ORMAT TECHNOLOGIES, INC.
Form 10-Q
May 06, 2016

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2016

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number: 001-32347

ORMAT TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**88-0326081**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification Number)*
6225 Neil Road, Reno, Nevada	**89511-1136**
(Address of principal executive offices)	*(Zip Code)*

(775) 356-9029

(Registrant’s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company
	(Do not check if a smaller reporting company)		

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: As of May 4, 2016, the number of outstanding shares of common stock, par value $0.001 per share, was 49,390,335.

ORMAT TECHNOLOGIES, INC.

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2016

PART I — FINANCIAL INFORMATION

Certain Definitions

Unless the context otherwise requires, all references in this quarterly report to "Ormat", "the Company", "we", "us", "our company", "Ormat Technologies" or "our" refer to Ormat Technologies, Inc. and its consolidated subsidiaries.

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PART I - FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2016	December 31, 2015
	(Dollars in thousands)	
ASSETS		
Current assets:		
Cash and cash equivalents	$148,498	$185,919
Restricted cash and cash equivalents (all related to VIEs)	64,129	49,503
Receivables:		
Trade	76,465	55,301
Other	8,646	7,885
Inventories	16,795	18,074
Costs and estimated earnings in excess of billings on uncompleted contracts	29,897	25,120
Prepaid expenses and other	35,135	33,334
Total current assets	379,565	375,136
Deposits and other	17,415	17,968
Deferred charges	42,613	42,811
Property, plant and equipment, net ($1,514,726 and $1,481,258 related to VIEs, respectively)	1,570,074	1,559,335
Construction-in-process ($64,668 and $129,165 related to VIEs, respectively)	220,981	248,835
Deferred financing and lease costs, net	4,430	4,022
Intangible assets, net	25,056	25,875
Total assets	$2,260,134	$2,273,982
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$82,487	$91,955
Short term revolving credit lines with banks (full recourse)	9,000	—
Billings in excess of costs and estimated earnings on uncompleted contracts	30,917	33,892
Current portion of long-term debt:		
Limited and non-recourse (all related to VIEs):		
Senior secured notes	29,917	29,930
Other loans	21,495	21,495
Full recourse	11,229	11,229
Total current liabilities	185,045	188,501
Long-term debt, net of current portion:		
Limited and non-recourse (all related to VIEs):		
Senior secured notes (less deferred financing costs of $10,549 and $10,852, respectively)	290,201	294,476
Other loans (less deferred financing costs of $7,137 and $7,492, respectively)	270,869	275,888
Full recourse:		
Senior unsecured bonds (plus unamortized premium based upon 7% of $436 and $513, respectively and less deferred financing costs of $239 and $283, respectively)	249,665	249,698

Other loans (less deferred financing costs of $420 and $435, respectively)	17,036	18,687
Accumulated losses of unconsolidated company in excess of investment	12,216	8,100
Liability associated with sale of tax benefits	6,714	11,665
Deferred lease income	57,516	58,099
Deferred income taxes	16,502	32,654
Liability for unrecognized tax benefits	10,639	10,385
Liabilities for severance pay	19,118	19,323
Asset retirement obligation	21,262	20,856
Other long-term liabilities	5,018	1,776
Total liabilities	1,161,801	1,190,108
Commitments and contingencies (Note 10)		
Equity:		
The Company's stockholders' equity:		
Common stock, par value $0.001 per share; 200,000,000 shares authorized; 49,320,335 and 49,107,901 shares issued and outstanding as of March 31, 2016 and December 31, 2015, respectively	49	49
Additional paid-in capital	854,260	849,223
Retained earnings	162,195	148,396
Accumulated other comprehensive income	(10,849)	(7,667)
	1,005,655	990,001
Noncontrolling interest	92,678	93,873
Total equity	1,098,333	1,083,874
Total liabilities and equity	$2,260,134	$2,273,982

The accompanying notes are an integral part of the consolidated financial statements.

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ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended March 31,	
	2016	2015
	(Dollars in thousands, except per share data)	
Revenues:		
Electricity	$107,868	$89,953
Product	43,726	30,278
Total revenues	151,594	120,231
Cost of revenues:		
Electricity	63,686	55,581
Product	24,035	20,625
Total cost of revenues	87,721	76,206
Gross margin	63,873	44,025
Operating expenses:		
Research and development expenses	349	363
Selling and marketing expenses	3,675	3,433
General and administrative expenses	8,749	10,204
Write-off of unsuccessful exploration activities	557	174
Operating income	50,543	29,851
Other income (expense):		
Interest income	320	9
Interest expense, net	(16,023)	(17,828)
Foreign currency translation and transaction gains (losses)	1,962	(1,366)
Income attributable to sale of tax benefits	4,398	5,552
Other non-operating income (expense), net	191	283
and equity in losses of investees	41,391	16,501
Income tax (provision) benefit	(9,509)	(5,459)
Equity in losses of investees, net	(937)	(775)
Income from continuing operations	30,945	10,267
Net income attributable to noncontrolling interest	(1,674)	(235)

