

British Columbia Ferry Commission



Annual Report **for the Fiscal Year Ending March 31 2008**

*Prepared and submitted in accordance with
Section 53 of the Coastal Ferry Act
of the Province of British Columbia*

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July 21st 2008



To the Lieutenant Governor in Council

Comox, B.C.
July 21st 2008

May It Please Your Honour:

**BC Ferry Commission Annual Report
For the Fiscal Year Ending March 31 2008**

I am pleased to submit to you the fourth Annual Report of the BC Ferries Commissioner.

As required by section 53 of the Coastal Ferry Act, the Report sets out briefly all applications and requests for decisions to the commissioner under the Act, all orders issued by the commissioner, the financial statements applicable to the office of the commissioner for the above period along with full disclosure of the expenses of, and associated with, the office of the commissioner.

Yours truly,

A handwritten signature in black ink, appearing to read "M. Crilly".

Martin Crilly
BC Ferries Commissioner

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1 Highlights and Message from the Commissioner

This report covers the Commission's fifth year of operations under the Coastal Ferry Act. This is also the final year of the first performance term (PT1).

Price cap ruling for 2008 through 2012

Ferry fares were our prime focus during the year. In late 2007, we issued our final price cap decision for performance term two (PT2), which comprises the four years from April 2008 to March 2012.

Under our ruling fares may climb at up to twice the rate of general inflation on the major route group, and up to three times on the other "non major" route groups.¹ In making our decision we faced certain realities:

- BC Ferries is in a catch-up phase to renew its ships and terminals, as illustrated at year-end by the deployment of the first of three new, large double-ended vessels;
- underlying costs of ferry service are climbing due to general inflation in the cost of labour, fuel and maintenance;
- a backlog of extra fuel costs paid by BC Ferries (deferred with our agreement and not recovered by fuel surcharges by the end of PT1) are to be recovered from ferry customers in PT2; and
- on the 22 routes supported by taxpayer funding, government contributions are growing, but not as fast as BC Ferries' total revenue needs. Faster growth in fare revenue must bridge the gap between the growth rate of revenue needs and government contributions.

Fuel price rise after the 2007 price cap ruling

We made our price cap decision before we saw the exceptional rise in marine diesel fuel prices in 2008. For fiscal 2008/9, our ruling assumed an average price of \$0.78/litre. Now, in July 2008, the revised figure is 70% higher, at \$1.34/litre. Fuel accounted for 15% of BC Ferries total costs² in fiscal 2007/8.

¹ On April 1, 2008 caps rose by 7.3% on the three major routes and 4.0% on all other routes. Increases for April 1 2009, 2010 and 2011 are linked by formula to CPI inflation: for example, if inflation were 2% through 2011, the formula lifts caps each year by 3% on the major routes and 6.7% on others.

² Commission estimate based on BC Ferries data. Includes full fuel costs, i.e. includes deferred fuel costs; total costs are total of operating costs (including full fuel costs), amortization and interest expense plus a return on equity.

When making our price cap decision we knew that future fuel prices were highly uncertain. We included an automatic fuel surcharge/rebate mechanism as part of our ruling. It operates to pass through to fare payers some of the fuel costs/savings due to variations in fuel price from the forecast \$0.78/litre baseline. Since actual fuel prices this year have been so much higher, a fuel surcharge will likely be triggered.

Fuel conservation plan

In December 2005 we set a fuel conservation target for BC Ferries through March 2008—a reduction of 1% in fiscal 2006/07 and a further 1% percent in 2007/08—and required a fuel conservation plan.

In July 2007 BC Ferries proposed an upward-revised target for 2007/08. This recognized the extra fuel necessarily burned due to the urgent replacement of the Queen of the North by a higher-consumption vessel, the Northern Adventure. BC Ferries has reported that it has successfully met the 2% cumulative efficiency target, which was at 2.3 million litres for 2007/8, but from an adjusted baseline.³

Federal tax relief for commuters

Some ferry commuters may see relief through a Federal income tax credit. This reduces the effective cost of some ferry fares by 15%. We note BC Ferries' new stored value card (The Experience Card™) offered for 2008/9 gives customers access to a record of their ferry journey which may be used for claiming an income tax credit.

Overall contracted service level met

As in previous years, we tracked quarterly the number of sailings that BC Ferries delivered, the quality of the service and the fares charged. BC Ferries again **substantially met its contractual obligation to provide core services for vehicles and passengers.**

Overall, BC Ferries operated its core services reliably, while maintaining its capacity and service frequencies at or above the minimum requirements and charging fares within the controlled maximums.

Customer satisfaction

This was the fifth year of consistent tracking of customer satisfaction through a sampling survey undertaken by an outside firm. The latest survey found that, after making gains in many areas in 2006, satisfaction levels subsided or reached a plateau in 2007. The key reasons appear to be related to late departures, sailing frequency, and perceived value for money.

