



May 3, 2021

Ms. Jill Sharland
Vice President & Chief Financial Officer
British Columbia Ferry Services Inc.
Suite 500, 1321 Blanshard Street
Victoria, BC V8W 0B7

Dear Ms. Sharland:

This is in response to your letter of April 22, 2021, that outlined the recommended approach to report on the funding for Fare Increase Relief provided to BC Ferry Services Inc. ("BC Ferries") under the Safe Restart Contribution Agreement.

The Commissioners recognize that BC Ferries received \$24 million in Fare Increase Relief in lieu of increasing fares in fiscal year 2021 and to further limit fare increases to 2.3% for the remainder of Performance Term 5.

The Commissioners agree that the recommended Funding Drawdown approach would result in more accurate and timely reporting than allocation on the basis of historic traffic, especially in these uncertain times. We can therefore confirm that:

1. The Fare Increase Relief funding should be treated as regulated revenue under the Price Cap; and
2. For reporting purposes during Performance Term 5, the \$24 million will be drawn down quarterly by increasing actual regulated revenue by 2.3% (annualized) or by the remaining balance of the Fare Increase Relief funds.

Sincerely,

A handwritten signature in blue ink that reads "S. T. Stoilen".

Sheldon Stoilen
BC Ferries Commissioner



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April 22, 2021

Mr. Sheldon Stoilen
British Columbia Ferry Commissioner
BC Ferry Commission
PO Box 9279 Stn Prov Gov
Victoria, BC V8W 9J7

Dear Mr. Stoilen:

RE: Price Cap Reporting of Safe Restart Funding

We are writing to propose how to recognize the portion of the Safe Restart Funding earmarked for fare increase relief as regulated revenue by British Columbia Ferry Services Inc. ("BC Ferries" or the "Company") for the purposes of Price Cap Reporting during Performance Term Five (April 1, 2020 to March 31, 2024) ("PT5").

In light of the global coronavirus pandemic, BC Ferries chose not to increase fares in F2021. This decision was taken with the understanding annual fare increases would be implemented over the remaining three years of PT5, resulting in average in-market fares by Fiscal 2024 consistent with the allowable Price Cap increases over the four years of PT5.

Following the onset of COVID-19, a joint task force was formed with the Province of British Columbia (the "Government" or the "Province"), to understand the impact of the pandemic and work towards a recovery plan, including government funding, aimed at protecting the service and the financial sustainability of the ferry system. To understand the financial impact of COVID-19, it was assumed BC Ferries was to have exited PT5 at the allowable price cap index prior to the pandemic.

On November 11, 2020, a Contribution Agreement (the "Agreement") was reached between the Province and BC Ferries under the Federal Government's "Safe Restart" program providing \$308 million in funding to provide:

1. Base Operating Relief;
2. Fare Increase Relief; and
3. Discretionary Sailing Relief.

The Fare Increase Relief component of the Contribution specified \$24 million (the "Fare Increase Relief Funding") to compensate BC Ferries for limiting the "average annual public fare increases" over the last three years of PT5 to the level of the annual price cap increases in those years. The Agreement also specifies in Schedule 1, that there is a 0% "average annual fare increase" in F2021.

Consistent with similar government funding initiatives (the PT4 Fare Initiative and Social Programs Funding), BC Ferries believes the Fare Increase Relief Funding should be treated as regulated revenue under the Price Cap.

Proposals for Recognizing the Funding as Regulated Revenue

Recognizing Fare Increase Relief Funding as regulated revenue would be consistent with price cap reporting to the Commissioner (the "Commissioner Reporting"), and the intent of the Fare Increase Relief Funding under the Contribution Agreement.

A retrospective approach to allocating the Fare Increase Relief Funding, applied at the end of PT5, would be consistent with the allocation method used for the PT4 fare initiative funding. While, consistent with Commissioner Reporting, it hinders BC Ferries ability to provide required quarterly Agreement Reporting inclusive of the Funding. This requirement therefore precludes using the retrospective approach for PT5.