Net income attributable to the Company's stockholders	$29,271	$10,032
Comprehensive income:		
Net income	30,945	10,267
Other comprehensive income (loss), net of related taxes:		
Change in unrealized gains or losses in respect of the Company's share in derivatives instruments of unconsolidated investment	(3,179)	(3,296)
Loss in respect of derivative instruments designated for cash flow hedge	21	23
Amortization of unrealized gains in respect of derivative instruments designated for cash flow hedge	(24)	(30)
Comprehensive income	27,763	6,964
Comprehensive income attributable to noncontrolling interest	(1,674)	(235)
Comprehensive income attributable to the Company's stockholders	$26,089	$6,729
Earnings per share attributable to the Company's stockholders:		
Basic:		
Net income	$0.60	$0.21
Diluted:		
Net income	$0.59	$0.21
Weighted average number of shares used in computation of earnings per share attributable to the Company's stockholders:		
Basic	49,173	47,244
Diluted	49,782	48,079
Dividend per share declared	$0.31	$0.08

The accompanying notes are an integral part of the consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited)

	The Company's Stockholders' Equity							
	Common Stock Shares	Amount	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Accumulated Other Income (Loss)	Total	Noncontrolling Interest	Total Equity
	(Dollars in thousands, except per share data)							
Balance at December 31, 2014	45,537	$ 46	$ 742,006	$ 41,539	$ (8,668)	$ 774,923	$ 11,823	$ 786,746
Stock-based compensation	—	—	1,127	—	—	1,127	—	1,127
Exercise of options by employees and directors	295	—	2,704	—	—	2,704	—	2,704
Share exchange with Parent	2,996	3	25,754	—	—	25,757	—	25,757
Cash paid to non controlling interest	—	—	—	—	—	—	(228)	(228)
Cash dividend declared, $0.08 per share	—	—	—	(3,898)	—	(3,898)	—	(3,898)
Net income	—	—	—	10,032	—	10,032	235	10,267
Other comprehensive income (loss), net of related taxes:								
cash flow hedge (net of related tax of $14)	—	—	—	—	23	23	—	23
Change in unrealized gains or losses in respect of the Company's share in derivative instruments of unconsolidated investment (net of related tax of $0)	—	—	—	—	(3,296)	(3,296)	—	(3,296)
Amortization of unrealized gains in respect of derivative instruments designated for cash	—	—	—	—	(30)	(30)	—	(30)

flow hedge (net of related tax of $19)								
Balance at March 31, 2015	48,828	$ 49	$ 771,591	$ 47,673	$ (11,971)	$ 807,342	$ 11,830	$ 819,172
Balance at December 31, 2015	49,107	$ 49	$ 849,223	$ 148,396	$ (7,667)	$ 990,001	$ 93,873	$ 1,083,874
Stock-based compensation	—	—	842	—	—	842	—	842
Exercise of options by employees and directors	213	—	4,195	—	—	4,195	—	4,195
Cash paid to noncontrolling interest	—	—	—	—	—	—	(2,869)	(2,869)
Cash dividend declared, $0.31 per share	—	—	—	(15,472)	—	(15,472)	—	(15,472)
Net income	—	—	—	29,271	—	29,271	1,674	30,945
Other comprehensive income (loss), net of related taxes:								
Loss in respect of derivative instruments designated for cash flow hedge (net of related tax of $12)	—	—	—	—	21	21	—	21
Change in unrealized gains or losses in respect of the Company's share in derivative instruments of unconsolidated investment (net of related tax of $0)	—	—	—	—	(3,179)	(3,179)	—	(3,179)
Amortization of unrealized gains in respect of derivative instruments designated for cash flow hedge (net of related tax of $14)	—	—	—	—	(24)	(24)	—	(24)
Balance at March 31, 2016	49,320	$ 49	$ 854,260	$ 162,195	$ (10,849)	$ 1,005,655	$ 92,678	$ 1,098,333

