# Performance Review of BC Ferries Vacations

British Columbia Ferry Commission

March 2015



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## **Executive Summary**

PricewaterhouseCoopers LLP ("PwC") was engaged by the British Columbia Ferry Commission (the "Commission") to conduct a performance review of BC Ferries Vacations ("BCFV").

The Coastal Ferry Act allows for the Commissioner to conduct a performance review of one or more aspects of the operations of British Columbia Ferry Services Inc. ("BC Ferries"). The purpose of the performance reviews is to hold BC Ferries accountable and by doing so to raise public confidence that the company is operating efficiently, making prudent use of its resources, and operating in such a way as to keep ferry fares as low as reasonably possible.

Our performance review included the following tasks:

- Assessing the business case for BC Ferries Vacations ("BCFV");
- Assessing the adequacy and reliability of systems or procedures used to measure the financial results of BCFV;
- Assessing the cost effectiveness and contribution of this operation towards BC Ferries' overall financial results; and
- Assessing whether there are any opportunities to enhance BCFV' contribution.

Our main conclusions regarding the analysis are as follows:

- BCFV is meeting its intended goals. The business case for the service appears to relatively strong given the consumer takeup since inception and the high level of participation by partners.
- BCFV gross and net revenue expectations have exceeded the initial targets set out in the original five-year business plan. BCFV has achieved a 151 percent growth in revenues in the last four years, while expenses have declined 45 percent from the first year.
- The contribution and costs of a centrally located service centre in downtown Vancouver relative to another central location in either Vancouver or Victoria do not appear unreasonable. The benefits and costs of locating the Vacations Centre in its current downtown location are difficult to assess, as the store-front location contributes to general marketing and many information requests lead to follow-on sales, some of which become part of general tariff and reservation revenues. While a greater takeup of the Vacations Centre services is by Lower Mainland residents than by out-of-province visitors, direct costs for labour and store front space of the downtown Vancouver location appear reasonable.
- Revenue and cost information for the BCFV is part of BC Ferries' annual budgeting process. From a reporting structure, BCFV is part of Travel Services within the Corporate Development department. The head of the service reports to the VP of Marketing & Travel Services. This reporting structure appears appropriate given the complementary activities within Corporate Development that includes Web services and branding activities.
- An extensive list of active partners that includes over 80 hotels has been developed. These
  partners have been receptive to participation in packaged tours in Northern and Southern
  routes, suggesting that widespread incremental economic benefits are being generated in coastal
  communities as a result of the services. BC Ferries' investment in tourism marketing programs
  is also building demand in communities that have limited marketing resources.

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- Discounts offered on fares and hotels are consistent with industry practice. BCFV discount policies are the same as those offered other tour operators and BC Ferries do not offer discounts in excess of their best tour operator customers.
- BCFV has yet to reach a mature state. It has the potential to expand further with self-serve options as the new on-line reservation system is further developed.

#### Notice to Reader

This Report is issued by PwC for the exclusive use of the Commission in connection with its performance reviews of BC Ferries.

Our work did not constitute an audit conducted in accordance with generally accepted auditing standards, an examination of internal controls nor attestation nor review services in accordance with the standards established by the Canadian Institute of Chartered Accountants. Accordingly, we do not express an opinion nor any other form of assurance on the financial or other information, or operating internal controls, of BC Ferries.

PwC did not examine, compile or apply agreed upon procedures to satisfy the requirements of the Canadian Institute of Chartered Accountants to the financial information used in this Report and we therefore are unable to express assurances on such information except where expressly stated in the Report to form part of the scope of our work.

Further this Report does not constitute an opinion as to legal matters, including the interpretation of the Coastal Ferry Act or any other similar matters. The economic impact of the various procurement options is also outside the scope of PwC's work.

Our work is based primarily on the information and assumptions listed in the body of this Report. While we read information from various sources we did not perform checking or verification procedures except where expressly stated in the Report to form part of the scope of our work. Our work and commentary is subject to assumptions, which may change with the benefit of further detailed information. We make no representation regarding the sufficiency of our work and had we been asked to perform additional work, additional matters may have come to our attention that would have been reported to the Commission.

Some of the documents and figures we reviewed were produced by third parties. We did not corroborate or verify these documents and figures with these parties. It is outside the scope of our review to evaluate the methodology used to conduct independent studies; therefore, we have accepted the information as presented, including conclusions. We did review the credentials of external consultants that BC Ferries management relied upon and that we were unfamiliar with.

