intermediary voting instructions or a proxy form which:

- is to be completed and returned as directed in the instructions provided; or
 - has been pre-authorized by your Intermediary indicating the number of Preferred Shares to be voted, which is to be completed, dated and signed and returned to Broadridge by mail or fax.
- **Option 2:** Attend the applicable Meeting(s) and vote in person.
 - Appoint yourself as your proxyholder by writing your name in the space provided on the request for voting instructions or proxy form.
 - Do not complete the voting section on the request for voting instructions or proxy form as your vote will be taken at the applicable Meeting and return the request for voting instructions or proxy form to your Intermediary.

See "*How to Vote*" in this Information Circular.

3. How many votes are needed to approve each applicable Arrangement Resolution?

- Each series of Preferred Shares will vote separately as a series at the applicable Meeting. Each Arrangement Resolution must be approved by not less than 66 $\frac{2}{3}$ % of the votes cast by the holders of the applicable series of Preferred Shares present in person or represented by proxy at the applicable Meeting.
- A quorum for each Meeting for purposes of considering the applicable Arrangement Resolution shall be one or more persons present in person or represented by proxy at the opening of such Meeting holding in the aggregate not less than a majority of the outstanding series of Preferred Shares entitled to be voted at such Meeting. If within 30 minutes from the time appointed for the Meeting, a quorum in respect of the applicable series of Preferred Shares is not present, the Meeting shall stand adjourned to a date not less than 15 days later, and at a time and place as may be determined by the Chair of the Meeting. Notice of any such adjourned meeting shall be given not less than 10 days prior to the date fixed for such adjourned meeting and at such adjourned meeting the Preferred Shareholders of the applicable series present in person or represented by proxy, whether or not they hold a majority of the applicable series of Preferred Shares then outstanding, shall constitute a quorum for all purposes.

See "*Quorum and Voting Results – Approval of the Arrangement Resolutions*" in this Information Circular.

4. How do dissent rights work?

- Dissent rights provide Preferred Shareholders with the right to dissent in respect of the applicable Arrangement Resolution and, in the event the Arrangement becomes effective for the applicable series of Preferred Shares held by such Dissenting Shareholder, to be paid by the Corporation the fair value of the Preferred Shares of the applicable series held by such Dissenting Shareholder.
- The fair value of a Preferred Share is determined as at the close of business on the day before the applicable Arrangement Resolution is adopted or, upon application, by the Court, all in accordance with the procedures set forth in Section 190 of the CBCA as modified by the Interim Order and the Plan of Arrangement.
- Section 190 of the CBCA, as modified by the Plan of Arrangement and the Interim Order, requires adherence to the procedures established therein and failure to do so may result in the loss of all rights thereunder.

See "*Dissent Rights*" in this Information Circular.

Motivations

5. Why is TransAlta pursuing the Arrangement? What are the benefits for TransAlta?

- TransAlta is pursuing the Arrangement because we believe that it provides benefits to both Preferred Shareholders and TransAlta.
- Upon completion of the Arrangement Preferred Shareholders are expected to benefit from the following:
 - (a) downside protection from the new minimum floor feature which will ensure dividends on the Series 1 Preferred Shares will never be below 6.50%;
 - (b) the 6.50% dividend rate is generally higher than the coupon rate for other similarly rated preferred share issuances in the Canadian market;
 - (c) an immediate increase in dividends as compared to the Preferred Shares, and the Series 1 Preferred Shares are expected to receive higher dividends over the next five years, assuming current interest rate levels continue to apply over such five year period;
 - (d) enhanced trading liquidity by virtue of a larger consolidated series of Series 1 Preferred Shares; and
 - (e) tax flexibility for Preferred Shareholders to effect the Arrangement on a tax deferred basis or elect to effect the Arrangement on a taxable basis to realize a capital gain or capital loss for Canadian federal income tax purposes.
- Upon completion of the Arrangement, TransAlta is expected to benefit in the following ways:
 - (a) a reduction in the carrying value associated with the Preferred Shares on our balance sheet, which in turn improves some rating agency credit ratios based on the equity treatment given to the Preferred Shares;
 - (b) an improvement in the liquidity and underlying features of the Series 1 Preferred Shares (including the minimum floor feature) which could improve the trading yield and provide a more beneficial benchmark for any subsequent preferred share issuances by TransAlta; and
 - (c) the Arrangement will provide future preferred share issuance capacity based on the equity treatment guidelines of the Corporation's credit rating agencies.