The accompanying notes are an integral part of the consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended March 31,	
	2016	2015
	(Dollars in thousands)	
Cash flows from operating activities:		
Net income	$30,945	$10,267
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	26,181	25,639
Amortization of premium from senior unsecured bonds	(77)	(77)
Accretion of asset retirement obligation	406	372
Stock-based compensation	842	1,127
Amortization of deferred lease income	(671)	(671)
Income attributable to sale of tax benefits, net of interest expense	(3,475)	(4,044)
Equity in losses of investees	937	775
Mark-to-market of derivative instruments	(162)	4,129
Write-off of unsuccessful exploration activities	557	174
Gain on severance pay fund asset	(564)	140
Deferred income tax provision	6,643	4,054
Liability for unrecognized tax benefits	254	(321)
Deferred lease revenues	88	(74)
Changes in operating assets and liabilities, net of amounts acquired:		
Receivables	(21,925)	(6,201)
Costs and estimated earnings in excess of billings on uncompleted contracts	(4,777)	20,367
Inventories	1,279	(356)
Prepaid expenses and other	(1,808)	1,189
Deposits and other	80	(79)
Accounts payable and accrued expenses	(4,846)	(4,903)
Billings in excess of costs and estimated earnings on uncompleted contracts	(2,975)	33,137
Liabilities for severance pay	(205)	(1,900)
Other long-term liabilities	317	916
Due from/to Parent	—	(513)
Net cash provided by operating activities	27,044	83,147
Cash flows from investing activities:		
Cash acquired in organizational restructuring and share exchange with parent (Note 1)	—	15,391
Net change in restricted cash, cash equivalents and marketable securities	(14,626)	(22,282)
Capital expenditures	(31,031)	(42,386)
Decrease in severance pay fund asset, net of payments made to retired employees	1,037	2,020
Net cash used in investing activities	(44,620)	(47,257)
Cash flows from financing activities:		
Proceeds from exercise of options by employees	4,195	2,704
Proceeds from revolving credit lines with banks	49,700	489,900
Repayment of revolving credit lines with banks	(40,700)	(479,600)

Cash received from non-controlling interest	1,972	1,654
Repayments of long-term debt	(11,631)	(10,494)
Cash paid to non-controlling interest	(6,317)	(3,503)
Deferred debt issuance costs	(1,592)	(2,159)
Cash dividends paid	(15,472)	(3,898)
Net cash provided by (used in) financing activities	(19,845)	(5,396)
Net change in cash and cash equivalents	(37,421)	30,494
Cash and cash equivalents at beginning of period	185,919	40,230
Cash and cash equivalents at end of period	$148,498	$70,724
Supplemental non-cash investing and financing activities:		
Increase (decrease) in accounts payable related to purchases of property, plant and equipment	$(5,296)	$(118)
Accrued liabilities related to financing activities	$3,768	$—

The accompanying notes are an integral part of the consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 — GENERAL AND BASIS OF PRESENTATION

These unaudited condensed consolidated interim financial statements of Ormat Technologies, Inc. and its subsidiaries (collectively, the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. Accordingly, they do not contain all information and notes required by U.S. GAAP for annual financial statements. In the opinion of management, these unaudited condensed consolidated interim financial statements reflect all adjustments, which include normal recurring adjustments, necessary for a fair statement of the Company’s consolidated financial position as of March 31, 2016, the consolidated results of operations and comprehensive income (loss) for the three-month periods ended March 31, 2016 and 2015 and the consolidated cash flows for the three-month periods ended March 31, 2016 and 2015.

The financial data and other information disclosed in the notes to the condensed consolidated financial statements related to these periods are unaudited. The results for the three-month period ended March 31, 2016 are not necessarily indicative of the results to be expected for the year ending December 31, 2016.

These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2015. The condensed consolidated balance sheet data as of December 31, 2015 was derived from the audited consolidated financial statements for the year ended December 31, 2015, but does not include all disclosures required by U.S. GAAP.

Dollar amounts, except per share data, in the notes to these financial statements are rounded to the closest $1,000.

Guadeloupe power plant transaction

On March 14, 2016, the Company signed an Investment Agreement and Shareholders Agreement with Sageos holding (“Sageos”), a wholly owned subsidiary of Bureau de Recherches Géologiques et Minières (“BRGM”), the French governmental geological survey company, to acquire, gradually, 85% of Geothermie Bouillante SA (“GB”). GB owns and operates the Bouillante geothermal power plant located on Guadeloupe Island, a French territory in the Caribbean. This plant currently generates approximately 10 MW and owns two exploration licenses providing for additional potential capacity of up to 30 MW. Under the agreements, the Company will pay approximately $24 million (linked to the US Dollar-Euro exchange rate) to Sageos for a 79.6% equity interest in GB at closing, which is expected in the second quarter of 2016. In addition, the Company is committed to further invest approximately $11 million (€10 million) during the first two years, which will increase its equity interest to 85%. The cash will be used mainly for the enhancement of the power plant. Under the Investment Agreement, the Company will pay Sageos an additional amount of up to approximately $17 million (€16 million) subject to the achievement of agreed upon production thresholds and capacity expansion within a defined time period.