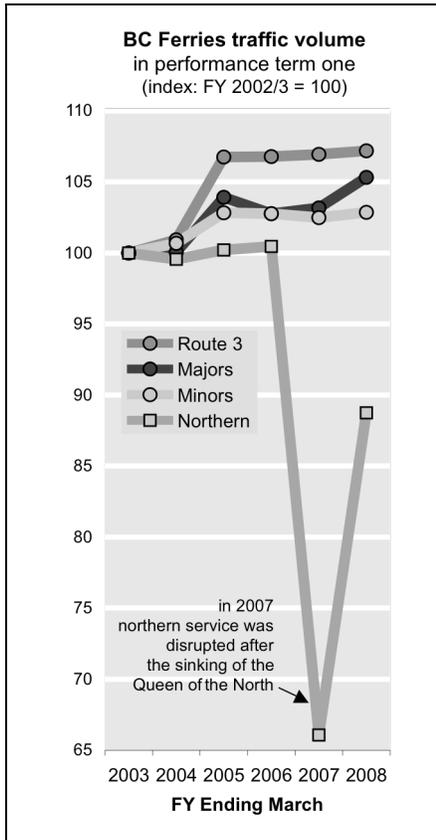
On-time performance

Punctuality⁴ remained high and strong on two of the major routes. This year on the third major route, Nanaimo-West Vancouver, though, it dropped noticeably, as it did on the Horseshoe Bay-Langdale route, due at least in part to heavy construction activity at terminals. On the 16 minor routes, notable improvements occurred across Jervis Inlet between Earl's Cove and Saltery Bay, between Tsawwassen and the Gulf Islands, and on the Hornby and Denman services. Deterioration was reported between Nanaimo and Gabriola Island, and on the Port McNeill-Alert Bay-Sointula runs.

³ The revised 2007/8 target for total fuel consumption was 121.7 million litres (up from 113.3 million litres originally).

⁴ On time performance, as measured by percentage of sailings in each quarter year which depart within 10 minutes of schedule.

Traffic volume trends



During PT1, traffic volume grew at an average of 1.1% per year, with variations by route and by year. On the **major routes**, volume growth averaged 1.3% per year while fares including fuel surcharges rose at 4.5% per year over the performance term.

The **Horseshoe Bay-Langdale** service (route 3) registered the highest traffic growth rate at 1.7% per year.

On the 16 **minor routes**, traffic growth averaged 0.5% per year, even though fares including fuel surcharges rose at an average of 8% per year on these routes during PT1.

In the north, although the regular service was resumed in 2007/8 after a one-year disruption after the sinking of the Queen of the North, traffic is still recovering, ending the performance term more than 10% under previous levels.

Alternative Service Delivery

Section 69 of the Act requires BC Ferries to seek alternative service providers (ASPs) on its routes, engaging them where cost-effective, and to submit a plan for doing so for each performance term. The PT1 plan called for ASPs to be sought on six routes in three clusters—three northern routes, Comox-Powell River-Texada, and Mill Bay-Brentwood Bay).

By the end of PT1, none of the search processes on these routes was fully complete. The PT2 plan, submitted at year-end, carries forward the PT1 processes, and adds three new routes to be tested for service delivery by alternative providers.

A farewell and a welcome

Mr. Alan Eastwood stepped down from the post of Deputy BC Ferries Commissioner in March 2008. I will miss him for his solid work at the commission, for his thoughtful advice and quiet guidance, and I thank him wholeheartedly for his contribution.

In June 2008, following an exhaustive search, **Mr. Sheldon Stoilen**, BSc, CA, was appointed by Order-In-Council to the post of Deputy BC Ferries Commissioner for a six-year term. I am thoroughly looking forward to working with him.

Respectfully submitted,

Martin Crilly
BC Ferries Commissioner

July 21, 2008

2 Productivity and Innovation

In our last annual report we raised the question of whether **significant productivity gains and innovation** will be forthcoming from BC Ferries, and how. This is key to keeping down fares and subsidies in the future.

Productivity improves when the growth rate of outputs (e.g. in traffic volume carried) exceeds that of inputs (labour, fuel, maintenance and capital inputs consumed).

At time of writing, the picture of BC Ferries' productivity performance in PT1 is incomplete and it requires further analysis. This section makes observations on what is known so far, and raises selected issues for the future.

Capacity utilization trends in performance term one

Higher load factors, i.e. better capacity utilization, are one avenue to productivity improvement. Over the five years of PT1 on the three **major routes**, comprising almost 60% of its total business⁵, BC Ferries achieved a notable increase in utilization of vehicle capacity⁶, from 66% to 70%. This resulted from 4.3% growth over PT1 in vehicles carried, achieved while increasing capacity by only 2.3%. The benefits of this improvement are being passed to PT2 customers on major routes since, in setting price caps for PT2, the performance of the company for the last year of PT1 was our baseline.

On the **minor routes**, however, vehicle capacity utilization in PT1 was much lower. There was virtually no gain over the five years: it remained, on average across all 16 minor routes, in the 43% to 44% range.

In the low-season fourth quarter (January-March 2008) on each of six of the minor routes, average vehicle capacity utilization was less than 30%. In other words, over 70% of deck space was empty on sailings made on these routes in this period.

The lack of improvement on the minor routes resulted from two conditions: relatively low growth in vehicle traffic coupled with limited ability to trim lightly used services. As observed in our last report, BC Ferries' service contract with the Province offers little flexibility in services to be provided. We note that the contract amendment of June 2007 gives

⁵Measured by share of general revenues totalling \$641 million in fiscal 2007/8.

⁶Measured by annual automobile-equivalents (AEQs) carried as a percentage of annual AEQ capacity provided. Passenger traffic and passenger capacity are not included in this measure.

BC Ferries ability on most routes to shift some sailings from times of relatively lower demand towards times of higher demand, while keeping the total annual number of sailings unchanged.

Productivity challenge for performance term two

In our remarks to the BC Ferries Board of Directors in September 2007, we stated that we would like to see the company follow a strong and systematic approach to innovation.

In setting price caps for PT2, we built in a challenge to BC Ferries to improve its productivity by 1% annually, system-wide.

