



From the Executive Committee of the Islands Trust,

Submitted to the Honourable Judith Reid, Minister of Transportation
February 28, 2002

A Response to the Wright Report

("Review of BC Ferry Corporation and Alternative Uses for the Fast Ferries",
Prepared by Fred R. Wright, FCA, December 2001)

BACKGROUND

The Wright Report

In December 2001, B.C. Ferries released the "Wright Report", commissioned by the Board of BC Ferries. It was prepared by an independent financial consultant, Mr. Fred R. Wright of Capital West Partners.

In his report, Mr. Wright analyzes the governance structure, operating framework, historical financial performance, and current 15-year strategic plan of BC Ferries. He uses this analysis as the basis for making specific recommendations to the provincial government regarding the future operation and structure of BC Ferries.

In fiscal 2001, BC Ferries had a corporate shortfall of \$49 million. The Wright Report asserts that these overall losses result largely from operating losses on individual ferry routes. A number of the routes identified serve island communities within the Islands Trust Area.

Mr. Wright recommends that BC Ferries should increase revenues and reduce costs associated with minor ferry routes to improve financial performance and reduce losses. Specific recommendations in the Wright Report include:

Tendering to private operators for the provision of subsidized vessel and terminal services where routes are not commercially viable;

Increasing tariffs and/or rationalizing service levels to stimulate private sector participation;

Building fixed links to reduce or eliminate existing routes, particularly in the Southern Gulf Islands.

The Islands Trust Area



BC Ferries serves fourteen islands in the Islands Trust Area: Denman, Hornby, Gabriola, Thetis, Salt Spring, North & South Pender, Saturna, Mayne, Galiano, Bowen, Gambier and Keats. A private ferry subsidized by BC Ferries serves Lasqueti Island.

The 26 elected officials of Islands Trust Council represent fourteen island communities that depend upon BC Ferries service. In 1995, BC Ferries and the Islands Trust Council entered into a Protocol Agreement regarding ferry services in the Islands Trust Area.

The Province established the Islands Trust under the *Islands Trust Act* to protect the environment and communities of the Gulf Islands, not only for residents, but also for the entire province. The provincially approved *Islands Trust Policy Statement* expresses the provincial 'Object' in detail. It was developed following lengthy public and agency consultation and includes policies about ferry transportation.

Over the last 7 years, a significant number of Island Trustees from across the Trust Area have participated in BC Ferries Stakeholder Committees, and the Coastal Council of BC Ferries. BC Ferries has asked local trust committees and the Bowen Island Municipal Council for recommendations regarding membership in their local Stakeholders Committees.

On behalf of the Islands Trust Council, the Executive Committee has reviewed the Wright Report.

We find the Report unconvincing in a number of key areas. In response, we offer our own review, analysis and recommendations regarding ferry service in the Islands Trust Area.

GENERAL COMMENTS

1. The Wright Report's analysis and recommendations regarding the operating framework and financial performance of BC Ferries are narrow in scope and lack context.

Wright's failure to compare the financial performance of BC Ferries to equivalent components of the Province's transportation infrastructure reduces both the value and credibility of his recommendations. Equivalent transportation components include the Ministry Of Transportation's highway system and public transit systems such as the Greater Vancouver Transit Authority (Translink).

2. The Wright Report does not consider several critical factors such as:

Tax Contributions paid by ferry users to fund transportation infrastructure, including ferries;

Cross-traffic among major and minor ferry routes;

Elasticity of demand related to tariffs ("as fares go up, traffic goes down");

Direct and indirect socio-economic benefits to the Province related to ferry service.

3. We strongly disagree with the Wright Report's assertions that corporate shortfalls at BC Ferries stem from operating losses on the minor ferry routes that serve island communities.

On a system-wide basis, in fiscal 2001, the 25 BC Ferries routes and contract routes recovered all Direct Operating Expenses for vessels and terminals (labour costs, fuel, repairs, maintenance, insurance, utilities, taxes & other operating expenses) from Direct Revenue (tolls, catering, & other revenues). They generated a Direct Operating Net of \$35.6 million.

Current subsidies of \$95 million (the Federal Contract and Provincial 1.25 cent per litre Motor Fuel Tax) offset about 90% of the \$105 million allocated by BC Ferries for capital renewal of vessels and terminals in fiscal 2001.