Alevo transaction

On March 30, 2016, the Company signed an agreement with a subsidiary of Alevo Group SA (“Alevo”), a leading provider of energy storage systems, to jointly build, own and operate the Rabbit Hill Energy Storage Project (“Rabbit Hill”) located in Georgetown, Texas. The Company will own and fund the majority of Rabbit Hill and under the terms of the agreements, will provide engineering and construction services and balance of plant equipment. Alevo will provide its innovative GridBank™ inorganic lithium ion energy storage system in conjunction with the power conversion systems. In addition, Alevo will provide ongoing management and operations and maintenance services for the life of the project. The Company will hold an 85% interest in the Rabbit Hill project entity which will decrease to 50.1% subsequent to reaching certain IRR achievements. The Company will consolidate the Rabbit Hill project as a majority owned indirect subsidiary.

Northleaf Transaction

On April 30, 2015, Ormat Nevada Inc. (“Ormat Nevada”), a wholly-owned subsidiary of the Company, closed the sale of approximately 36.75% of the aggregate membership interests in ORPD LLC (“ORPD”), a new holding company and subsidiary of Ormat Nevada, that indirectly owns the Puna geothermal power plant in Hawaii, the Don A. Campbell geothermal power plant in Nevada, and nine power plant units across three recovered energy generation assets known as OREG 1, OREG 2 and OREG 3 to Northleaf Geothermal Holdings, LLC.

Under the agreement with Northleaf, we are currently conducting the required power generation tests to determine the final capacity attributable to the second phase of Don A. Campbell and upon Ormat Nevada's contribution of the project to ORPD, Northleaf will pay the value equivalent to their interest share in ORPD. We estimate that Ormat Nevada will receive approximately $40 million cash for the sale of the second phase of Don Campbell expected in the second quarter of 2016.

Other comprehensive income

For the three months ended March 31, 2016 and 2015, the Company classified $3,000 and $7,000, respectively, from accumulated other comprehensive income, of which $4,000 and $12,000, respectively, were recorded to reduce interest expense and $1,000 and $5,000, respectively, were recorded against the income tax provision, in the condensed consolidated statements of operations and comprehensive income. The accumulated net loss included in Other comprehensive income as of March 31, 2016 is $581,000.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Write-off of unsuccessful exploration activities

Write-off of unsuccessful exploration activities for the three months ended March 31, 2016 and 2015 was $0.6 million and $0.2 million, respectively. These write-offs of exploration costs are related to the Company's exploration activities in Nevada, which the Company determined in the first quarter of 2016 would not support commercial operations.

Concentration of credit risk

Financial instruments that potentially subject the Company to a concentration of credit risk consist principally of temporary cash investments and accounts receivable.

The Company places its temporary cash investments with high credit quality financial institutions located in the United States ("U.S.") and in foreign countries. At March 31, 2016 and December 31, 2015, the Company had deposits totaling $21,548,000 and $18,992,000, respectively, in seven U.S. financial institutions that were federally insured up to $250,000 per account. At March 31, 2016 and December 31, 2015, the Company's deposits in foreign countries amounted to approximately $144,257,000 and $181,000,000, respectively.

At March 31, 2016 and December 31, 2015, accounts receivable related to operations in foreign countries amounted to approximately $46,192,000 and $27,846,000, respectively. At March 31, 2016 and December 31, 2015, accounts receivable from the Company's primary customers amounted to approximately 72% and 66%, respectively, of the Company's accounts receivable.

Sierra Pacific Power Company and Nevada Power Company (subsidiaries of NV Energy, Inc.) accounted for 23.2% and 24.0% for the three months ended March 31, 2016 and 2015, respectively.

Southern California Public Power Authority accounted for 12.1% and 5.9% for the three months ended March 31, 2016 and 2015, respectively.

Kenya Power and Lighting Co. Ltd. accounted for 17.4% and 17.8% for the three months ended March 31, 2016 and 2015, respectively.

The Company performs ongoing credit evaluations of its customers' financial condition. The Company has historically been able to collect on all of its receivable balances, and accordingly, no provision for doubtful accounts has been made.

