



FORWARD LOOKING STATEMENTS

This report contains certain “forward looking statements”. These statements relate to future events or future performance and reflect management’s expectations regarding our growth, results of operations, performance, business prospects and opportunities and industry performance and trends. They reflect management’s current internal projections, expectations or beliefs and are based on information currently available to management. Some of the market conditions and factors that have been considered in formulating the assumptions upon which forward looking statements are based include traffic, the Canadian Dollar relative to the US Dollar, fuel costs, construction costs, the state of the local economy, fluctuating financial markets, demographics, tax changes, and the requirements of the Coastal Ferry Services Contract.

Forward looking statements included in this document include statements with respect to:

- traffic levels;
- our short-term and long-range business plans;
- our asset renewal programs for vessels and terminals; and
- our pricing promotions, underwater radiated noise, Salish Class vessels, the *Northern Sea Wolf*, Spirit Class mid-life upgrades, and minor vessel replacements.

In some cases, forward looking statements can be identified by terminology such as “may”, “will”, “should”, “expect”, “plan”, “anticipate”, “believe”, “estimate”, “predict”, “potential”, “continue” or the negative of these terms or other comparable terminology. A number of factors could cause actual events or results to differ materially from the results discussed in the forward looking statements. In evaluating these statements, prospective investors should specifically consider various factors including, but not limited to, the risks and uncertainties associated with: vendor non-performance; capital market access; interest rate, foreign currency, fuel price, and traffic volume fluctuations; the implementation of major capital projects; security, safety, and environmental incidents; confidential or sensitive information breaches; changes in laws; vessel repair facility limitations; economic regulatory environment changes; tax changes; and First Nation claims.

Actual results may differ materially from any forward looking statement. Although management believes that the forward looking statements contained in this report are based upon reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward looking statements. These forward looking statements are made as of the date of this report, and British Columbia Ferry Services Inc. assumes no obligation to update or revise them to reflect new events or circumstances except as may be required by applicable law.

NON-IFRS MEASURES

In addition to providing measures prepared in accordance with IFRS, we present certain financial measures that do not have any standardized meanings prescribed by IFRS and therefore are unlikely to be comparable to similar measures presented by other companies. These include, but are not limited to, net earnings adjusted for the effect of rate regulation. These supplemental financial measures are provided to assist readers in determining our ability to generate cash from operations and improve the comparability of our results from one period to another. We believe these measures are useful in assessing operating performance of our ongoing business on an overall basis.



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BC Ferries is one of the largest ferry operators in the world, providing year-round vehicle and passenger service on 25* routes to 47 terminals, with a fleet of 36** vessels. We are an essential transportation link that connects coastal communities and facilitates the movement of people, goods and services. In fiscal 2018, we carried 22 million passengers and 8.7 million vehicles throughout coastal British Columbia.

Our New Vision, Mission and Values

Our new vision and mission summarizes our future desired state and describes why we exist and what we do. All of the work we do is in pursuit of our vision and mission.

Our vision builds on what we have achieved in the past 15 years. We strive to be trusted and valued by our customers, stakeholders and employees. To earn the public's trust and provide a service our customers value, we are connecting coastal communities, businesses and employees while ensuring they have a voice in the decisions that impact their lives.

*Rt. 28 between Port Hardy and Bella Coola commences in 2018.

**Took ownership of the *Northern Sea Wolf* in fiscal 2018. Vessel will enter service in fiscal 2019.



Our Vision

Trusted, valued.

Our Mission

We connect communities and customers to people and places important in their lives.

Our Values

Safe Safety is our highest value.

Caring We operate from a position of kindness and empathy for those who travel and work with us.

Honest We conduct business with integrity, honesty and accountability.

Collaborative We collaborate with others to enhance the customer experience.

Respectful Respect is paramount in our interactions with others.

Sustainable Our environmental, social and economic impact are central to business decisions.

Strategic Goals

Our strategic goals focus on the broad outcomes we will pursue to achieve our vision and mission to turn them into a reality.

