

British Columbia Ferry Commission



Reasons for Determinations Regarding A Fuel Price Deferral Mechanism

**in the matter of Order 12-03 under
Section 41.1 of the Coastal Ferry Act, S.B.C. 2003, c. 14**

30 September 2012

British Columbia Ferries Commissioner
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1 Overview

Background

During the latter stages of the first performance term, which ended on March 31, 2008, British Columbia Ferry Services Inc. (BCFS) experienced significant volatility in the price of fuel. BCFS responded initially by applying under section 42 of the *Coastal Ferry Act* (prior to Bill 47) for a price cap increase due to the extraordinary increase in the price of fuel.

Due to further increases and the expectation of further volatility the Commission authorized a mechanism under Memorandum 24 to address the issue of continued volatility and avoid delays caused by additional section 42 applications from BCFS. The mechanism was modified under Memorandum 24A and subsequently Memorandum 24B to allow BCFS greater flexibility in addressing fuel price volatility.

Under this mechanism, BCFS charges only a “set” price per litre for fuel consumed in its operations. Actual prices above or below the set price, which is established by the commissioner, are recovered or refunded by way of fuel surcharges or rebates.

For the second performance term, which commenced on April 1, 2008 and ended on March 31, 2012, the Commission incorporated the Mechanism 24B into the final price cap decision published on September 30, 2007.

In his report on the preliminary price cap decision dated March 31, 2011 for the third performance term, which commenced on April 1, 2012, the commissioner stated that “the commissioner has decided to continue to permit the use through PT3 of fuel cost deferral accounts for regulatory purposes.”

Subsequent to the preliminary price cap decision on March 31, 2011, under Bill 41, the Province mandated the commissioner to undertake a six-month review of the *Coastal Ferry Act* and to submit recommendations to the Minister of Transportation and Infrastructure to better enable the commissioner to balance the interests of ferry users (taxpayers) and the financial sustainability of the ferry operator. Bill 14

also deferred the final decision on price caps for the third performance term for one year to September 30, 2012.

Coastal Ferry Act Amended

As part of his recommendations for changes to the Coastal Ferry Act, the commissioner recommended that the Act should explicitly empower the commissioner to authorize the use of fuel deferral accounts. This recommendation was accepted and under Bill 47, which came into force on June 25, 2012, the Act was amended by adding section 41(1) which explicitly provides for fuel deferral accounts.

In anticipation of Bill 47 coming into force, BCFS submitted an application dated June 21, 2012 for a fuel price deferral mechanism. The commissioner posted the application on his website on June 28, 2012 and invited public comments by July 29, 2012.

This paper summarizes BCFS' application for such a mechanism, the commissioner's determinations and reasons and comments received from the public.

2 Governing Legislation

Amended Legislation

On May 31, 2010, Royal Assent was given to Bill 47 amendments to the *Coastal Ferry Act* of 2003 and came into force by Regulation on June 25, 2012.

Section 41 of the amended Act provides as follows:

1. The commissioner may
 - a. require a ferry operator to establish a fuel deferral account in relation to one or more route groups, and
 - b. establish terms and conditions for the use of any fuel deferral account established by the ferry operator.
2. The commissioner may, on any conditions the commissioner may specify,
 - a. allow a ferry operator to add a temporary fuel surcharge, or
 - b. require the ferry operator to provide a temporary discount, to reflect fluctuations in the fuel deferral account for any period.

3 Commissioner Determinations and Reasons

Establishment of a fuel price deferral mechanism

In anticipation of the new provision for fuel deferral accounts, BCFS submitted an application dated June 21, 2012 to the commissioner proposing the establishment of a fuel price deferral mechanism.

In its application, BC Ferries submits that the proposed fuel price deferral mechanism is consistent with regulatory principles and industry practice and advances the following principles:

- (a) fairness and equity for both ferry users and BC Ferries by ensuring that actual fuel costs are recovered from ferry users over time;
- (b) fare stability and predictability enhanced through the use of surcharges and rebates;
- (c) transparency and accountability with BC Ferries having the ability to manage fuel deferral account balances at its discretion subject to certain conditions.

Commissioner Determination

The commissioner agrees with BCFS that a fuel price deferral mechanism is consistent with regulatory principles and industry practice and generally would advance the above principles. Fairness and equity is ensured for ferry users, taxpayers and BC Ferries by ensuring the risk of fuel price is borne by the ferry users. Fare stability is accomplished by establishing price caps for the entire third performance term without an attempt of forecasting fuel prices out into the future. The only variant would be fuel surcharges or rebates as a result of differences in the actual price of fuel and the set price of fuel. Transparency and accountability is ensured by monthly reporting to the commissioner of fuel deferral account balances and oversight by the commissioner of BC Ferries' fuel management practices.