NOTE 2 — NEW ACCOUNTING PRONOUNCEMENTS

New accounting pronouncements effective in the three-month period ended March 31, 2016

Amendments to Fair Value Measurement

In June 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-10, Amendment to Fair Value Measurement, Subtopic 820-10. The amendment provides that the reporting entity shall disclose for each class of assets and liabilities measured at fair value in the statement of financial position the following information: for recurring fair value measurements, the fair value measurement at the end of the reporting period, and for non-recurring fair value measurement, the fair value measurement at the relevant measurement date and the reason for the measurement. The amendments in this update are effective for annual reporting periods beginning after December 15, 2015, including interim periods within those reporting periods. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

Amendments to the Consolidation Analysis

In February 2015, the FASB issued ASU 2015-02, Amendments to the Consolidation Analysis, Topic 810. The update provides that all reporting entities that hold a variable interest in other legal entities will need to re-evaluate their consolidation conclusions and potentially revise their disclosures. This amendment affects both variable interest entity ("VIE") and voting interest entity ("VOE") consolidation models. The update does not change the general order in which the consolidation models are applied. A reporting entity that holds an economic interest in, or is otherwise involved with, another legal entity (i.e. has a variable interest) should first determine if the VIE model applies, and if so, whether it holds a controlling financial interest under that model. If the entity being evaluated for consolidation is not a VIE, then the VOE model should be applied to determine whether the entity should be consolidated by the reporting entity. Since consolidation is only assessed for legal entities, the determination of whether there is a legal entity is important. It is often clear when the entity is incorporated, but unincorporated structures can also be legal entities and judgment may be required to make that determination. The update contains a new example that highlights the discretion used to make this legal entity determination. The update is effective for annual reporting periods beginning after December 15, 2015, including interim periods within those reporting periods. The adoption of this guidance did not have a material impact on the Company’s consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Simplifying the Presentation of Debt Costs

In August 2015, the FASB issued ASU 2015-15, Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, Subtopic 835-30. The update clarifies that given the absence of authoritative guidance within Update 2015-03 for debt issuance costs described below, debt issuance costs related to line-of-credit arrangements can be deferred and presented as assets and subsequently amortized ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings under the line-of-credit arrangement. The amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company adopted this update in its interim period beginning January 1, 2016 and continues to present debt issuance costs related to such line-of-credit arrangements as assets amortized ratably over the respective term of the line-of credit arrangements. Debt issuance costs related to such line-of-credit arrangements as of March 31, 2016 and December 31, 2015, totaled $1.7 million and $1.0 million, respectively.

In April 2015, the FASB issued ASU 2015-03, Interest-Imputation of Interest: Simplifying the Presentation of Debt Costs, Subtopic 835-30. The update provides that debt issuance costs related to a recognized debt liability be presented in the balance sheet as direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company retrospectively adopted this update in its interim period beginning January 1, 2016. The impact of the adoption resulted in a reclassification of debt issuance costs totaling $18.3 million and $19.1 million as of March 31, 2016 and December 31, 2015, respectively.

New accounting pronouncements effective in future periods

Improvement to Employee Share-Based Payment Accounting

In March 2016, the FASB issued ASU 2016-09, Improvement to Employee Share-Based Payment Accounting, an update to the guidance on stock-based compensation. Under the new guidance, all excess tax benefits and tax deficiencies will be recognized in the income statement as they occur. This will replace the current guidance, which requires tax benefits that exceed compensation cost (windfalls) to be recognized in equity. It will also eliminate the need to maintain a “windfall pool,” and will remove the requirement to delay recognizing a windfall until it reduces current taxes payable. The new guidance will also change the cash flow presentation of excess tax benefits, classifying them as operating inflows, consistent with other cash flows related to income taxes. Today, windfalls are classified as financing activities. Also, this will affect the dilutive effects in earnings per share, as there will no longer be excess tax benefits recognized in additional paid in capital. Today those excess tax benefits are included in assumed proceeds from applying the treasury stock method when computing diluted EPS. Under the amended guidance, companies will be able to make an accounting policy election to either (1) continue to estimate forfeitures or (2) account for forfeitures as they occur. This updated guidance is effective for annual and interim periods beginning after December 15, 2016. Early adoption is permitted. The Company is currently evaluating the potential impact, if any, of the adoption of this update on its consolidated financial statements.

Revenues from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenues from Contracts with Customers, Topic 606 (“Topic 606”), which was a joint project of the FASB and the International Accounting Standards Board to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and International Financial Reporting Standards. The update provides that an entity should recognize revenue in connection with the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, an entity is required to apply each of the following steps: (1) identify the contract(s) with the customer; (2) identify the performance obligations in the contracts; (3) determine the transaction price; (4) allocate the transaction price to the performance obligation in the contract; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. The amendments in this update are effective for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. Early adoption is permitted no earlier than 2017 for calendar fiscal year entities. The Company is currently evaluating the potential impact, if any, of the adoption of these amendments on its consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

In March 2016, the FASB issued ASU 2016-08, Principal versus Agent Considerations. The amendment in this Update do not change the core principal of the guidance and are intended to improve the operability and understandability of the implementation guidance on principal versus agent considerations. When another entity is involved in providing goods or services to a customer, an entity is required to determine if the nature of its promise is to provide the specific good or service itself (that is, the entity is a principal) or to arrange for that good or service to be provided by the other party (that is, the entity is an agent). The guidance includes indicators to assist an entity in determining whether it acts as a principal or agent in a specified transaction. The amendments in this update are effective for annual reporting periods beginning after December 15, 2017, including interim periods within those reporting periods. Early adoption is permitted no earlier than 2017 for calendar fiscal year entities. The Company is currently evaluating the potential impact, if any, of the adoption of these amendments on its consolidated financial statements.