Half of the target gain we expect to occur as a result of traffic growth, the rest through tighter and more effective management of fuel, labour, maintenance and capital, including the use of new technology and other sources of productivity gain yet to be uncovered by the company.

Importance of the length of the performance term

Incentives for the company are crucial to achieving such gains. Under our system of price cap regulation under the Coastal Ferry Act, one incentive is the ability to retain cost savings until the end of a performance term.

Specifically, BC Ferries can keep cost savings made within a given performance term (e.g. PT2), knowing that fares for all of that term, once set at its start, are disconnected from actual costs in that term, except in extraordinary circumstances.

Then, at the start of the next term (e.g. PT3), the Act requires the commission to re-set fare caps for that term to cover costs based on a new forecast that will incorporate productivity gains achieved in PT2 and any productivity gains the commission thinks that the company should achieve in PT3. This procedure captures any productivity gains made in PT2 for the benefit of PT3 customers, in the form of lower-than-otherwise fares. The cycle will then repeat.

This year **the importance of the length of the performance term**, fixed by the Coastal Ferry Act at four years for PT2 onwards, became more apparent. We saw signs that the four-year performance term creates only a modest incentive to cost-saving.

We find the company to be understandably risk-averse. Even a low-to-medium-risk capital investment, with significant potential returns in the form of operating cost savings, seems not particularly attractive to the company, under the four-year term. From its point of view it seems, understandably, best to behave conservatively, not experimenting much and risking relatively little, knowing that the regulator is required to re-set fares, based on actual costs, within a short four years. At that point the regulator must put priority on financial sustainability of the company as one of the statutory principles for price-cap setting.

Commission responses within the framework

We think that a longer than four-year limit for retaining savings would more strongly encourage innovation and investment for efficiency, which is in the long-term interests of ferry customers. Accordingly we have offered to commit to postpone for more than one four-year term the capture for fare-payers of cost savings from specific initiatives. We know that the

company may question how real this offer can be: whether the commission has the right to make it, and if it does, whether future commissioners will be bound by undertakings of their predecessors.

Beyond this offer, however, the company is on notice that we may find it insufficiently aggressive on specific productivity gains during PT2. In this case we may take its PT2 conduct into account when setting fare caps for PT3, in the form of a higher-than-otherwise productivity challenge in PT3.

3 The Role of the Commission

**Policy Principles
for the BC Ferry Commission**
Coastal Ferry Act, s 38

- (a) priority is to be placed on the financial sustainability of the ferry operators;
- (b) ferry operators are to be encouraged to adopt a commercial approach to ferry service delivery;
- (c) ferry operators are to be encouraged to seek additional or alternative service providers on designated ferry routes through fair and open competitive processes;
- (d) ferry operators are to be encouraged to minimize expenses without adversely affecting their safe compliance with core ferry services;
- (e) cross subsidization from major routes to other designated ferry routes is (i) to be eliminated within the first performance term of the first Coastal Ferry Services Contract to be entered into under this Act, and (ii) before its elimination, to be minimized;
- (f) the designated ferry routes are to move towards a greater reliance on a user pay system so as to reduce, over time, the service fee contributions by the government.

The **BC Ferry Commission** regulates ferry operators under the Coastal Ferry Act of 2003. The Province appoints the commissioner and up to two deputy commissioners as statutory officers for six- to eight-year terms. They are independent of both the government and of ferry operators.

Their decisions cannot be appealed, except on a question of law. They may be terminated only for mental infirmity, conviction for an indictable offence under Canada's criminal code, or a judicial finding of conflict of interest or material breach of duties or obligations.

The Commission is not an ombudsperson acting to resolve any private disputes with ferry operators; nor is it a general complaints or compliments bureau. Further, it is not responsible for regulating safety or environmental impacts of ferry operations.

In exercising its powers as watchdog, the Commission is obliged to follow six policy principles in protecting the public interest (see box, left).

BC Ferries was created in April 2003 from the former BC Ferry Corporation, which was a taxpayer-supported crown corporation. It is now a self-financing company with a mandate to widen travel choices for users and improve service quality.

Under a long-term contract with the Province, BC Ferries must operate its system to provide defined **minimum core service levels** on each of the 25 routes. On three of them, called **major routes**, which are financially self-sufficient, BC Ferries receives no subsidy. On the other 22, the government pays BC Ferries a **ferry transportation fee** per-round trip sailing.

One of the Commission's tasks is to **regulate ferry fares**. The Commission sets a ceiling or "price cap" on the average level of fares which BC Ferries can charge. The goal in setting the price cap is to balance consumer protection with financial sustainability of the ferry operator, while encouraging efficiency.

The routes are divided into seven geographic groups. Each group has its own price cap, which is a ceiling on the weighted average level of the individual fares within the group. The level is re-set after every fourth year.

Each four year⁷ period is termed a "performance period". In its surveillance of ferry fares, the Commission ensures that the weighted average of ferry fares, for each of seven groups of routes, does not rise above the cap for each group. If it does, the Commission may penalize the operator unless corrective action, e.g. reducing fares, is taken within the next quarter.

Regulation of service quantity

In overseeing the amount or **quantity of service** provided by BC Ferries, the Commission monitors the adherence of BC Ferries to the terms of its service contract with the Province. The Commission checks that the numbers of sailings on each route are at a minimum equal to those required in the service contract, subject to an allowance for missed sailings for certain reasons (e.g. bad weather). If there is a shortfall in the quantity of service the operator sacrifices the service fee and may face other more serious consequences.