The outputs of the Report are intended to provide the Commission with information to assist in informing their decision making process pertaining to BC Ferries. PwC accepts no liability in respect of any loss, damage or expense of whatsoever nature caused by any use the reader may choose to make of this Report, or which is otherwise consequent upon the gaining of access to the Report by the reader.

Our Report, including its schedules must be considered in its entirety by the reader. Selecting and relying on specific portions of the analyses, or factors considered by us in isolation may be misleading.

## Background

In April 2003, the Province of British Columbia (the "Province") established the British Columbia Ferry Authority (the "Authority"), an independent corporation that holds the single issued voting share of BC Ferries.

BC Ferries, as the operating subsidiary of the Authority, provides coastal ferry services on the west coast of British Columbia. With 35 vessels travelling between 47 terminals, on 24 routes, BC Ferries is one of the largest ferry operators in the world, both in terms of fleet size and passengers carried. Its fleet includes a number of older vessels and BC Ferries has undertaken a process to upgrade its fleet and conduct necessary maintenance.

A Coastal Ferry Services Contract existing between the Province and BC Ferries defines service levels on each regulated route and the British Columbia Ferry Commission sets price caps across the route groups every four years. Within its operating framework, BC Ferries can decide on fares, and can access capital markets directly. The Commission is a provincial regulatory agency operating under the Coastal Ferry Act with responsibilities for making regulatory decisions affecting ferry operators in the Province, including BC Ferries.

Under Section 46.1 of the Coastal Ferry Act the Commissioner may conduct a performance review of one or more aspects of a ferry operator's operations including ancillary services. The purpose of the performance reviews is to identify any opportunities for further efficiencies in the operations of BC Ferries which may be incorporated in the determination of the price caps for future performance terms.

In conjunction with the price review which commenced early in October 2014, the Commission is conducting performance reviews of several areas. The Commission sought the assistance of PwC to conduct the performance reviews including the efficiency of BC Ferries Vacations.

## Scope and Approach

The scope of the performance review includes the following:

#### 1. Assessing the business case for BC Ferries Vacations

We assessed the business case by:

- Reviewing the business case for the service;
- Examining the current range of services currently offered by BC Ferries Vacations;
- · Gaining an understanding of issues that have arisen with the evolution of the service;
- Assessing pricing policies; and
- Confirming the business case for continuation of the service.

## 2. Assessing the adequacy and reliability of systems or procedures used to measure the financial results of BC Ferries' Vacations

We assessed the measurement of results by:

- Examining the current reporting structure
- Commenting on the adequacy and reliability of systems or procedures used to measure financial results

## 3. Assessing the cost effectiveness and contribution of this operation towards BC Ferries' overall financial results

We assessed the cost effectiveness and contribution by:

- Analyzing revenue by channel;
- Analyzing costs including direct and indirect costs (staff costs, rent, advertising);
- Analyzing contribution margins; and
- Analyzing the incremental revenues and cost benefit of the services.

## 4. Assessing whether there are any opportunities to enhance BC Ferries Vacations' contribution

We assessed the impact of new reservation system on potential sales.

Our work has included interviews with management, a visit to the Travel Centre, and development of a number of written questions for BC Ferries and the review of the responses. Our assessment is at a high level and as such we have not examined space requirements or benchmarked rental space costs for the Travel Centre.

## Profile of the Service

### Strategic Initiative

The creation of a Travel Services division and an integrated destination-oriented marketing approach has been developed as a strategic growth initiative by BC Ferries to earn incremental revenue by leveraging the existing customer base and growing new business by capturing incremental and discretionary travel dollars.

BCFV was developed to capitalize on demand from BC Ferries' primary market: British Columbia residents and short-haul regional travellers. BC Ferries is well positioned to package ferry travel with accommodation and activities as the Company services some of British Columbia's most desirable destinations. The focus is on developing vacation packages that represent each of the Company's route groups, major port destinations and high demand travel destinations.

#### Location

The Vacations Centre is centrally located in a high traffic area in Vancouver's downtown core. It occupies 2,600 square feet of retail space directly across from the Vancouver Convention Centre, and the cruise ship terminal at Canada Place. In 2013, these facilities combined attracted over 1.3 million people to the area, many of whom were interested in extending their city stay beyond Vancouver.