Leases

In February 2016, the FASB issued ASU 2016-02, Leases, Topic 842. The amendment in this Update introduce a number of changes and simplifications from previous guidance, primarily the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases. The Update retains the distinction between finance leases and operating leases and the classification criteria between the two types remain substantially similar. Also, lessor accounting remains largely unchanged from previous guidance, however, key aspects in the Update were aligned with the revenue recognition guidance in Topic 606. Additionally, the Update defines a lease as a contract, or part of a contract, that conveys the right to control the use of identified asset for a period of time in exchange for considerations. Control over the use of the identified means that the customer has both (a) the right to obtain substantially all of the economic benefits from the use of the asset and (b) the right to direct the use of the asset. The amendments in this update are effective for annual reporting periods beginning after December 15, 2018, including interim periods within those reporting periods. Early adoption is permitted. The Company is currently evaluating the potential impact, if any, of the adoption of these amendments on its consolidated financial statements.

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities. The update primarily requires that an entity should present separately, in other comprehensive income, the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk if the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. The application of this update should be by means of cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The amendments in this update are effective for financial statements issued for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted as of the beginning of the fiscal year of adoption. The Company is currently evaluating the potential impact, if any, of the adoption of this update on its consolidated financial statements.

Simplifying the Measurement of Inventory

In July 2015, the FASB issued ASU 2015-11, Simplifying the Measurement of Inventory, Topic 330. The update contains no amendments to disclosure requirements, but replaces the concept of ‘lower of cost or market’ with that of ‘lower of cost and net realizable value’. The amendments in this update are effective for annual reporting periods beginning after December 15, 2016, including interim periods within those reporting periods. The amendments should be applied prospectively with early adoption permitted. The Company is currently evaluating the potential impact, if any, of the adoption of this update on its consolidated financial statements.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

NOTE 3 — INVENTORIES

Inventories consist of the following:

	March 31, 2016	December 31, 2015
	(Dollars in thousands)	
Raw materials and purchased parts for assembly	$3,604	$ 8,819
Self-manufactured assembly parts and finished products	13,191	9,255
Total	$16,795	$ 18,074

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(Unaudited)

NOTE 4 — UNCONSOLIDATED INVESTMENTS

Unconsolidated investments consist of the following:

	March 31, 2016	December 31, 2015
	(Dollars in thousands)	
Sarulla	$(12,216)	$ (8,100)

The Sarulla Project

The Company holds a 12.75% equity interest in a consortium which is in the process of developing the Sarulla geothermal power project in Indonesia with expected generating capacity of approximately 330 megawatts ("MW"). The Sarulla project is located in Tapanuli Utara, North Sumatra, Indonesia and will be owned and operated by the consortium members under the framework of a Joint Operating Contract ("JOC") and Energy Sales Contract ("ESC") that were signed on April 4, 2013. Under the JOC, PT Pertamina Geothermal Energy ("PGE"), the concession holder for the project, has provided the consortium with the right to use the geothermal field, and under the ESC, PT PLN, the state electric utility, will be the off-taker at Sarulla for a period of 30 years. In addition to its equity holdings in the consortium, the Company designed the Sarulla plant and will supply its Ormat Energy Converters ("OECs") to the power plant, as further described below.

The project will be constructed in three phases of approximately 110 MW each, utilizing both steam and brine extracted from the geothermal field to increase the power plant's efficiency. The first phase of operations is expected to commence towards the end of 2016 and the remaining two phases of operations are scheduled to commence within 18 months thereafter. Engineering and procurement for the first and second phases has been substantially completed but is still in progress for the third phase. Construction for the first phase is in progress with major activities related to mechanical and electrical equipment installation. The infrastructure work for the second phase is in progress. Major equipment, including Ormat's OECs and Toshiba's steam turbine, for the first phase has arrived and is currently being installed. The drilling of production and injection wells is also in progress for all three phases. The project is still experiencing delays mainly in field development, but also in the plant's construction work. The project has missed a few milestones, but has received waivers from the lenders. The project is also facing certain cost overruns resulting from delays and excess drilling costs. Although estimated cost at completion is still within the approved budget (including the contingent equity), the lenders have requested that the sponsors commit additional equity. The sponsors have agreed and financing documents are being revised to reflect this request. With respect to Ormat's role as a supplier, all contractual milestones under the supply agreement were achieved and the main shipment of the second phase is on its way to the Indonesian port. Manufacturing of third phase equipment is progressing as planned.