Establishment of fuel deferral accounts

In its application BCFS respectfully requested the following approvals and orders in connection with the establishment of fuel deferral accounts:

1. An order pursuant to section 41.1(1)(a) of the *Coastal Ferry Act*, permitting BCFS to establish a single fuel deferral account for all route groups, as described in the Application (the “Fuel Deferral Account”) effective the date of this Order. The commissioner may consider further sub-divisions of the Fuel Deferral Account from time to time.
2. An order pursuant to section 41.1(1)(b) of the *Coastal Ferry Act*, approving the following terms and conditions for the use of the Fuel Deferral Account by BCFS:
 - a. the balances from the existing deferral accounts for all route groups as of the date of this Order, together with all excluded variances under the bandwidth from the start of the current Review Performance Term, will be recorded in the Fuel Deferral Account;
 - b. the set price for fuel will be as specified by the commissioner;
 - c. all variances between the set price for fuel and the delivered price for fuel will be recorded to the Fuel Deferral Account;
 - d. the Fuel Deferral Account balance will be reported to the Commissioner on a monthly basis in the form similar to the present reporting, and in a manner that is consistent with applicable securities laws regarding disclosure of information; and
 - e. interest will be charged/credited on the Fuel Deferral Account balance, calculated in the manner described in the Application.

Commissioner Determinations

The commissioner’s determinations are as follows:

1. The commissioner does not agree with the establishment of a single fuel deferral account in view of the provision in the amended Coastal Ferry Services Contract whereby the Province covers a portion of any fuel surcharges on routes 10, 11 and 40. Accordingly the establishment of at least two fuel deferral accounts

is authorized for routes 10, 11 and 40 and the other for all other routes.

2. The commissioner authorizes the above terms and conditions except for the following:
 - a. all variances between the set price for fuel and the delivered price of fuel will be recorded in the applicable Fuel Deferral Account for reasons stated above;
 - b. balances for all fuel deferral accounts will be reported to the commissioner on a monthly basis;
 - c. there will be no interest charged or credited on Fuel Deferral Accounts. This symmetry is considered by the commissioner to be fair and equitable to the ferry users and BC Ferries and does not create an incentive nor a disincentive for BC Ferries' in their management of the Fuel Deferral Account balances.
3. An order pursuant to section 41.1(2)(a) and 41.1(2)(b) of the *Coastal Ferry Act* approving the following conditions for the use of temporary fuel surcharges and temporary discounts:
 - a. BCFS may implement, adjust or remove fuel surcharges or rebates at any time and in its discretion, subject to the following conditions:
 - i. if the month end balance in the Fuel Deferral Account is a debit balance which exceeds X% of the annual pre-surge tariff revenue ("the X% trigger") for all route groups combined, BCFS will adjust the fuel surcharge to target the elimination of the Fuel Deferral Account debit balance, including the expected growth in the balance, over the following 12 months;
 - ii. if the month end balance in the Fuel Deferral Account is a credit balance which exceeds the X% trigger, BCFS will have a grace period of one quarter to reduce the credit balance below the X% trigger;
 - iii. BCFS shall ensure that the balance in the Fuel Deferral Account reaches \$0.00 (zero dollars) at least once every 24 months; the time period within which BCFS is required to zero the balance of

*Terms and conditions
for fuel deferral
accounts and for
temporary surcharges or
rebates*

- the Fuel Deferral Account shall be reset each time the deferral account balance reaches \$0.00;
- iv. surcharges and credits will be applied as a percentage of fares equally across all routes; and
 - v. fuel surcharges applied by BCFS cannot exceed a maximum of 15% of a fare in effect for a route, except as required to comply with (a)(i) above.
- b. BCFS shall provide 15 days public notice of any increase in fares that results from:
- i. the imposition of a fuel surcharge;
 - ii. an increase in a fuel surcharge;
 - iii. the removal of an existing rebate; or
 - iv. a decrease in the amount of an existing rebate.

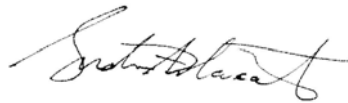
Commissioner Determinations

The commissioner has approved the above terms and conditions for the use of temporary fuel surcharges with the following modifications:

- The trigger in (a)(i) is set at 2% to allow BC Ferries some flexibility while still holding them accountable for managing the fuel deferral accounts. Together with (a)(iii) above this will prevent large balances to accumulate which may not be in the interests of ferry users or taxpayers.

The commissioner has determined it to be reasonable to allow BC Ferries a grace period of two quarters to reduce the credit balance below the 2% trigger. BC Ferries has suggested due to accounting and implementation delays it may be challenging to reduce credit balances over a grace period of only one month if fuel prices decline dramatically.

For (a)(v) above the commissioner has determined a maximum of 10% shall apply to fuel surcharges - 15% is deemed to be excessive when applied to some of the minor routes in particular and further justification should be required to exceed the 10% maximum.



Gord Macatee
BC Ferries Commissioner



Sheldon Stoilen
BC Ferries Deputy
Commissioner

September 30, 2012