The Vacations Centre is in close proximity to Jack Poole Plaza which has become a tourism draw and a major point of gathering during local celebrations, including annual Canada Day celebrations. The area is also surrounded by major convention hotels and attractions and is the nucleus for sightseeing/tour bus services. The Vacations Centre is also near the core of Vancouver's central business district and conveniently located close to two Skytrain Stations and the West Coast Express providing access to business and commuter traffic.

BC Ferries' management examined this potential marketing strategy and decided to pursue a downtown Vancouver Vacations Centre as part of its marketing program to promote the brand and stimulate incremental traffic. This decision was supported by research conducted by InterVISTAS Consulting Inc. on the effects of storefront operations. It suggests that locating a sales office in a high traffic area in the downtown core has a more positive effect on sales than operating without one.

### Reporting

From a reporting structure, BCFV is part of Travel Services within the Corporate Development department. The head of the service reports to the VP of Marketing & Travel Services.

## **Business Model**

## Package Concepts, Pricing Model, Tour Operator Program

Vacation packages are developed to include a comprehensive mix of experiences that combine BC Ferries' products in key destinations that represent each route group, major ports of call and high demand routes. Packages are comprised of short getaway trips ranging from one to three nights, as well as longer vacations that include multiple destinations throughout the province with multiple activities and accommodation offerings.

BCFV offers over 100 pre-set packages that include a comprehensive mix of experiences that combine BC Ferries' products in key destinations that represent each route group, major ports of call and high demand routes.

Several sales channels are employed:

- Vancouver Vacations Centre
- Bcferries.com/vacations
- BC Ferries' toll free phone number

BCFV's business model is organized as a tour operator business model rather than a travel agency model. In this model, BC Ferries negotiates net rates from select suppliers, bundles several components together, adds a mark-up and then promotes the inclusive package price to the customer. This focus is to utilize price strategies that are built on offering a value-oriented retail price to generate a managed yield and higher volume.

Tariff within a package is set at a price consistent with the net rates set in BC Ferries' Tour Operator Pricing Program. The Tour Operator Pricing Program (TOPP) is structured to enhance sales of BC Ferries transportation by providing international travel resellers (tour operators) with net rate pricing based on sales volume. BCFV uses the same pricing that the Company is providing to a comparable reseller.

### Seasonal Pricing

Seasonal pricing is determined for each package based on the sum of the components in the package. The Company changes tariff pricing up to twice per year (depending on route), but accommodation and activities suppliers may have as many as 10 seasonal prices for the same product. The overall package price depends on the mix of products sold at any given period in time. Special offers may be developed within a season or holiday, and while the package rate may not change, the inclusions may. For example, inclusions such breakfast, a spa component or other hotel credits may be added to the existing packages to create a seasonal package. In this case, the package price would not change. The ferry component net price also does not change nor is it lower than the TOPP net rate.

### Supplier Selection

Each region is examined to determine the anticipated volume of hotel rooms that may potentially be sold each year. Seasonal demand patterns are considered, along with ease of access to and from the location. After that, accommodations are categorized using a common star rating system to ensure that BCFV has

a good range of quality and price points. The number of rooms and properties contracted depends on the popularity of the location and size of the property. Cities like Victoria, which are well known as a destination, are easily accessed by car and transit and have a wide variety of accommodation offerings. These will be more popular and therefore will require more room inventory. Smaller destinations, while popular, may have a very limited accommodation base available. In this case there is limited choice, which limits the potential for growth in these destinations. A similar process is used to select activities and excursions.

Specific business requirements have been determined to ensure consistency among BC Ferries' potential partners. To be considered for inclusion within the BCFV program, BC Ferries look for partners who can offer most of, if not all, of the following:

- An exceptional level of guest service with a minimum of one year in operation.
- Located in an area serviced by BC Ferries, or within a 90 minute drive of any BC Ferries terminal, or at the end of a logical driving route.
- Adequate insurance as determined by BC Ferries for all components of their business.
   BC Ferries must be added as an additional" named insured" with a copy of the insurance supplied to the Company prior to commencement of sales.
- A net rate that is lower than the published prices.
- Daily room availability.
- Minimal number of pricing seasons with no weekend, holiday or event surcharges.
- Accept payment terms of net 45 days from receipt of invoice.
- Allow BC Ferries to obtain a daily/nightly block of services with agreed upon release dates.
- Adhere to a maximum response time of 12 hours to all BCFV inquiries.
- For accommodations, there must be a private restroom in each guest's room.
- Provide BC Ferries with high-quality product and service imagery for unlimited use by the Company.
- BCFV will evaluate market-ready packages that include multiple services as long as they fulfill the other requirements and consist of one contract and one invoice for the entire package (e.g. accommodation, transportation and meals).