See "*The Arrangement – Reasons for the Arrangement*" in this Information Circular.

6. Why have other companies with rate reset preferred shares not pursued a similar type of transaction?

- There have been other preferred share exchange transactions from other issuers, but each transaction is unique and is not comparable to the proposed Arrangement.

7. Does TransAlta require that all series of Preferred Shares approve the applicable Arrangement Resolution in order to effect the Arrangement?

- The Corporation may proceed with the Arrangement for each series of Preferred Shares for which the applicable Arrangement Resolution has been approved and the Final Order has been granted even if holders of one or more series of Preferred Shares do not approve the applicable Arrangement Resolution. In the event that one or more of the Arrangement Resolutions are not approved by the applicable series of Preferred Shareholders, the Arrangement will not be completed in respect of such series of Preferred Shares and such holders will continue to hold their Preferred Shares.
- The Corporation has full flexibility to proceed with the Arrangement in respect of one or more of the series of Preferred Shares assuming all required conditions to effect the Arrangement have been satisfied and/or waived, as applicable.
- In order to give effect to the Arrangement for a particular series of Preferred Shares, the applicable Arrangement Resolution must be approved by not less than 66⅔% of the votes cast by holders of such particular series of Preferred Shares and all other conditions must be satisfied and/or waived by TransAlta, as applicable.

See "*Quorum and Voting Results – Approval of the Arrangement Resolutions*" and "*The Arrangement – Conditions Precedent to Completion of the Arrangement*" in this Information Circular.

8. Why did TransAlta modify the exchange ratio for the Series A Shares? Why were none of the other series adjusted?

- Following the announcement of the proposed Arrangement, the Corporation decided to increase the exchange ratio in respect of the Series A Shares to 0.530 which represents an implied offer premium of 10.9% relative to the December 16, 2016 closing prices for the Series A Shares on the TSX. This more appropriately aligns the premium offered to the Series A Shareholders to the premium offered to other Preferred Shareholders. The Corporation believes this adjustment will increase the support of the proposed Arrangement while maintaining fairness for holders of all other series of Preferred Shares.

See "*The Arrangement – Reasons for the Arrangement*" in this Information Circular and the Fairness Opinion attached as Appendix "G" to this Information Circular.

Exchange Ratios

9. How were the exchange ratios determined?

- TransAlta evaluated many metrics in determining the exchange ratios including, but not limited to, (i) the immediate dividend increase applicable to the Series 1 Preferred Shares; (ii) the price premium being offered in respect of each series of Preferred Shares; (iii) the reset spread premium; (iv) the impact to longer term dividends; (v) the value attributable to the minimum floor feature; and (vi) the value of the Series 1 Preferred Shares to be received in exchange for the Preferred Shares.
- The Arrangement is expected to provide an immediate increase in dividends as compared to the Preferred Shares, and the Series 1 Preferred Shares are expected to receive higher dividends over the next five years, assuming current interest rate levels.
- The proposed exchange ratios provide an increased dividend for all series of Preferred Shares assuming they would reset at current interest rate levels over the next five years.

- The proposed exchange ratios were also considered and evaluated by the Fairness Advisor and upon completion of such evaluation the Fairness Advisor issued its Fairness Opinion and concluded that the proposed exchange of Preferred Shares in accordance with the Arrangement is fair, from a financial point of view, to the holders of each series of Preferred Shares.

10. Why was a constant premium not applied to each series of Preferred Shares?

- A constant premium was not applied across all series of Preferred Shares as this would result in select series of Preferred Shares receiving an increase in dividends and others series of Preferred Shares receiving lesser dividends, as a result of the different attributes and trading values for each such series of Preferred Shares.
- If TransAlta were to apply such an approach, it would be difficult to achieve fairness across each series of Preferred Shares.
- Accordingly, the applicable exchange ratio was calculated and tailored to each series of Preferred Shares on an individual basis.

See "*The Arrangement – Reasons for the Arrangement – Implied Offer Premia Ranges from 11% to 17%*" in this Information Circular.