On May 16, 2014, the consortium closed $1.17 billion in financing for the development of the Sarulla project with a consortium of lenders comprised of Japan Bank for International Cooperation ("JBIC"), the Asian Development Bank and six commercial banks and obtained construction and term loans on a limited recourse basis backed by a political risk guarantee from JBIC. Of the $1.17 billion, $0.1 billion (which was drawn down by the Sarulla project company on May 23, 2014) bears a fixed interest rate and $1.07 billion bears interest at a rate linked to LIBOR.

The Sarulla consortium entered into interest rate swap agreements with various international banks in order to fix the Libor interest rate on up to $0.96 billion of the $1.07 billion credit facility at a rate of 3.4565%. The interest rate swap became effective as of June 4, 2014 along with the second draw-down by the project company of $50.0 million.

The Sarulla project company accounted for the interest rate swap as a cash flow hedge upon which changes in the fair value of the hedging instrument, relative to the effective portion, will be recorded in other comprehensive income. As such, during the three months ended March 31, 2016, the project recorded a loss equal to $24.9 million, net of deferred tax of $12.8 million, of which the Company's share was $3.2 million, which was recorded in other comprehensive income. The related accumulated loss recorded by the Company as of March 31, 2016 is $10.3 million.

Pursuant to a supply agreement that was signed in October 2013, the Company is supplying its OECs to the power plant and has added the $255.6 million supply contract to its Product segment backlog. The Company started to recognize revenue from the project during the third quarter of 2014 and will continue to recognize revenue over the course of the next two years. The Company has eliminated the related intercompany profit of $7.6 million against equity in loss of investees.

During the three months ended March 31, 2016, the Company did not make any additional equity investments in the Sarulla project.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

NOTE 5— FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value measurement guidance clarifies that fair value is an exit price, representing the amount that would be received upon selling an asset or paid upon transferring a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. The guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under the fair value measurement guidance are described below:

Level 1 — Unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities;

Level 2 — Quoted prices in markets that are not active, or inputs that are observable, either directly or indirectly, for substantially the full term of the asset or liability;

Level 3 — Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (supported by little or no market activity).

The following table sets forth certain fair value information at March 31, 2016 and December 31, 2015 for financial assets and liabilities measured at fair value by level within the fair value hierarchy, as well as cost or amortized cost. As required by the fair value measurement guidance, assets and liabilities are classified in their entirety based on the lowest level of inputs that is significant to the fair value measurement.

March 31, 2016

	Carrying Value at March 31, 2016	Fair Value Total	Level 1	Level 2	Level 3
	(Dollars in thousands)				
Assets:					
Current assets:					
Cash equivalents (including restricted cash accounts)	$47,457	$47,457	$47,457	$—	$ —
Derivatives:					
Currency forward contracts [2]	1,759	1,759	—	1,759	—
Liabilities:					
Current liabilities:					
Derivatives:					
Call and put options on oil price [1]	$(1,612)	$(1,612)	$—	$(1,612)	$ —
Call option on natural gas price [1]	(1,196)	(1,196)	—	(1,196)	—
	$46,408	$46,408	$47,457	$(1,049)	$ —

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

	December 31, 2015				
		Fair Value			
	Carrying Value at December 31, 2015	**Total**	**Level 1**	**Level 2**	**Level 3**
	(Dollars in thousands)				
Assets					
Current assets:					
Cash equivalents (including restricted cash accounts)	$31,428	$31,428	$31,428	$—	$ —
Derivatives:					
Currency forward contracts [2]	7	7	—	7	—
Liabilities:					
Current liabilities:					
Derivatives:					
Currency forward contracts [2]	(169)	(169)	—	(169)	—
	$31,266	$31,266	$31,428	$(162)	$ —

(1) These amounts relate to call and put option transactions on oil and natural gas prices, valued primarily based on observable inputs, including spot prices for related commodity indices, and is included within "Accounts payable and accrued expenses" on March 31, 2016 in the consolidated balance sheets with the corresponding gain or loss being recognized within "Foreign currency translation and transaction losses" in the consolidated statement of operations and comprehensive income.