Regulation of service quality

While the broader and less readily measured performance parameter of **service quality** (e.g. punctuality, reliability, comfort and convenience to customers, or other qualitative dimensions of ferry service) are of great import to ferry customers, the Commission does not try to regulate in this area. To do so would be difficult, inconsistent with the legislature's intention that regulation be exercised in a light handed fashion.

However, the Commission does track BC Ferries' regular reports of its on-time performance, and the number of "overload" sailings which depart leaving customers behind in the waiting area. The Commission also inspects regular customer satisfaction sampling surveys which BC Ferries is contractually bound to carry out using an outside polling firm.

Pro-competitive regulation

Although BC Ferries has weighty service obligations, it also enjoys **privileges as a near-monopoly**. It has exclusive use of terminals, which are facilities of major strategic and competitive importance to an operator. On 22 of its routes (those other than the three major routes), BC Ferries is the sole recipient of taxpayer support. The company is also income-tax exempt. It has the advantages of a large, incumbent operator with flexibility in vessel deployment, able to take advantage of economies of scale and network coverage. These give the company a low risk profile from the investors' perspective and result in a comparatively low cost of borrowing.

These advantages are intended by the legal and contractual framework, but they largely **protect BC Ferries from meaningful competition**. There are few existing competitors against whom to benchmark BC Ferries. The market and regulatory structure does not foster the emergence of such competitors in future. It falls to the regulatory framework and the commission to provide a substitute discipline.

In this context, to promote **efficiency**—which helps keep down both ferry fares and the need for taxpayer funding—the Commission's rulings aim to provide incentives to BC Ferries to deliver ferry service in an

⁷ Except for the first performance period, which was five years, ending on March 31, 2008.

efficient fashion while maintaining the required priority on its financial sustainability.

The Coastal Ferry Act requires BC Ferries, in each performance period, to submit to the Commission a plan to **seek additional or alternative service providers** (ASPs)—and then to execute that plan. ASPs could **serve on BC Ferries routes under subcontract**, if they could reduce the costs of ferry operations. The Commission sees this clause, in part, as guarding against the danger of BC Ferries, in the absence of little other competition, becoming complacent about its own methods and cost-efficiency. The Act empowers the commission to penalize BC Ferries if it considers that BC Ferries has not submitted a satisfactory plan, and to order it to submit one and to execute it—to a deadline.

Commission probes

Overall, the Commission is alert for information, either from its own observations or from the public, suggesting how the performance, service quality, efficiency or productivity of ferry operations could be improved. The Commission may decide to launch a probe on any topic of interest to it, in which the ferry operator is legally required to answer the Commission's questions and comply with any resulting orders, with no appeal.

4 Activity Summary

Commission Activities in the fiscal year 2007/8

1. **Regulation of Ferry Fares**
 - confirmed actual fares were within caps during the year
 - issued a final decision on price caps for performance term two (2008-2012)
2. **Regulation of Service Levels**
 - confirmed that BC Ferries delivered contracted round-trips
 - undertook probes on service quality on two routes
3. **Special Decisions**
 - monitored implementation of BC Ferries' Alternative Service Providers Plan
4. **Enforcement**
 - monitored BC Ferries public reporting
5. **Publication and Outreach**
 - maintained records, published decisions, and communicated with the public and stakeholders.
 - attended seven meetings with stakeholder groups
6. **Administration and Reporting**
 - operated an office, obtained support services and consulting advice
 - participated in search for new Deputy Commissioner

The Commission's activities fall into **six headings** shown on the left. These headings are taken from the Commission's Service Plan and Budget for the year ending March 31 2008, published in September 2006. The core, ongoing activities are in headings 1 and 2: the **regulation of fares** through the price cap mechanism, and the **regulation of service levels**.

Special decisions under heading 3 include pre-approval of major capital deployments (e.g. new ships), and overseeing the search for alternate service providers. The Commission found no reason to undertake **enforcement** action (under heading 4).

Two further activity areas were to inform the public about the Commission's role (under heading 5 - **publication and outreach**) and maintaining routines and procedures under **administration and reporting** under heading 6.

Readers will find **more detail** in the table on the following pages. It lays out the Commission's **planned versus actual activities** under the same headings, keyed to the relevant section number of the Coastal Ferry Act.

5 Activity Detail

This section takes the list of the planned Commission activities from its Service Plan and offers a detailed description of actual activities.

Activity number	Coastal Ferry Ac Section	Activity Description copied from our Service Plan for 2007/8 which was published in September 2006	Actual Activity in Fiscal 2007/8
1.0		Regulation of Ferry Fares	
1.1	39	Monitor how weighted average price is calculated	
		<p>The Commission will monitor the functioning of the Average Fare Model. This was developed in collaboration with BC Ferries in 2003/4 as the key measuring tool for judging whether BC Ferries' weighted average fares are within the price cap established by the Commission. The model requires adjustment and improvement (e.g. for changes in type and quality of source data) and cross-checking from time to time. Where necessary, the operation of the model will be externally validated.</p>	<p>We considered various observations and concerns offered by BC Ferries on the behaviour and usefulness of the Average Fare Model.</p> <p>We noted that revenue from Social Programme Reimbursements (fare subsidies paid by the Province for certain ferry customers) had not been included in the revenue figure used for calculating the average fare index, though the units carried had been included in the traffic volume figure used for calculating the index. We satisfied ourselves that (1) this was not a material issue in the first performance term, since the base of the index had been calculated in the same way, and (2) the revenue from Social Programme Reimbursements would be included in the calculation for the second performance term.</p> <p>On April 30 2007 we reported on an examination of assured loading premiums for the major routes, where BC Ferries currently determines both the price charged and amount of space devoted to assured loading ticket holders.</p> <p>In November 2007 in Nanaimo, we held a half-day seminar for chairs of Ferry Advisory Committees. The session responded to questions on how the Commission compares the fares actually charged by BC Ferries in relation to fare caps. We issued an associated six-page Q&A paper.</p> <p>Normally the Commission permits the average fare to go over the price cap for just one quarter before requiring BC Ferries to return all excess revenue to customers (through lower-than-otherwise fares) in the very next quarter after the overage. At BC Ferries' request the commission agreed to a one-time extension of this "grace period" to two consecutive quarters for the measurement point at March 31 2008. We issued a Commission Memorandum 27 explaining why.</p>