11. Did TransAlta take the forward curve into account when setting the exchange ratios?

- TransAlta evaluated a number of outlook scenarios in determining the exchange ratios, including (i) the forward curve, which, historically has not been an accurate predictor of interest rates in either Canada or the United States, (ii) a flat curve and (iii) a softening in the curve given recent events and commentary by the Bank of Canada.

12. Am I better off to hold my current Preferred Shares?

- TransAlta believes that Preferred Shareholders are better off exchanging their current series of Preferred Shares for Series 1 Preferred Shares given (i) the downside protection from the minimum floor feature; (ii) the 6.50% dividend rate of the Series 1 Preferred Shares; (iii) the immediate increase in dividends as compared to the Preferred Shares; (iv) the enhanced trading liquidity expected for the Series 1 Preferred Shares and (v) the tax flexibility for Preferred Shareholders in connection with the Arrangement and given the benefits to the Corporation including (i) a reduction in the carrying value associated with the Preferred Shares on the Corporation's balance sheet, which in turn improves some rating agency credit ratios; (ii) an improvement in the liquidity and underlying features of the series 1 Preferred Shares which TransAlta anticipates will improve the trading yield; and (iii) future preferred share issuance capacity.

See "*The Arrangement – Reasons for the Arrangement*" in this Information Circular.

13. The Series 1 Preferred Shares provide a minimum floor feature and a new dividend rate. Are there other differences as compared to the current Preferred Shares?

- Series 1 Preferred Shares will have the benefits outlined above including the minimum floor feature (the Series 2 Preferred Shares do not have a minimum floor feature) and a dividend rate of 6.50%. The other features of the Series 1 Preferred Shares will be equivalent to the current Preferred Shares, including resetting the dividend rate every five years and having the option to select a floating rate security (available with the Series 2 Preferred Shares) at each reset period (the initial reset period to be on December 31, 2021).

- The dividend rate in respect of any Series 2 Preferred Shares will reset quarterly. In each case, the new dividend rate is unlikely to be the same as, and may be lower than, the dividend rate for the applicable preceding dividend period.
- The Floating Quarterly Dividend Rate is the annual rate of interest (expressed as a percentage rounded to the nearest one hundred thousandth of one percent (with 0.000005% being rounded up)) equal to the sum of the T-Bill Rate on the applicable Floating Rate Calculation Date and 5.29%.

See "*The Arrangement – Rights, Privileges, Restrictions and Conditions Attaching to the New Preferred Shares*" in this Information Circular.

Value

14. Is there any value in the minimum floor? Particularly given the forward curve?

- TransAlta believes significant value can be ascribed to the minimum floor for a number of reasons including, but not limited to, the following:
 - (a) based on the Government of Canada Yield of 1.21% at the time the Arrangement was announced, the Arrangement offers significantly more downside protection to a decline in the Government of Canada Yield than all other minimum floor rate reset preferred shares issued on the TSX since September 2015. The average Government of Canada Yield for such previous issuances of rate reset preferred shares with a minimum floor feature on the TSX is approximately 0.78%, resulting in a floor value for the Government of Canada Yield that is approximately 43 basis points higher for the Series 1 Preferred Shares compared to prior issuances; and
 - (b) over the past few years, many Canadian listed companies, including companies in the Corporation's peer group, have issued rate reset preferred shares with and without a minimum floor feature. The preferred share issuances without a minimum floor feature have demonstrated higher return requirements relative to preferred share issuances with a minimum floor feature issued from the same issuer.

See "*The Arrangement – Reasons for the Arrangement – Minimum Floor Feature Reduces Dividend Volatility*" in this Information Circular.

15. Will the Series 1 Preferred Shares trade above \$25.00 per share?

- The Corporation expects that the Series 1 Preferred Shares will trade closer to their Issue Price of \$25.00, given the initial dividend rate attributable to the Series 1 Preferred Shares, the minimum floor feature, the redemption price and the improved credit profile of TransAlta upon completion of the Arrangement.

16. Does this transaction limit my upside in share price value for Series 1 Preferred Shares? Also, does this transaction take away the capital appreciation for the Preferred Shares I currently hold?

- Preferred shares that have a redemption feature allow issuers of such preferred shares to call the preferred shares at a pre-determined price at each reset date and this limits the potential price appreciation upside for such preferred shares, including the Series 1 Preferred Shares.
- However, it is possible that the Series 1 Preferred Shares will trade above \$25.00 as several other series of rate reset preferred shares issued by other issuers with a minimum floor feature are currently trading at or above \$25.00.