(2) These amounts relate to derivatives which represent currency forward contracts valued primarily based on observable inputs, including forward and spot prices for currencies, netted against contracted rates and then multiplied against notional amounts, and are included within "accounts payable and accrued expenses" on March 31, 2016 and December 31, 2015, in the consolidated balance sheet with the corresponding gain or loss being recognized within "Foreign currency translation and transaction gains (losses)" in the consolidated statement of operations and comprehensive income.

The amounts set forth in the tables above include investments in debt instruments and money market funds (which are included in cash equivalents). Those securities and deposits are classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices in an active market.

ORMAT TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

The following table presents the amounts of gain (loss) recognized in the consolidated statements of operations and comprehensive income on derivative instruments not designated as hedges:

Derivatives not designated as hedging instruments	**Location of recognized gain (loss)**	**Amount of recognized gain (loss) Three Months Ended March 31, 2016**	**2015**
Call options on natural gas price	Foreign currency translation and transaction losses	518	—
Call and put options on oil price	Foreign currency translation and transaction losses	(643)	—
Swap transactions on natural gas price	Electricity revenue	—	317
Currency forward contracts	Foreign currency translation and transaction gains (losses)	1,814	(1,251)
		$1,689	$(934)

On March 6, 2014, the Company entered into an Natural Gas Index (“NGI”) swap contract with a bank for notional quantity of approximately 2.2 million British Thermal Units (“MMbtu”) for settlement effective January 1, 2015 until March 31, 2015, in order to reduce its exposure to fluctuations in natural gas prices to below $4.95 per MMbtu under its power purchase agreements (“PPAs”) with Southern California Edison. The contract did not have any up-front costs. Under the terms of this contract, the Company made floating rate payments to the bank and receive fixed rate payments from the bank on each settlement date. The swap contract had monthly settlements whereby the difference between the fixed price of $4.95 per MMbtu and the market price on the first commodity business day on which the relevant commodity reference price is published in the relevant calculation period (January 1, 2015 to March 1, 2015) was settled on a cash basis.

On February 2, 2016, the Company entered into Henry Hub Natural Gas Future contracts under which it has written a number of call options covering a notional quantity of approximately 4.1 MMbtu with exercise prices of $2 and expiration dates effective February 24, 2016 until December 27, 2016 in order to reduce its exposure to fluctuations in natural gas prices under its PPAs with Southern California Edison. The Company received an aggregate premium of approximately $1.9 million from these call options. The call option contracts have monthly expiration dates at which the options can be called and the Company would have to settle its liability on a cash basis.

On February 24, 2016, the Company entered into Brent Oil Future contracts under which it has written a number of call options covering a notional quantity of approximately 185,000 barrels (“BBL”) of Brent with exercise prices of $32.75 to $35.5 and expiration dates effective March 24, 2016 until December 22, 2016 in order to reduce its exposure to fluctuations in Brent prices under its PPA with HELCO. The Company received an aggregate premium of approximately $1.1 million from these call options. The call option contracts have monthly expiration dates whereby the options can be called and the Company would have to settle its liability on a cash basis. Moreover, during March 2016, the Company rolled 2 existing call options covering a total notional quantity of 31,800 BBL of Brent in order to limit its exposure to $41.0 to $42.5 instead of $33.0 to $33.5. In addition, the Company entered into Short Risk Reversal transactions (sell call and buy put options) by rolling existing call options covering notional quantities of 16,500 BBL and 17,000 BBL in order to limit its exposure from the outstanding call options originally entered into in February, 2016 to a range of $28.5 to $37.5 and $28.0 to $38.5, respectively. The net cost from the additional transactions in March 2016 was $0.3 million.

The foregoing futures and swaps transactions were not designated as hedge transactions and are marked to market with the corresponding gains or losses recognized within “Foreign currency translation and transaction gains (losses)” and “Electricity revenues” in the consolidated statements of operations and comprehensive income, respectively. The Company recognized a net loss from these transactions of $0.1 million in the three months ended March 31, 2016 under foreign currency translation and transaction gains (losses), compared to a net gain of $0.3 million in the three months ended March 31, 2015 under Electricity revenues.

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(Unaudited)

There were no transfers of assets or liabilities between Level 1, Level 2 and Level 3 during the three months ended March 31, 2016.

The fair value of the Company's long-term debt approximates its carrying amount, except for the following:

	Fair Value		Carrying Amount	
	March 31, 2016	December 31, 2015	March 31, 2016	December 31, 2015
	(Dollars in millions)		(Dollars in millions)	
Olkaria III Loan - DEG	$24.5	$ 24.2	$23.7	$ 23.7
Olkaria III Loan - OPIC	262.7	262.6	260.1	264.6
Amatitlan Loan	40.7	41.7	39.4	40.3
Senior Secured Notes:				