

**BC Ferry Commission
MEMORANDUM 32**

To: Mr. Rob Clarke
Executive Vice President and
Chief Financial Officer, BCFS

From: Martin Crilly
BC Ferry Commissioner

Date: January 26, 2009

Re: Feasibility Costs and Risk for the Cable Ferry Project

This Memorandum 32 responds to your letter of January 19 on the same subject, which is attached.

I confirm the understanding set out in your letter.

A handwritten signature in black ink, appearing to read 'M Crilly', is positioned below the text of the memorandum.

Attachment:
Your letter of January 19 2009

January 19, 2009

Mr. Martin Crilly
British Columbia Ferry Commissioner
PO Box 1497
Comox, BC.
V9M 8A2

Dear Mr. Crilly:

SUBJECT: Feasibility Costs and Risk for the Cable Ferry Project

I am writing to follow up on our November 19, 2008 meeting regarding the recovery of costs for the cable ferry feasibility project.

As discussed, the project involves a material level of effort and spending to take place in PT2 in order to determine whether economic savings can be achieved for PT3 and beyond. Recognizing the risks associated with the timing implications of setting price caps in advance for four-year performance terms, British Columbia Ferry Services Inc. (BC Ferries) and the British Columbia Ferries Commissioner (Commissioner) have agreed on the following principles: If the feasibility project leads to implementation of a cable ferry, BC Ferries is entitled to recover all of its costs, including the feasibility project costs, over the associated assets' useful lives and to earn 50% of the savings (versus the application of conventional service) during PT3; If the feasibility project does not lead to implementation of a cable ferry, BC Ferries is entitled to recover 50% of the external feasibility project costs over PT3.

Without prejudice to the principles above, the implications for accounting and price cap determination will be as follows:

1. If the feasibility project results in implementation:
 - o all external feasibility costs will be capitalized thus forming part of the capital structure of the company, for which BC Ferries is entitled to make a full recovery plus earn its rate of return,
 - o the minor route group price cap for PT3 will be set such that BC Ferries would effectively retain 50% of the PT3 cost savings resulting from the implementation of the cable ferry.

2. If the feasibility project does not result in implementation:
 - o 50% of the external feasibility project costs will be treated as a regulatory asset to be recovered through a deferral account mechanism, with the remainder of costs being expensed at the time it is decided to not proceed with implementation of a cable ferry,
 - o the deferral account balance will be recovered over the four year period of PT3 through the inclusion of these costs in determination of the PT3 price caps.
3. Prior to a determination of whether or not the project will result in implementation of a cable ferry, BC Ferries will account for the external feasibility project costs incurred as capital assets (construction-in-progress).

BC Ferries is prepared to accept the terms as outlined above, and requests confirmation of the same from the Commissioner.

Thank you.

Sincerely,



Rob Clarke
Executive Vice President
& Chief Financial Officer

cc: Sheldon Stoilén, Deputy Commissioner
William Cottick, Executive Vice President Corporate Affairs & General Counsel
Cynthia Lukaitis, Vice President & Corporate Secretary
Sheldon Schmidt, Manager, Business and Economic Regulatory Affairs