If a prospective supplier can meet the above criteria, the properties or services are inspected and graded, and a determination is made as to the suitability for inclusion into the existing product line. Suppliers who do not meet these standards, or who have ongoing service or product issues are discontinued from the supplier list. BCFV currently works with 85 properties, 12 attractions, two excursion companies and five transportation companies. New suppliers are only added when demand or business strategy dictates. Having the right amount of suppliers ensures that both BCFV and the supplier are achieving their business goals. Contracting too many suppliers in one category or destination would dilute business, eroding BCFV's ability to negotiate room block and favourable pricing.

It is the goal of BCFV to have at least one package available in all of the destinations that BC Ferries services. However, as previously stated, in some regions, there is either no market-ready product that is suitable or the accommodation provider chooses not to participate in the BCFV program as it doesn't fit their business needs. Consequently, expansion in some BC Ferries service areas is somewhat limited. In 2014, the product line expanded to include the Okanagan after consumer feedback showed it is one of the top two destinations they want to visit. This product line offers a new option to Vancouver Island residents and provides an alternative route option for completing the Inside Passage Circle Tour package.

### **Future Growth Plans**

Future plans may include the Rockies (Banff, Jasper and Calgary), which will allow marketing to both Alberta (inbound) and Vancouver Island (outbound) markets. In addition, the Rockies provide another option to 'add on' to the Inside Passage Circle Tour, rather than returning through Whistler or the Okanagan. This addition will increase the average package sale, increasing revenues and discretionary spend. In future, the business may also consider adding air and rail travel as secondary transportation options for customers who wish to travel on the ferry without their vehicle.

## Travel Consultant Production and Distribution Channels

BCFV is the call-to-action for marketing initiatives developed by the Company, and in some cases is also the call-to-action for cooperative marketing programs with regional destination marketing organizations (DMOs) and private sector partners. Consumers can book on the web (bcferries.com/vacations) on the phone (1-888-223-3779,\*3), send an email or walk into the Vacations Centre located in downtown Vancouver. Reservations are handled by a small team of trained travel consultants who are focused on providing the customer with relevant, well-priced vacation options and exceptional service.

Eighty-five percent of all bookings are handled by the travel consultants (Vacations Centre, On-Request and the 1-800 number). Currently, the average yearly gross sales by travel consultants are approximately \$450,000 - \$500,000 per year. The maximum achievable depends on several factors:

- Volume of calls, web requests and walk-in guests
- · Average length of each call and complexity of package
- Availability of travel consultants

Each year, a detailed budget is developed as part of the annual business planning process. Each travel consultant has specific daily, weekly, monthly and yearly targets for which they are accountable.

### **Incremental Ridership**

According to the 2013 Annual Customer Satisfaction Tracking (CST) survey conducted for the Company by Mustel Group, 74 percent of all surveyed passengers travel for purely discretionary personal reasons, with 41 percent residing in the Metro Vancouver region.

	F11	F12	F13	F14	F15 YTD  (at Dec. 31)
BC Ferries Passengers - All Routes - booked on a Vacations Package	11,567	18,054	21,805	25,110	27,532

## **Business Results**

BCFV revenues and expenses are captured as part of the overall financial reporting for the Company; however, in order to ensure accountability, a separate Profit & Loss ("P&L") statement is also generated for the business unit to assist in the ongoing analysis of key performance metrics.

The P&L statement contains all expenses that pertain directly to the operation of BCFV that would not exist if the business was not in operation. The Company's goal is to drive discretionary travel and increase incremental revenue streams. Corporate services that would exist without the BCFV division are not charged as an expense unless it is a direct requirement by BCFV. For example, payroll services are not charged as an expense, but incremental support to implement hotel reservation (Travelink) software is. The statement also contains all revenue generated through the sale of packaged vacations and/or components, as well as all revenue generated through the Vacations Centre.