1.2	38,65	Review BCF quarterly reports on price level	
		<p>The Commission will specify contents required in BC Ferries quarterly reports respecting fare levels for each route group. The Commission will determine if the weighted average of the tariffs charged for each route group, as measured using the above Average Price Model are within the price cap established, and if not make appropriate orders.</p>	<p>We reviewed BC Ferries quarterly reports comparing the actual weighted average fare for each route group with the price cap for that group. We found the company in compliance.</p> <p>In May 2007 we noted that for the minor route group of 16 routes (serving mainly the Gulf Islands), BC Ferries' actual fares were some 4% beneath the maximum average it is allowed to charge.</p>
1.3	42	Handle any BCF applications for extraordinary price increases	
		<p>The Commission will review and consider applications by the ferry operator for extraordinary tariff/price cap increases, for example due to extraordinary increases in the price of fuel.</p>	<p>BC Ferries made no application for an extraordinary price cap increase during the year. Existing fuel surcharges previously authorized under section 42 were left in place.</p> <p>In December 2005 in our Order 05-06 authorizing a fuel surcharge under section 42 of the Act, we set a fuel conservation target for BC Ferries through March 2008—a reduction of one percent in fiscal 2006/07 and a further one percent in fiscal 2007/08—and required the company to show a fuel conservation plan. For 2006/7 BC Ferries reported that it met the target.</p> <p>For 2007/8, fuel consumption was expected to increase overall due to deployment on long northern routes, for the whole year, of the Northern Adventure, a vessel with relatively high fuel consumption. In July 2006, this vessel had been declared as reasonably required by the commission, to replace urgently the Queen of the North which sank in March 2006.</p> <p>Accordingly, in July 2007, BC Ferries proposed an upward-revised target consumption for 2007/08 recognizing the extra fuel necessarily burned in the north. The 2% savings target for the second year remained at 2.3 million litres for 2007/8, but from an adjusted baseline.</p> <p>The revised 2007/8 target for total fuel consumption was 121.7 million litres (up from 113.3 million litres originally). Data on actual performance are expected shortly from BC Ferries and will be reported when received.</p> <p>Note that just before the start of the year, for performance term two, we provided, as part of our price cap review under section 40 of the Act, a new mechanism to provide a fuel surcharge/rebate to customers through our Memorandum 24 dated March 30 2007.</p>
1.4	45	Adjust price cap for any service cuts/route discontinuances	
		<p>The Commission will review service reductions or discontinuance of routes for impact on price cap and make appropriate adjustments in price cap.</p>	<p>We received no applications for service reductions or route discontinuance during the year.</p>
1.5	40, 41	Conduct price cap review for next performance term	
		<p>The Commission will initiate on or before October 1</p>	<p>Just before the start of FY 2007/8 we had issued our preliminary decision on fare caps for the second performance term. We issued a companion memorandum to our preliminary decision for a new automatic adjustment mechanism for fuel surcharges/rebates responding to changes in fuel prices from 2008 to 2012.</p>

