



BRITISH COLUMBIA
FERRY COMMISSION

ORDER
NUMBER: 12-02

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IN THE MATTER OF

Section 40 of the *Coastal Ferry Act*, S.B.C. 2003, c.14
and
Final Decision on Price Caps for Performance Term 2013-2016

BEFORE: Gordon Macatee, BC Ferries Commissioner
Sheldon Stoilen, BC Ferries Deputy Commissioner

ORDER

WHEREAS:

- A. The commissioner issued a preliminary decision on March 31, 2011 regarding price caps for the third performance term commencing April 1, 2012 and ending March 31, 2016, as required under section 40(2) of the *Coastal Ferry Act* (the "Act");
- B. Under Bill 14 (*Coastal Ferry Amendment Act*, 2011), the Province of British Columbia ("the Province") set the price caps for the first year of the third performance term at 4.15 per cent for all route groups. Bill 14 also mandated the commissioner to conduct a review of the Act and to submit a report to the Minister of Transportation and Infrastructure (the "Minister") containing recommendations to amend the Act to better enable the balancing of the interests of ferry users with the financial sustainability needs of the ferry operator. After extensive public consultations in all coastal communities served by British Columbia Ferry Services Inc. ("BC Ferries") and consideration of over 200 written submissions, the commissioner submitted his report to the Minister on January 24, 2012 containing 31 recommendations to improve the regulatory process;
- C. Effective June 25, 2012, the Province further amended the Act pursuant to Bill 47 (*Coastal Ferry Amendment Act*, 2012) with new provisions which must be reflected in the final decision on price caps for the final three years of the third performance term including:

- (1) defines that the primary role of the commissioner is to balance, in the manner the commissioner considers appropriate, the interests of ferry users, taxpayers and the financial sustainability of ferry operators;
- (2) allows cross subsidization of ferry routes;
- (3) requires the commissioner's approval of capital plans and major capital expenditures, and allows the commissioner to decide what level of capital expenditure would trigger a requirement for approval by the commissioner;
- (4) requires that the price cap, when combined with all other price caps applicable to all route groups, must allow for a financial return sufficient to enable the operator to meet its debt obligations and maintain access to reasonable borrowing rates;
- (5) permits the commissioner to authorize the ferry operator to establish fuel deferral accounts in relation to one or more route groups, and to establish terms and conditions for the use of any fuel deferral account;

D. BC Ferries and the Province have amended the Coastal Ferry Services Contract ("the CFSC") to provide for increased service fees as follows:

- (1) Contract Year 2012/13 – \$148,573,268;
- (2) Contract Year 2013/14 – \$136,750,783;
- (3) Contract Year 2014/15 – \$135,811,395; and
- (4) Contract Year 2015/16 – \$135,072,971.

CFSC was also amended to allow for the amalgamation of Route 3 (Horseshoe Bay-Langdale) with the major routes;

E. The Province provided the increases to service fees with certain conditions including:

- (1) required efficiency improvements on the part of BC Ferries which would contribute an additional \$15 million over Performance Term Three ("PT3"); and
- (2) required service level adjustments which would contribute \$30 million towards lower price caps in PT3 for all routes. Of the \$30 million in service level adjustments, \$4 million is to come from service level adjustments to Routes 1, 2 and 30. Clause 38(1) of the amended CFSC states there will be no reduction in maximum service fees as a result of service adjustments;

F. The Province paid to BC Ferries the sum of \$25 million as contributed surplus at the end of the second performance term to support the financial sustainability of BC Ferries;

- G. The commissioner is required under the Act to make a final decision on or before September 30, 2012 regarding price caps for the final three years of PT3 commencing April 1, 2013 and ending March 31, 2016;
- H. At the end of the second performance term, gaps of varying magnitude existed between the allowed price caps and actual weighted average tariffs for each route group (the “Price Cap Gaps”). Furthermore, Bill 47 made fundamental changes to the regulation of ferry fares and the rules for the price cap model. These circumstances make continuation of existing calculated indexes less meaningful going forward.

NOW THEREFORE the commissioners order that:

1. **Price Caps**

In consideration of the amendments to the Act and the CFSC, including the provision for service level adjustments, and the efficiency targets identified herein, the price cap indexes for all route groups will be increased as follows:

- (1) April 1, 2013 – 4.1 per cent;
- (2) April 1, 2014 – 4.0 per cent; and
- (3) April 1, 2015 – 3.9 per cent.

2. **Fuel Deferral Accounts**

Fuel deferral accounts will be addressed by a separate order.

3. **Financial Return**

For purposes of section 41(2)(b) of the Act, the commissioner has established price caps with the intention of allowing the ferry operator to achieve by the end of the third performance term equity not lower than 17.5 per cent of total capitalization and a Debt Service Coverage Ratio (“DSCR”) of 2.5 or higher.

4. **Price Cap Index**

The index for each route group will be recalculated and set to an index level of 100 as of April 1, 2012 based on the weighted average tariffs that existed as of March 31, 2012.

5. **Efficiency Target**

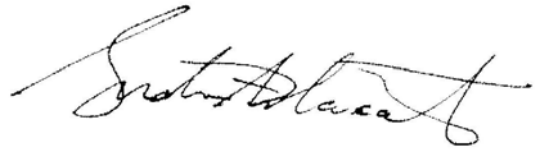
BC Ferries is required to achieve at least \$15 million in operating cost reductions or productivity gains during PT3 in addition to an annual cost reduction of \$9.8 million which BC Ferries has previously agreed to in its submission to the commissioner dated April 30, 2011 in connection with the preliminary price cap decision for a total efficiency target of \$54.2 million over the four years of PT3.

6. **Service Level Adjustments**

The price caps have been determined based on the expectation that the CFSC will be amended by June 30, 2013 to implement service level adjustments to achieve net savings of \$30 million during PT3. If the CFSC is not amended by June 30, 2013, or the amendments will not enable BC Ferries to achieve the target of \$30 million in net savings, BC Ferries may apply for relief under Section 42 of the Act.

DATED at Victoria in the Province of British Columbia, this 30th day of September 2012.

BY ORDER

A handwritten signature in black ink, appearing to read "Gordon Macatee".

Gordon Macatee
BC Ferries Commissioner

A handwritten signature in black ink, appearing to read "S. Stoilen".

Sheldon Stoilen
BC Ferries Deputy Commissioner