- 1 Ensure Safe, Reliable & Efficient Operations
- 2 Deliver a Customer-Focused Travel Experience
- 3 Foster a Productive, Motivated & Engaged Workforce
- 4 Be a Leader in Environmental and Social Governance
- 5 Grow & Profitably Diversify our Revenue Base
- 6 Drive Prudent Investment in our Capital Assets



On behalf of the Board of Directors of British Columbia Ferry Services Inc., I would like to recognize all BC Ferries' employees for their continued commitment to safety, customer service and delivering reliable and efficient ferry service to communities in coastal British Columbia. Our employees' expertise unlocked more capacity than ever, accommodating as many customers as possible while providing an exceptional customer experience during a very busy year. The past fiscal year was an excellent one, with many accomplishments, improvements for our customers and progress on capital projects.

BC Ferries welcomed 22 million passengers on more than 174,000 sailings. We saw increases of 5 per cent in passenger traffic and 4.7 per cent in vehicle traffic compared to the prior year. These passenger traffic levels are the highest experienced in 20 years, and vehicle traffic levels are the highest BC Ferries has ever experienced.

We continued to focus on safety, with crews performing 29 marine rescues this past year. The Canadian Safe Boating Council awarded BC Ferries the Rescue of the Year. This recognition was for the decisive actions of the *Spirit of Vancouver Island* to deploy a skilled rescue crew, retrieve six people from the water and bring them to safety. This year, we were also honoured to receive the DuPont Global Safety Award, an achievement that recognizes global excellence in workplace safety across all industries.

The three new Salish Class ferries entered service on the Comox – Powell River route and in the Southern Gulf Islands. These dual-fuel vessels run primarily on natural gas to reduce costs and improve BC Ferries' environmental performance significantly.

BC Ferries continued to invest in its fleet, purchasing a used vessel, the *Northern Sea Wolf*, to serve a new direct route between Port Hardy and Bella Coola. The *Northern Sea Wolf* was upgraded significantly at Esquimalt Drydock Company in Victoria, with contracts for Esquimalt

Drydock and other local contractors and suppliers totalling over \$20 million for interior and safety upgrades.

The *Spirit of British Columbia* had its mid-life upgrade at Remontowa Ship Repair SA in Poland, which started in the fall of 2017 and was completed in the spring of 2018. The mid-life upgrade included converting the vessel to dual-fuel, so it now runs on natural gas or ultra-low sulphur diesel, significantly reducing emissions and costs while operating on natural gas.

Terminal improvements continued, including a \$12 million project to replace aging infrastructure which improved the customer experience at Prince Rupert terminal. The upgrade includes a more comfortable covered and wider walkway, a new waiting room for walk-on passengers and a wider trestle for vehicles loading onto the vessel. Terminal upgrades also began at Bella Coola, Ocean Falls, Shearwater and Bella Bella to accommodate the *Northern Sea Wolf*.

I would like to recognize the achievements of the executive management team for their focused direction and financial leadership, and all BC Ferries employees for their continued efforts to make BC Ferries a great company of which we can all be proud.

Over the next year, BC Ferries will continue its commitment to safety, as well as focus on customers' experience by providing new and upgraded ships, terminal enhancements and technology improvements. Looking to the future, BC Ferries continues to focus on the online as well as face to face travel experience, while prioritizing vessel interoperability and exploring options for more environmentally-friendly operations. The Board looks forward to the year ahead and our continued focus overseeing the success of BC Ferries.

A handwritten signature in black ink that reads "Donald P. Hayes". The signature is fluid and cursive, written over a thin horizontal line.

DONALD P. HAYES

CHAIR OF THE BOARD OF DIRECTORS
BRITISH COLUMBIA FERRY SERVICES INC.



I want to open with my sincere thanks to the staff and crews of BC Ferries who make this such an amazing organization. We set traffic and volume records this year thanks in no small part to their dedication, professionalism and unfailing safety focus. They truly are the heart of our business.

Safety is a core value at BC Ferries, vital to everything we do. BC Ferries' SailSafe program has transformed the company's safety culture, processes and performance to deliver safe operations for our customers and a safer workplace for our employees. We continue to receive recognition for safety, winning the 2017 Safety at Sea Employer of the Year Award and the 2017 DuPont Global Safety Award. That being said, the safety incident on the *Queen of Cumberland* where employees were injured this year shows we still have much to do.

We continued to invest in clean technology for B.C. coastal residents this year. A significant highlight was bringing our three new natural gas-fuelled Salish Class vessels into service, a major accomplishment by our staff and crews. These new vessels are more sustainable and affordable, emit fewer greenhouse gas emissions and are the quietest ships in our fleet.