	<p>2006 a price cap review for second performance term, i.e. for the period April 1, 2008 – March 31, 2012</p>	<p>We issued a 15-page set of Questions and Answers as background to our preliminary decision, and invited comments from the public to the Commission by June 30 2007 on the preliminary decision.</p> <p>The price cap review continued through FY 2007/8 as the main topic addressed in meetings between the Commission and with BC Ferries and its consultants during the year, which were held mainly at BC Ferries head office in Victoria.</p> <p>On April 26 2007 we issued a paper for the public titled Supplementary Q&A on Price Caps for Performance Term Two addressing further questions received from the public about the preliminary price cap decision. As required by the Act we received public input on the preliminary decision through June 30 2007 and thereafter published a report titled Public Response to Preliminary Fare Caps Decision.</p> <p>Under the timeline in the Coastal Ferry Act, the Province and BC Ferries had three months, to June 30, 2007, to make any changes to their Coastal Ferry Services Contract (CFSC), which could in principle involve changes in ferry service and changes in taxpayer funding. BC Ferries provided us with an amendment to the CFSC dated June 30 2007. The amendment included:</p> <ul style="list-style-type: none"> • no change in taxpayer funding that would produce a substantial adjustments in our March 30 preliminary decision on fare caps for performance term two; and • some increased flexibility for BC Ferries on some routes in scheduling its sailings and in structuring its tariff, giving an opportunity for BC Ferries to be more productive. <p>To aid public understanding we issued a three-page Commission Summary and Comments on the amendment. We also published the complete and more technical full text of the 61-page official signed contract amendment (a 4MB pdf file).</p> <p>On September 18 2007 we issued our price cap decision for performance term two in Order 0701. We noted fare caps will rise faster than the consumer price index for the next four years. The reasons are vessel and terminal renewal, recovery of deferred fuel cost, taxpayer funding increasing but not as quickly as costs, and general cost inflation. The decision adjusted the preliminary decision on fare caps issued March 30, 2007, recognizing higher fuel prices, changes in new vessel costs and timing, changes in the Coastal Ferry Services Contract, and other factors.</p> <p>Concerning cost efficiency related to effective procurement processes, based on a concern raised by the Independent Contractors and Businesses Association, in October 2007 the Commission asked BC Ferries to respond to a series of questions on the tender process used for certain construction contracts at its Departure Bay Terminal. BC Ferries responded. The Commission did not pursue the matter further.</p> <p>The Coastal Ferry Act section 41(2)(b) obliges us to establish an appropriate return on equity for BC Ferries. Our Commission Memorandum 25 of December 14 2007 recorded a final ruling of 13.16% p.a. for BC Ferries' before-tax return on equity for performance term two, which figure had been used in the setting of price caps for performance term two.</p> <p>Commission Memorandum 26 of December 17 2007 detailed for BC Ferries how the CPI adjustments to price caps in performance term two should be calculated.</p> <p>Commission Order 0701A dated December 21 2007 superseded the above September 18 decision. The Order corrected a Commission error in determining BC Ferries' allowable costs</p>
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			<p>for the second performance term. This affected only the major route group and raised the price cap as follows:</p> <ul style="list-style-type: none"> • On April 1, 2008 the price cap will increase by 7.3% (up from 6.4% in Order 07-01), and • On each of April 1, 2009, 2010 and 2011 the price cap will increase by 2.7% (up from 2.0%) plus 0.49 times the latest reported annual increase in the Consumer Price Index for British Columbia. <p>All other conditions of the previous order remained in effect, including the price caps for all other route groups as follows:</p> <ul style="list-style-type: none"> • On April 1, 2008 the price cap will increase by 4.0%, and • On each of April 1, 2009, 2010 and 2011 the price cap will increase by 5.7% plus 0.73 times the latest reported annual increase in the Consumer Price Index for British Columbia.
2.0	Regulation of Ferry Service Levels		
2.1	38,65	Review BCF quarterly reports on service level	
		The Commission will specify the format of, and review quarterly reports of BC Ferries as the ferry operator to determine if it is meeting the contract service requirements.	<p>We reviewed BC Ferries quarterly reports on on-time performance, overloads, and sailings provided relative to contract.</p> <p>On April 30 2007 we reported our probe into crewing at less-than-maximum levels on the Comox-Powell River route, which resulted in passengers being refused passage, even though the vessel was not full, in the summer of 2006.</p>
2.2	38,66	Review BCF annual reports on service level	
		The Commission will specify the format of, and review annual reports of BC Ferries as the ferry operator to determine if it is meeting the contract service requirements. It will also review BC Ferries' annual customer satisfaction survey, which BC Ferries must provide to the Commission under the terms of the Coastal Ferry Services Contract.	<p>We reviewed BC Ferries annual report made in July 2007, and reviewed the annual customer satisfaction survey.</p> <p>Prompted by a number of customer complaints about the quality of service on the Bowen Island service, the Commission asked BC Ferries to respond: the company did so with a memorandum addressing the Commission's questions on service quality for Bowen Island</p>
2.3	43	Handle any BCF applications for service reductions	
		Review and consider any applications by the ferry operator for reductions in service (temporary reductions would occur immediately)	We made no rulings authorizing service reductions in FY 2007/8.
2.4	44	Handle any BCF applications for route discontinuance, possibly hold hearing	
		Review and consider any applications by the ferry operator to discontinue a route. After October 2006, route discontinuance applications may be made (the determination process takes 9 months).	Route discontinuance is allowed from October 2006 but no application was made.

3.0		Special Decisions	
3.1	55	On ferry operator's request, decide if a proposed capital deployment is reasonable	
		If a ferry operator makes an application, the Commissioner will consider a proposed capital deployment or capital expenditures in connection with a route or terminal to determine if they are reasonably required. Consultants of various specialties will be engaged to undertake a "process audit" of the BC Ferries analysis.	BC Ferries made no applications for a ruling under this section in FY 2007/8.
3.2	38(4)	Deregulate a ferry route if competition sufficient	
		Make a determination of removing the route designation for a route upon which sufficient competition exists so that regulation of that route is no longer necessary.	There was no activity in this area.
3.3	69	Review BC Ferries Plan to Seek Alternate Service Providers (ASPs)	
		<p>Monitor the market for ferry services with a view to encouraging competition for BC Ferries; monitor BC Ferries implementation of its Additional and Alternate Service Providers Plan (supplemented in August 2005) to provide service on BC Ferries designated routes by subcontract, franchise, or other means.</p>	<p>In our last Annual Report, for FY 06/07, issued in July 2007, we noted that plans to test whether other ferry operators (ASPs) would be cost-effective subcontractors had not advanced much. During this year FY 07/08, we continued monitoring BC Ferries activities in implementing its plan for performance term one and observe that during the year:</p> <ul style="list-style-type: none"> the search for ASPs for the north (routes 10,11 and 26) and Comox-Powell River-Texada (routes 17 and 18) remained on hold for reasons partly beyond the control of BC Ferries; the process for Mill Bay-Brentwood Bay (route 12) continued quite slowly and was not completed by the end of the year; discussions with a potential ASP on a pilot project for routes 21 and 22 (Hornby and Denman Island services) ended when BC Ferries terminated its Memorandum of Understanding with the potential ASP. <p>At the end of the year, just before the start of the second performance term, BC Ferries issued its Additional or Alternative Service Providers Plan: Second Performance Term. In it, BC Ferries reviews experience in the first performance term (2003-2008), indicates lessons learned, and describes how it will seek ASPs in the second term (2008-2012).</p> <p>The company states that as time and resources permit, certain additional routes would be offered for alternative service delivery:</p> <ul style="list-style-type: none"> Campbell River-Quadra Island and Quadra Island-Cortes Island Port McNeil-Sointula-Alert Bay
4.0		Enforcement	
4.1	38(2)	Monitor BCF reporting to public	
		The Commissioner will observe how BC Ferries reports its own performance respecting pricing its fares under the price cap, and respecting its service level actually delivered versus the contracted service levels.	BC Ferries issues tariffs in print and on the world wide web, while the Commission publishes average fare levels compared with price caps for regulatory purposes.