Our review of relevant financial data reveals the following factors related to the \$49 million corporate shortfall for BC Ferries in fiscal 2001:

FACTOR	COST
Labour Costs for (Regional) and Corporate Management & Administration There is one corporate manager or administrator at BC Ferries for every 11 employees in the field. 11% of 3339 FTE's account for 15% of total labour costs. The average cost for each of 331 regional/corporate management and administrative employees is \$104,834, as compared with an average cost of \$66,290 for the 3008 employees who work in the operations side of the BC Ferries Corporation.	\$34.7 million
Corporate Overhead and Administration Expenses Free travel for employees and VIPs (estimated cost: \$ 3 million) Advertising & Professional fees (\$10.3 million) Communications & Computers (\$5 million)	\$18.3 million
Provincial Social Programs -- Free Passage BC Ferries bears the costs of "Social Program Free Passage" for seniors, medical patients, students, and persons with disabilities	\$7 million

FACTOR	COST
TOTAL	\$60 million

COMPARATIVE REVIEW OF BC FERRIES FINANCIAL PERFORMANCE (see Attachment 1)

We have reviewed and evaluated the most recent financial performance data for BC Ferries in comparison with equivalent components of the Province's transportation infrastructure. In particular, we have compared the following three Financial Performance Indicators with the Greater Vancouver Transit Authority (Translink), and the Ministry of Transportation's highway network:

FINANCIAL PERFORMANCE INDICATORS	BC FERRIES PERFORMANCE (OUR RATING)	BCFC	GVTA (TRANSLINK)	MoT
Cost Recovery Ratio Percentage of Direct Operating Expenses recovered from Direct Revenue (non-tax) sources	VERY HIGH (Excellent)	111.7%	55.9%	24.2%
Level of Subsidization Percentage of Total Revenues derived from taxation and other Direct Subsidies	RELATIVELY LOW (Acceptable)	21.8%	52.6%	73.8%
Corporate & Administrative Overhead Ratio Percentage of Corporate Overhead and Administration Expenses Relative to Total Operating and Capital Expenditures	VERY HIGH (Poor)	14.7%	3.5%	3.9%

RECOMMENDATIONS

We believe that BC Ferries can achieve improved financial performance if it implements the following recommendations.

The objective of these recommendations is to ensure that BC Ferries can:

Sustain itself on a "break-even basis";

Improve its operating and financial performance over the short, medium, and long term;

Provide safe, reliable, affordable, and cost effective public ferry services for the benefit of the residents of British Columbia, and the provincial government, at a level acceptable to the majority of British Columbia taxpayers.

Guiding Principles

1. The Province should recognize BC Ferries as an essential and integral part of the provincial transportation infrastructure, equivalent to public roads and transit. It should fund it accordingly.

Like the provincial network of public roads, highways, bridges, and transit systems, BC Ferries plays a critical role in BC's social fabric and overall economy. In a marine-based province such as British Columbia, public ferry transportation infrastructure should be considered equivalent to public road and other transportation infrastructure.

The Province's financial support for each of BC Ferries routes should be comparable to the level of funding that government would give to fund the equivalent length of public highway on a "cost per mile" basis.

BC Ferries should not be evaluated as a commercial enterprise.

2. The substantial financial contributions made by island and other coastal communities to BC Ferries' revenues and subsidies, through taxation and other means, should be factored into any evaluation of BC Ferries' financial performance.

Ferry users contribute to BC Ferries' \$22.4 million Federal Contract subsidy through their federal income taxes. They contribute to the \$72.5 million Provincial Motor Fuel Tax subsidy through their purchase of motor fuel. They also contribute to the funding of all forms of essential public transportation infrastructure in BC (including ferries, roads, and transit systems) through provincial income taxes, provincial rural taxes and regional district transit levies.

Ferry users and taxpayers from ferry-dependent communities reasonably expect the Province to use a portion of their tax contributions to fund the transportation links provided by public ferries in addition to other transportation infrastructure throughout the province.

- 2. BC Ferries' minor routes and contract services routes serve hundreds of thousands of British Columbians and tourists annually, in addition to the resident populations of island and coastal communities. Tourism and other "spin-off" benefits to the provincial economy from ferry travel must be taken into consideration in any plans to alter ferry services.**

The province should not measure the financial performance on BC Ferries minor routes and contract services routes on a "subsidy per capita basis", as suggested by the Wright Report. The resident populations and tourist economies of the Lower Mainland and Vancouver Island benefit greatly, both directly and indirectly, from the scenic and recreational amenities of the islands and other coastal communities they access through BC Ferries service. In peak seasons, less than a quarter of travelers on Southern Gulf Island routes are residents.