Speaking of quiet ships, this past year we made significant progress understanding the underwater radiated noise (URN) our fleet emits to the Salish Sea. Studies show BC Ferries is one of the largest emitters of URN because of our many sailings, routes and length of service day. We are working in partnership with the federal government on mitigations, culminating in our 2018 Long Range Underwater Radiated Noise Mitigation Plan released this summer.

This year, our 2018 Strategic Plan released our new Vision - to be "Trusted, Valued" by our customers, stakeholders and employees. To earn the public's trust and provide a service our customers value, we are engaging with communities and staff to ensure they have a voice in the decisions that impact them.

The 2018 Strategic Plan also established our new Mission - *we connect communities and customers to people and places important in their lives.* This recognizes we provide more than transportation; we connect the lives of inhabitants, visitors and businesses of coastal B.C. Connectivity allows B.C. coastal life to flourish, a responsibility we take seriously.

We are proud that BC Ferries was once again named one of B.C.'s Top Employers, an award that recognizes organizations that offer exceptional places to work. BC Ferries has focused on developing a progressive workplace, with career opportunities across the organization, extensive training and development programs, and community involvement initiatives.

We continued to focus on improving our environmental performance, with our Fleet Maintenance Unit becoming only the second shipyard in Canada to be certified by the Green Marine environmental certification program. BC Ferries is now one of only three companies certified by Green Marine in all three main categories, as a ship owner, terminal operator and shipyard. In the past year, we also began a project to build two new 47-car ferries that will use a hybrid electric battery propulsion system for service in the Northern Gulf Islands in 2020. This is a continuation of our Clean Technology Adoption Plan released this year.





































During fiscal 2018, we generated \$98.3 million in gross revenue from our food service and retail outlets. BC Ferries Vacations also increased revenue, generating \$6.7 million in fiscal 2018. Together these two lines of business earned \$7.8 million more than last year. These services not only provide an enjoyable travel experience for our customers, they reduce upward pressure on fares. We continue to focus on affordability for our customers. We have held the cost of ferry travel constant for the past two years while also offering promotions to provide customers with a choice of discount travel. This year, working with the provincial government, we reduced or froze fares for all customers.

Even as we move ahead, we are alive to the challenges we face. On some routes, notably Langdale and the northern services, peak season capacity is too little for the growing demand. Increasing capacity is costly and we are discussing the way forward with ferry users, communities and government. We also face challenges finding skilled mariners, and this sometimes leads to operational disruptions. We have plans which mitigate these issues and customers will see changes in coming years.

With record traffic levels across the system, continued investment in our ships, terminals and employees is essential. We will continue our commitment to safety, while connecting communities and customers to the people and places important in their lives.

A handwritten signature in black ink, appearing to read 'Mark F. Collins'. The signature is fluid and cursive, written over a thin horizontal line.

MARK F. COLLINS
PRESIDENT & CHIEF EXECUTIVE OFFICER
BRITISH COLUMBIA FERRY SERVICES INC.

	CAPACITY			CAPACITY			CAPACITY	
	PASSENGER	CAR		PASSENGER	CAR		PASSENGER	CAR
	2,100	358		638	115		300	52
	2,100	358		600	138		300	44
	1,604	310		600	138		269	26
	1,604	310		600	138		200	26
	1,604	310		462	112		200	21
	1,494	312		462	112		150	45
	1,494	316		457	100		150	38
	1,494	308		450	92		150	35
	1,494	308		400	58		150	26
	1,332	254		400	61		150	19
	1,200	280		400	59		150	16
	640	87		400	63		100	12