4.2	46	Inspect BCF records as required	
		Order inspections of the records of the ferry operator as necessary	No activity was necessary.
4.3	48	Issue orders to BCF re: non-compliance with the law as required	
		Issue orders for non-compliance with the legislation as necessary	No activity was necessary.
5.0	Publication and Outreach		
5.1	52	Maintain Commission records, provide public access	
		<p>Files will be maintained accessible to the public under the Freedom of Information and Protection of Privacy Act. Response to public enquiries will be made via telephone, postal mail, e-mail. A web site will be maintained and regularly updated as needed, preferably at least monthly.</p>	<p>We retained a part-time contractor to organize and maintain our public correspondence on an internet server in all-electronic form to both the Commissioner and Deputy Commissioner.</p> <p>Members of the public accessed the Commission in a number of ways: by logging on to our website at www.bcferrycommission.com, by contacting us directly via email, phone, fax or regular mail, and by subscribing to receive email information updates.</p> <p>Our website continued to be the primary means of providing Commission information to the public. It was updated as needed throughout the year.</p> <p>We sent out important Commission news periodically to the almost 700 subscribers on our email distribution list. For example, updates were issued at the completion of every milestone of the Price Cap Review process. Our updates included a brief summary of any Commission decisions to date, a reminder of the overall review process and links to the Commission website for more details and frequently asked questions. We gave contact information, along with where to direct comments on specific topics, the Commission, BC Ferries and the Ministry of Transportation.</p> <p>Members of the public contacted us directly, with over 500 emails, letters and faxes, and some 20 phone calls received. An electronic database of all correspondents and their comments was maintained and reviewed regularly.</p> <p>With the price cap review process as the main driver, our correspondents focused primarily on rising fares, with the majority identifying three public policy issue areas: the economic and social impacts of higher fares on island communities, the consideration of all ferries as part of the provincial highway system, and the level of user-pay for coastal ferry service vs. other public transportation services.</p> <p>Everyone who contacted the Commission directly received a personalized response from the Commissioner or staff. We directed matters outside the Commission’s purview to the Ministry of Transportation or BC Ferries for a response, and in some cases we forwarded comments on our correspondents’ behalf to the appropriate agency.</p>
5.2	52	Publish decisions/determinations/orders/proceedings	
		The Commissioner will publish every decision, determination and order in a manner that the Commissioner believes will bring it to the attention of the public. All such items will be published on the Commission's website, at a minimum.	We published all decisions, determinations and orders on our web site with explanatory text, and included question-and-answer sheets as required.

5.3	NA	Communicate with public and stakeholders	
		The Commission will actively communicate the role and responsibilities of the Commission to the public; make appearances in the media; make presentations and speeches to stakeholder groups.	During the year, we attended meetings with the public and stakeholders as follows: Chairs of the Ferry Advisory Committees (two meetings); Gabriola Ferry Advisory Committee; officials of the Ministry of Transport; BC Ferries Annual Public Meeting in Powell River; a potential alternative service provider; BC Ferries Board of Directors with formal remarks. We were interviewed some 6 times by the broadcast media and on several occasions by print media.
6.0	Administration and Reporting		
6.1	36	Operate office and engage external support services	
		Operate the office of the Commission. Maintain arrangements for telephone, mail and electronic access. Rent office space as required. Office operations (secretarial, phone, courier, post, internet, website) Office equipment dedicated to Commission use. Work with Office of the Attorney General as provider of payment system on behalf of the Commission. Obtain internal bookkeeping, archiving, and legal services as required.	We operated a virtual office. Our accounting and payment system was provided by Office of the Attorney General at no charge to the Commission. We did not engage independent legal advice during the year. We engaged a contractor to develop our communication and outreach plans and to assist with public correspondence. The Commissioner and Deputy Commissioner sat on the selection panel for a new Deputy Commissioner in a search process under the auspices of the Board Resourcing and Development Office of the Province of BC
6.2	NA	Research background to ferry operating environment	
		This activity is Commissioner's ferry system familiarization and background study. The Commissioner intends to travel all ferry routes in person. Research and Investigations initiated by Commission.	During the year the Commissioner attended the Interferry Conference in Sweden and visited a Swedish Road Administration inland ferry operation.
6.3	69	Prepare Commission's annual budget	
		Budget will include expenditures reasonably expected to be incurred in the following year, supported by a Service Plan for the year.	We prepared our Annual Service Plan and Budget for FY 2008/9. We submitted it to the Minister and BC Ferries by September 30 2007 as required.
6.4	53	Report annually to Lieutenant-Governor in Council	
		Within 4 months after the end of each fiscal year, the Commissioner will make a report to the Lieutenant-Governor in Council for the preceding fiscal year, setting out briefly (a) all applications and requests for decisions to the commissioner under the Act, (b) all orders issued by the commissioner, (c) the financial statements applicable to the office of the commissioner for that year along with full disclosure of the expenses of, and associated with, the office of the commissioner, and (d) other information the Lieutenant-Governor in Council directs.	We submitted our FY 2006/7 Annual Report to the Lieutenant Governor in Council as required.