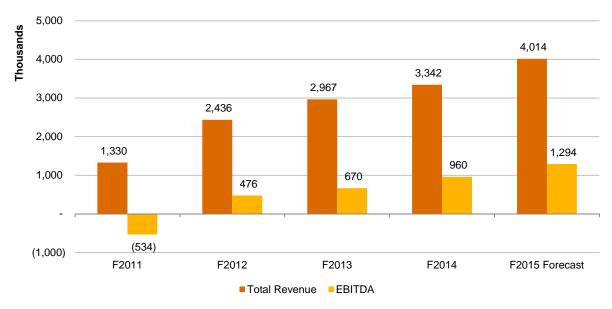
BCFV gross and net revenue expectations have exceeded the initial targets set out in the original five-year business plan. BCFV has achieved a 151 percent growth in revenues in the last four years, while expenses have declined 45 percent from the first year.

Since the service began in fiscal 2011 it has generated \$13.6m in revenue. Commencing November 2013, an online booking engine was introduced which has provided incremental sales without eroding voice sales. Simple one and two night packages are offered on the web for customers who want to self-serve, while multi-port and multi-designation packages remain as a "call to book" due to the complexity of the product.

BCFV revenues and earnings before interest, taxes, depreciation and amortization ("EBITDA") have increased each year since its inception in fiscal 2011. Figure 1 illustrates the financial results of BCFV, including projections for fiscal 2015 based on the most recent available data.

Figure 1





#### **BCFV Highlights**

#### BCFV highlights include:

- Over 100 packages available to choose from with more than 120 accommodation and activity partners
- 60 percent of Vacations Centre visitors are Vancouver locals, 40% are from Europe, the United States and Asia
- 98 percent of all vacations include travel by car
- Packages sold to major routes make up 75 percent of volume
- Northern routes account for 19 percent of volume
- All other routes represent remaining 5 percent of volume

#### Since Opening:

- 45,263 people have visited the Vacations Centre, with the top inquires being about vacation packages and ferry reservations
- 90,000+ incoming phone calls
- 2 million web visits
- 175,000+ quotes made
- 25,000+ packages sold
- 66,000+ passengers have travelled on a BCFV package
- \$13.5 million Total Revenue achieved

Sales are expected to continue to improve as the BCFV brand gains more recognition in both the local and short-haul markets. Additionally, the implementation of a robust commercial strength e-commerce platform for BC Ferries will assist in growing revenues for BCFV along with BC Ferries' other ancillary services.

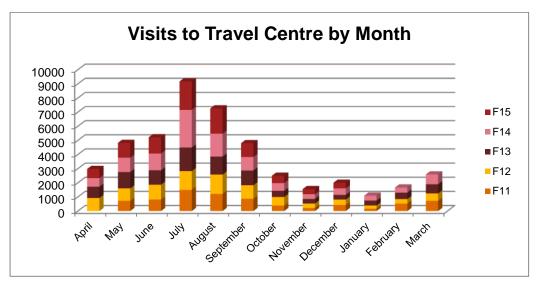
## Target Market, Demographics, Customer Satisfaction Scores

BCFV's target market is primarily the British Columbia regional and short-haul markets. Generally, the customer demographics are closely aligned with those of BC Ferries. It is almost an even split of male to female, with an age range of 30-60 years. BCFV statistics show that 85 percent of its customers are adults, 8 percent are seniors and 7 percent are children. Customers are generally looking for unique getaways ranging from one to five nights.

BCFV customer demographics are tracked in a number of ways. Visitors to the Vacations Centre are recorded on a daily basis along with the reason for the visit and their area of origin. Convention and cruise ship business is monitored to assist with determining appropriate staffing levels by day, week and season. April through September represent the busiest months at the Vacations Centre and correspond

to warmer weather patterns and the Vancouver tourist season. Visitors to the centre increased by 14 percent in fiscal 2014.