In place of the retrospective approach, BC Ferries is proposing two options to recognize the Fare Increase Relief Funding. These are to:

1. prospectively allocate it across fiscal years 2022 – 2024, or
2. to draw it down by 2.3% of actual revenue each quarter from fiscal 2022 to fiscal 2024.

1. The Prospective Approach

The prospective approach would allocate the Fare Increase Relief Funding to each quarter of fiscal years 2022 – 2024 based on a traffic and revenue forecast, using either the medium – case traffic scenario depicted in the Agreement (the "Agreement Scenario"), or the first update to the long term forecast also stipulated in the Agreement.

The prospective approach would allow Reporting during PT5 that was inclusive of the Funding. However, as the Funding allocation would be based on an historical forecast, reported results could differ from actual results. Traffic pattern variations from whichever forecast used could introduce Price Cap results that may be significantly over or under the cap due to the allocation of the funding across the year, route groups, and traffic types.

Overall, the prospective approach poses significant challenges as it introduces a rigid amount of funding into a dynamic Price Cap model.

2. The Funding Drawdown Approach

Under the funding drawdown approach, actual regulated revenue would be increased each quarter by the lesser of 2.3% or the remaining balance of the Fare Increase Relief Funding. The balance of the Fare Increase Relief Funding would then be drawn down by the amount regulated revenue was increased.

This approach would allow for the Fare Increase Relief Funding to be included in the ongoing Price Cap reporting during PT5. Unlike the prospective approach, it would also create a link between actual traffic and the Fare Increase Relief Funding. In addition, this approach would have a much smaller chance of creating a Price Cap underage, as this could only occur if the Fare Increase Relief Funding was not fully drawn before the end of the performance term.

Overall, the funding drawdown approach provides a dynamic Funding Allocation mechanism into a dynamic Price Cap model.

Recommendation

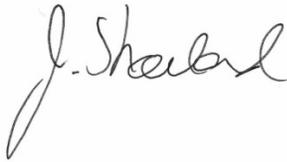
BC Ferries' recommends recognizing the Fare Increase Relief Funding as regulated revenue applying the drawdown approach, as it allows for both Price Cap compliance reporting and Contribution Agreement performance reporting during PT5 that is inclusive of the Fare Initiative Relief Funding, and provides results that are best linked to actual traffic, minimizing allocation distortions.

Summary

BC Ferries is proposing:

- A. Recognising the \$24 million specified as Fare Increase Relief in the Safe Restart Contribution Agreement as Regulated Revenue in Fiscal Years 2022 – 2024 and allocating these funds across the fiscal years based on the drawdown approach.

Sincerely,



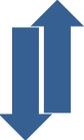
Jill Sharland
Vice President & Chief Financial Officer

cc: Eva Hague

APENDIX: Comparison of Options

Approach	Allows Ongoing Reporting	Risk of a False Positive Overage	Risk of a False Negative Overage	Reflects Actual Traffic	Potential Severity of Distortion	Risk of Missing an Overage	Risk of Missing an Underage
Prospective Funding Drawdown	Yes	Large	Small	No	Large	Moderate	Moderate
	Yes	Small	Small	Mostly	Small	Small	Small

Legend

Good  Bad	Yes	None
	Mostly	Small
	Partially	Moderate
	No	Large

Allows Ongoing Reporting: Price Cap Reporting during PT5 that is inclusive of Safe Restart Funding.

Risk of a False Positive Overage: The risk that the Price Cap Reporting during PT5 identifies an overage that is the result of the allocation approach, not of actual traffic.

Risk of a False Negative Overage: The risk that the allocation approach does not identify an overage that results from actual traffic in the Price Cap Reporting during PT5.

Reflects Actual Traffic: Approach allocates funding to actual traffic evenly replacing forgone revenue on a dollar for dollar and timing basis.

Potential Severity of Distortion: Worst case estimate of how far the allocation of funding could deviate from replacing forgone revenue on a dollar for dollar and timing basis.

Risk of Missing an Overage: The risk that the approach does not identify that BC Ferries was over the Price Cap and should have returned money to the customers through discounting.

Risk of Missing an Underage: The risk that the approach does not identify correctly a return to Price Cap compliance by BC Ferries such that more money was discounted to customer than was necessary to return to compliance.