6 Average Fare Levels

The table below shows the values of a price cap index (=100 at 2003) and compared to an index of actual weighted average fares, for each of seven groups of routes in the BC Ferries system. The figures are computed by methods laid down in Commission Order 05-01. They exclude extraordinary increases allowed in performance term one due to high fuel prices, which are separately measured and tracked.

Normally the Commission permits the average fare to go over the price cap for just one quarter before requiring BC Ferries to return all excess revenue to customers (through lower-than-otherwise fares) in the very next quarter after the overage. We agreed to a one-time extension of this “grace period” to two consecutive quarters for the measurement point at March 31 2008. We issued a [Commission Memorandum 27](#) explaining why.

These figures confirm that BC Ferries was in compliance with price caps in fiscal 2007/8.



Average Fare Index Summary

Route Group	Jun-2006	Sep-2006	Dec-2006	Mar-2007	Jun-2007	Sep-2007	Dec-2007	Mar-2008	
#1: Majors	Cap	107.37	108.40	109.06	109.58	110.33	111.45	112.10	112.67
	Actual	106.92	108.52	108.55	109.33	111.78	111.13	112.46	114.00
#2: Route 3	Cap	111.91	113.42	114.46	115.39	116.65	118.35	119.55	120.59
	Actual	110.13	111.61	113.30	114.93	116.59	117.92	119.00	119.76
#3: Northern	Cap	111.00	113.60	114.13	114.71	115.98	118.47	119.24	119.87
	Actual	108.49	101.91	104.28	104.58	106.78	115.23	114.13	114.28
#4: Route 40	Cap	109.96	113.79	No Service	114.38	118.79	No Service		
	Actual	107.17	122.24		122.45	133.18			
#5: Route 12	Cap	111.57	113.34	114.36	115.27	116.53	118.32	119.48	120.49
	Actual	107.17	108.67	110.67	112.20	117.07	117.67	121.84	124.36
#6: Minors	Cap	111.78	113.47	114.43	115.33	116.57	118.39	119.50	120.68
	Actual	106.97	108.44	109.66	115.21	116.77	118.38	119.62	117.07
#7: Route 13	Cap	111.16	113.70	114.27	115.14	116.16	118.20	119.46	120.59
	Actual	115.84	106.40	111.90	115.82	116.29	117.71	117.80	116.37

7 Financial Statements

Accounting Services

The Commission is grateful for the assistance of the Ministry of the Attorney General which provides accounting, banking and payment services at no cost to the Commission. These financial statements are based upon the financial information provided by the Ministry.

Summary Financial Statements

BC Ferry Commission
Summary Financial Statements
(In \$ thousands)

	FY	2007/08 Budget	Actual	2006/07 Actual
Statement of Operation				
<i>Revenues</i>		437	328	237
<i>Expenditures</i>				
Operating Costs		437	145	280
Surplus (deficit)		0	183	-43
Change in Net Assets				
Opening balance			46	89
Surplus (Deficit)			183	-43
Net Assets end of year			229	46

Revenues

Revenues consist of a percentage levy on toll revenues from ferry operators. In fiscal year 2007/8, the total paid to the Commission by BC Ferries, the only ferry operator regulated by the Commission during the year, was \$328,000.

Expenditures

Expenditures in fiscal 2007/08 were \$145,411. Expenditures were for Commissioners fees and expenses and for the cost of consultants engaged to assist and advise the Commission.

The Coastal Ferry Act s.58 allows the Commissioner a budget which does not exceed the total of the following:

- (a) for each quarter, if any, of that fiscal year in which the commissioner is to take any action under section 40, 1/20 of 1 % of the previous year's tariff revenue;
- (b) for every other quarter of that fiscal year, 1/40 of 1 % of the previous year's tariff revenue.

Section 40 of the Act concerns establishment of price caps for subsequent performance terms. The Commission was active under section 40 in the first three quarters of fiscal 2007/8, so that paragraph (a) above is applicable for three quarters, and paragraph (b) for one quarter, giving a maximum annual budget of 0.175% (3 x 0.05% plus 1 x 0.025%) of the previous year's tariff revenue.

BC Ferries' tariff revenue was \$363.228 million (i.e. excluding retail and other ancillary revenue and service fees) for fiscal 2006/07. The cost of operating the Commission in 2007/8 represented 0.040% of this figure, or less than one quarter of the budget maximum.

Commissioner Remuneration

The Commissioner and Deputy Commissioner are paid a per-diem fee for their services. The Commissioner received \$90,825 in fees during the year. In addition he was reimbursed \$12,687 for expenses incurred during the year, including travel, dedicated office equipment, office supplies, telephone, web site and other communications expenses. The Deputy Commissioner received \$24,418 in fees for his services and he was reimbursed \$1,479 for travel and other expenses incurred in the period.

Net Assets

The difference between the amounts received from ferry operators and expenditures is carried forward for use in the next fiscal year. \$228,972 was carried forward into fiscal 2008/09. The Net Assets of the Commission are included in the Financial Statements of the Province of BC.