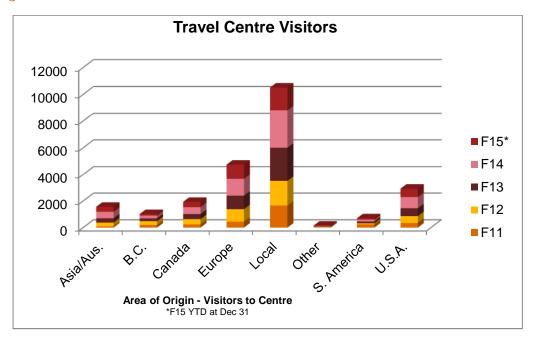
Figure 2



(Fiscal 2015 Year to date as of December. 31, 2014)

Customers are predominantly locals from the lower mainland (45 percent), but during convention days and tourist season, visitors come from around the world. Europe, the United States and Asia are the top three areas of origin, after Canada.

Figure 3



Top reasons to visit the Vacations Centre in fiscal 2014 included: inquiries on booking packages, BC Ferries' schedules, retail and gift certificate purchases, ferry tickets, reservations, and directions. Many of BCFV's international guests make inquiries or book packages for a return trip to British Columbia, when they can bring their families back and have more time to explore the province.

Figure 4

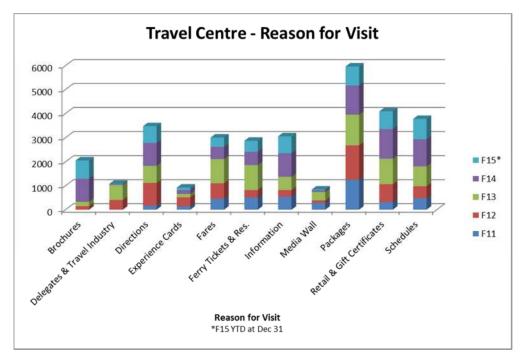
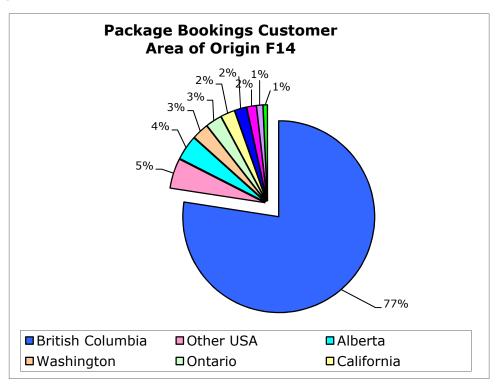


Figure 5



When looking at all customers who have booked a package (all channels), there is a slightly different area of origin. Fully 75 percent of customers are residents of British Columbia who book a one- or two-night getaway. The average number of nights is trending at 2.5 room nights per package. United States customers in fiscal 2014 represented 11 percent of the total, with Washington and California at three percent each and all other American states making up the remaining five percent. Alberta residents make up just over four percent of customers who booked.

Customer Satisfaction scores have been consistently high for BCFV, as measured by ResponseTec. Customers who have utilized the service find it convenient and the vacation options presented provide good value.

Customer Satisfaction Scores (Response Tec)			
Year	Overall - BCFV		
F14	82%		
F13	87%		
F12	79%		
3 Yr Average	83%		

Although BCFV has exceeded expectations since inception, there are several challenges affecting the business including: limited hotel inventory; a lack of market-ready products; and no new inventory development in key areas like Haida Gwaii, Port Hardy and Prince Rupert. Furthermore, BC Ferries is not on pace with industry trends in technology like mobile apps for booking travel and use of smart phones for travel redemption. BCFV consistently received negative customer feedback about this specific issue.

## **Conclusions**

Our main conclusions regarding the analysis are as follows:

- BCFV is meeting its intended goals. The business case for the service appears to be relatively strong given the consumer takeup since inception and the high level of participation by partners.
- BCFV gross and net revenue expectations have exceeded the initial targets set out in the original five-year business plan. BCFV has achieved a 151 percent growth in revenues in the last four years, while expenses have declined 45 percent from the first year.
- The contribution and costs of a centrally located service centre in downtown Vancouver relative to another central location in either Vancouver or Victoria do not appear unreasonable. The benefits and costs of locating the Vacations Centre in its current downtown location are difficult to assess, as the store-front location contributes to general marketing and many information requests lead to follow-on sales, some of which become part of general tariff and reservation revenues. While a greater takeup of the Vacations Centre services is by Lower Mainland residents than by out-of-province visitors, direct costs for labour and store front space of the downtown Vancouver location appear reasonable.
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  in excess of their best tour operator customers.
- BCFV has yet to reach a mature state. It has the potential to expand further with self-serve options as the new on-line reservation system is further developed.