Ferry service in the Islands Trust Area and other coastal communities has "spin-off" economic benefits for the provincial economy, similar to those derived from funding of highways such as the "Sea-to-Sky" route that provides access to the Resort Municipality of Whistler.

Ferry access has helped to retain the unique character and appeal of the islands in the Strait of Georgia and Howe Sound, to the benefit of the residents of nearby urban centres, and the provincial tourist industry. Fixed links, such as those to the City of Richmond on Lulu Island, would destroy the very nature of B.C.'s coastal islands.

The provincial ferry system has provided the foundation for the social and economic development of the Trust Area Islands and other coastal communities for over forty years. "Altering ferry service levels, increasing tariffs, and building fixed links", as suggested in the Wright Report, would have far-reaching social and economic impacts. The Province should carefully assess the impacts, in consultation with stakeholders, prior to making changes to the delivery of BC Ferries and related transportation services.

*□ no island in the Trust Area should be connected to Vancouver Island, the mainland or to another island by a bridge or tunnel □
— the Islands Trust Policy Statement —*

An important and distinctive aspect of coastal British Columbia's "Quality of Life" would be lost forever if coastal island ferry services became too expensive through excessive tariff increases, if ferry services are reduced or eliminated, or if fixed links are used to access the coastal islands.

Financial Performance

- 2. BC Ferries' financial performance should be measured on a system-wide basis (like Highways and Transit). Direct Revenues at BC Ferries should cover the Direct Operating Costs of ferry routes on a system-wide basis, not on a route-by-route basis.**

'Cross-Traffic' going to and from minor ferry routes feed a significant portion of traffic on major ferry routes, as traffic on major urban bus routes, Skytrain, and Seabus feeds to and from minor suburban bus routes. Financial performance on one route cannot be accurately measured without considering influences within the entire system.

MAJOR ROUTE	MINOR FEEDER ROUTE(s)
Route 1 Tsawwassen – Swartz Bay	Southern Gulf Islands routes
Route 2 Horseshoe Bay – Departure Bay	Northern Gulf Islands routes
Route 3 Horseshoe Bay – Langdale	Earls Cove – Saltery Bay (Powell River) route Langdale – Gambier-Keats route

Alterations to service, schedules, and fares on individual minor routes will change service demand and financial performance on related major ferry routes.

- 2. Find efficiencies in the acquisition, operation, repair, and maintenance of vessels and terminals to reduce Direct Operating Expenses.**
- 3. Reduce Labour Costs for (Regional) and Corporate Management & Administration, and Corporate and Administration Overhead Expenses to bring them in line with similar costs for other transportation services.**

4. Should the Province wish to fund free personal travel for BC Ferries employees, VIPs, it should do so in a way that does not affect BC Ferries' 'bottom line'. Costs of 'social programs – free passage' should be attributed to the appropriate Provincial Ministry, and not reflected in BC Ferries' 'bottom line'.
5. Commuter discounts for frequent users of the ferry system are equivalent to transit passes and should be retained for the same socio-economic reasons.
6. Federal and Provincial subsidies given to BC Ferries should be used to offset infrastructure costs for capital replacement of vessels and terminals. The Motor Fuel Tax should continue and should be adjusted, if necessary, to offset projected annual capital replacement costs.

Provincial funding should be sufficient to ensure that BC Ferries does not need to borrow money to finance essential public transportation infrastructure.

BC Ferries has only been required to carry a debt for the last 10 years. During that period, annual debt servicing costs at BC Ferries have averaged about \$20 million per year. The 15-year strategic plan projects that BC Ferries' debt will increase from \$21 million to \$325 million between 2002 and 2016. Interest on projected debt is expected to average \$12 million per year.

Over the last 10 years, there have been serious problems with the BC Ferries due to political interference. The Fast Ferry initiative and the province's decision to make BC Ferries pay infrastructure costs through borrowing money, unfairly burdened BC Ferries with debt.

The Province rectified this situation somewhat by reassuming \$1.1 billion of the debt caused by provincial initiatives, and by giving BC Ferries the 1.25 cents per litre Motor Fuel Tax.

2. **The Province should listen closely to the recommendations of BC Ferries' Stakeholders Committees and the Coastal Council before making changes to the ferry system.**

BC Ferries Stakeholders Committees and the Coastal Council have volunteered thousands of hours to study BC Ferries and make recommendations to BC Ferries. Community members, commuters, business people, and local government representatives who regularly use and understand the ferry service sit on these committees.