- The Corporation believes that the beneficial features of the Series 1 Preferred Shares provide immediate and tangible benefits including the downside protection from the minimum floor feature and higher immediate and expected dividends under current interest rates, which will be favoured relative to the uncertainty associated with potential price volatility of the existing Preferred Shares.

See "*The Arrangement – Rights, Privileges, Restrictions and Conditions Attaching to the New Preferred Shares*" in this Information Circular.

17. Will TransAlta just call the Series 1 Preferred Shares at the next reset date if they are trading above \$25.00 per share?

- TransAlta does not currently have any intention to call outstanding Preferred Shares. Decisions on calling Preferred Shares at the next reset date will be dependent on a number of variables including TransAlta's funding requirements and access to capital markets, in addition to the then current trading price of the Series 1 Preferred Shares.
- The equity attributable to the Preferred Shares is viewed as an integral part of the Corporation's capital structure and supports TransAlta's current credit ratings.

18. How did the Fairness Advisor come to the conclusion that the Arrangement is fair, from a financial point of view, to the holders of each series of Preferred Shares?

- The Fairness Advisor conducted a rigorous review of the Arrangement and evaluated a number of quantitative and qualitative considerations comparing each existing series of Preferred Shares to the Series 1 Preferred Shares under a number of potential market outlook scenarios including shorter-term and longer-term perspectives. There were significant alternative scenarios evaluated for each series of Preferred Shares and ultimately the exchange ratios and the premiums offered to the holders of each series of Preferred Shares were adjusted to ensure that the proposed exchange of Preferred Shares in accordance with the Arrangement is fair, from a financial point of view, to each series of Preferred Shares, taking into account the wide range of quantitative and qualitative considerations that the Fairness Advisor evaluated.

See the Fairness Opinion attached as Appendix "G" to this Information Circular.

Tax

19. How is the exchange treated for Canadian federal income tax purposes?

- The exchange of Preferred Shares for Series 1 Preferred Shares will generally be tax-deferred for Preferred Shareholders for Canadian federal income tax purposes.
- However, Preferred Shareholders are being provided with the option to elect by filing with the Depositary the Election Form prior to the Election Deadline to effect the exchange in such a manner that may allow such Preferred Shareholders to realize a capital gain or a capital loss for Canadian federal income tax purposes.

See "*Certain Canadian Federal Income Tax Considerations – Exchange of Preferred Shares for New Preferred Shares*" in this Information Circular.

20. Why would I elect to realize capital gains or capital losses? How does this work?

- Preferred Shareholders may elect to realize capital gains or capital losses in order to align with their personal tax planning.

- Registered Preferred Shareholders who wish to exchange their Preferred Shares in a way that may allow such registered Preferred Shareholders to realize a capital gain or a capital loss for Canadian federal income tax purposes may do so by completing and submitting the Election Form with the Depository on or before the Election Deadline in accordance with the instructions on the Election Form. In the event a registered Preferred Shareholder does not submit an Election Form with the Depository prior to the Election Deadline, such registered Preferred Shareholder will receive his, her or its Series 1 Preferred Shares on a tax-deferred basis for Canadian federal income tax purposes.
- Preferred Shareholders should consult with their own tax, accounting and/or financial advisor to determine whether this election would be beneficial based on each Preferred Shareholder's unique circumstances.
- TransAlta in no way expresses an opinion as to whether a Preferred Shareholder should or should not file an Election Form.

See "*Certain Canadian Federal Income Tax Considerations – Taxation of Capital Gains and Capital Losses*" in this Information Circular.

21. If I have questions regarding the Arrangement, who do I contact?

- Questions and requests for assistance concerning how Preferred Shareholders can vote their Preferred Shares or the exchange of their Preferred Shares for Series 1 Preferred Shares may be directed to the Depository (CST Trust Company) at 1-800-387-0825 toll free in North America, or at 1-416-682-3860 outside of North America, or by e-mail at inquiries@canstockta.com, and questions with respect to the Arrangement may be directed to the Solicitation Agent (Kingsdale Advisors) at 1-877-659-1820 toll free in North America, or at 1-416-867-2272 outside of North America, or by e-mail at contactus@kingsdaleadvisors.com.