Stakeholders have suggested many ways to reduce costs and improve financial performance at BC Ferries without reducing service or raising fares.

Most regular users of the ferry system agree that BC Ferries provides excellent ferry services to the people of BC most of the time. As with other forms of transportation, chronic problems can occur in meeting peak demands (commuter overloads, weekends and holidays). We believe most users accept this as part of the imperfect nature of transportation infrastructure.

The Islands Trust Object

"to preserve and protect the trust area and its unique amenities and environment for the benefit of the residents of the trust area and of British Columbia generally, in cooperation with municipalities, regional districts, improvement districts, other persons and organizations and the government of British Columbia"

-- the Islands Trust Act

Bowen Denman Gabriola Galiano Gambier Hornby Lasqueti Mayne North Pender Salt Spring South Pender Thetis

ATTACHMENT 1

(all figures in \$ millions)		BC Ferries Corporation source for figures used: Wright Report pgs. 17, 24, 33; BCFC 2000/2001 Annual Report pg.53 See also Attachment 2	Greater Vancouver Transit Authority (Translink) source for figures used: Consolidated Financial Statements of GVTA, December 31, 2000, pg.3	Ministry of Transportation & Highways source for figures used: Annual Performance Report 2000/2001, pgs. 18, 19
Direct Revenues		Tolls 292.806 Catering 41.770 <u>Other</u> 4.900 Total Direct Revenues 339.476	Transit Fares 208.250 Other 25.887 Pension Refunds 12.340 <u>Other</u> 3.652 Total Direct Revenues 250.129	Highway Tolls 42.181 Fines & Penalties 76.378 <u>Other</u> 2.432 Total Direct Revenues 120.991
Direct Operating Expenses		Vessel Labour 125.254 Fuel 52.767 Vessel Refit & Maintenance 56.568 Marine Insurance 2.524 Other Vessel Related 5.033 Terminal Operations 40.513 Terminal Maintenance 12.330 Contracted Routes 1.364 Other Operating Expenses* Insurance, taxes, utilities 5.976 Unidentified Expenses 1.580 Total Direct Operating Expenses (303.909)	Security 4.904 Customer Services 3.821 Transportation Demand 1.353 Major Road Network 20.986 Bus & Seabus 326.477 Skytrain 42.887 Commuter Rail 21.562 Albion Ferry 4.048 Aircare 21.271 Total (447.309)	Commissions (ins. agents) 4.849 Highways Maintenance 419.779 (roads, bridges) Highways Operations 27.583 Motor Vehicle Impound Refunds 47.734 Total (499.945)
Operating Net (Shortfall) Cost Recovery Ratio		35.567 339.6/303.9 = 111.7%	(197.180) 250.1/447.3 = 55.9%	(378.954) 120.9/499.9 = 24.2%
Direct Subsidies Level of Subsidization Ratio		Federal Contract 22.438 Provincial Motor Fuel Tax 72.519 Total Direct Subsidies 94.957 95/434.4 = 21.8%	Taxation 278.058 (Fuel Tax & Transit Levy) Total Direct Subsidies 287.058 278.1/528.2 = 52.6%	Motor Vehicle Act 192.972 Commercial Transport Act 148.048 Motor Carrier Act .683 Total Direct Subsidies 341.703 341.7/462.7 = 73.8%
Capital Expenses		Vessels 84.018 Terminals 21.220 Total Sustaining CAPX (105.238)	Amortization of Capital Assets (47.404)	Highway Capital Construction (403.549)
Corporate Over head & Administration Expenses Corporate Administrative Overhead Ratio		Management & Administration Labour 34.700 *Other Unallocated Expenses 25.486 (travel, fees, communications & computers) Total Corporate/Admin. (60.186) 60.2/409.1 = 14.7%	Administration (17.414) 17.4/494.7 = 3.5%	Corporate Services & Minister's Office 23.615 Planning (Major Projects) 6.842 Superintendent of MV Office 4.440 Motor Carrier Commission .561 Total Corporate Administration (35.458) 35.5/903.5 = 3.9%
Interest on Debt Expense		(8% on \$235 million) (14.000)	(6% on 579.3 million) (35.553)	Provincial debt servicing associated with Highways Capital Construction and Ministry over-runs is unknown

Total Sustaining Cash (Shortfall)	(48.900)	(19.493)	(476.258)
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*from BCFC 2000/2001 Annual Report pg. 53