LEGEND

- 1 Tsawwassen – Swartz Bay
- 2 Horseshoe Bay – Departure Bay
- 3 Horseshoe Bay – Langdale
- 4 Fulford Harbour – Swartz Bay
- 5 Swartz Bay – Southern Gulf Islands
- 6 Vesuvius Bay – Crofton
- 7 Earls Cove – Saltery Bay
- 8 Horseshoe Bay – Bowen Island
- 9 Tsawwassen – Southern Gulf Islands
- 10 Port Hardy – Prince Rupert
- 10s Bella Bella - Ocean Falls - Shearwater - Bella Coola
- 11 Prince Rupert – Haida Gwaii
- 12 Brentwood Bay – Mill Bay
- 13 Langdale – Gambier Island – Keats Island
- 17 Comox – Powell River
- 18 Powell River – Texada Island
- 19 Nanaimo Harbour – Gabriola Island
- 20 Chemainus – Thetis Island – Penelakut Island
- 21 Buckley Bay - Denman Island
- 22 Denman Island – Hornby Island
- 23 Campbell River – Quadra Island
- 24 Quadra Island – Cortes Island
- 25 Port McNeill – Sointula – Alert Bay
- 26 Skidegate – Alliford Bay
- 28 Port Hardy – Bella Coola
- 30 Tsawwassen – Duke Point

Southern Gulf Island Routes



ROUTE 9 = TSAWWASSEN SERVICE FOR PENDER, SATURNA, MAYNE, GALIANO, SALT SPRING
 ROUTE 5 = SWARTZ BAY SERVICE FOR PENDER, SATURNA, MAYNE, GALIANO



Delivering an Improved Customer Experience

BC Ferries places our customers at the centre of all we do, striving to make every customer interaction a safe, positive and satisfying experience.

- Established our new vision (trusted, valued) and our new mission.
- Delivered over 174,000 sailings to 22 million passengers and 8.7 million vehicles. On average, this is more than 470 sailings, 60,000 people and 23,000 vehicles per day.
- Achieved a 99.83 per cent sailing reliability rate, a customer satisfaction rate of 87 per cent in our annual customer satisfaction tracking survey, and an on-time performance rating of 89 per cent.
- Generated \$98.3 million in Catering & Retail gross revenue.
- BC Ferries Vacations generated \$6.7 million in gross revenue, an increase of 8 per cent over the prior year. BC Ferries Vacations offers packages that combine hotel accommodations with ferry travel and activities to attract visitors to the west coast.
- Offered several pricing promotions on over 3,300 sailings, including a summer promotion, Thanksgiving savings promotion and Holiday savings promotion as well as our popular “Size up the Savings” for extra length passenger vehicles. The seasonal promotions offered fares from \$39 for vehicle and driver on select early morning and late evening sailings.
- Conducted a public engagement process to gather input on schedule changes for the Metro Vancouver to Sunshine Coast and Metro Vancouver to Bowen Island routes. Based on customer input, new schedules were developed and went into effect in January 2018. The new schedules show improved on-time performance for our customers.
- To support the health and wellness of the travelling public and our employees, BC Ferries implemented a smoke-free environment on all vessels and terminals as of January 22, 2018.
- Began preparations for a new direct service between Port Hardy and Bella Coola. The ship purchased for the new route was renamed *Northern Sea Wolf*, following a community engagement process with local First Nations, Ferry Advisory Committee Members, BC Ferries employees and the Mid-Coast Ferry Working Group. The name is inspired by a First Nations legend in which the Sea Wolf is a manifestation of the Orca. The Sea Wolf symbolizes family and loyalty and the spirit of the Sea Wolf protects those travelling their waters.
- Working with local Ferry Advisory Committees, BC Ferries added sailings to the schedules on several of its routes. Extra service is now scheduled on the Earls Cove – Saltery Bay, Horseshoe Bay – Bowen Island, Buckley Bay – Denman Island, Hornby Island – Denman Island, Comox – Powell River and Alliford Bay – Skidegate routes.
- In partnership with Parks Canada, implemented the 12th season of our Coastal Naturalist program on the Tsawwassen – Swartz Bay and Horseshoe Bay – Departure Bay routes for the summer months. The program highlights the wonders of the west coast by providing education on B.C.’s unique wildlife and marine life, as well as coastal, nautical and cultural history, and showcasing Parks Canada’s beautiful areas to explore. Over the years, more than one million passengers have enjoyed these free educational programs.

Investing in British Columbia's Coastal Ferry System

We invest sensibly in assets and infrastructure, ensuring customers see their fares put to the best use with improved services.

- The *Spirit of British Columbia* underwent its mid-life upgrade at Remontowa Ship Repair S.A. in Poland in the fall of 2017, completed in the spring of 2018. The mid-life upgrade includes conversion to dual fuel, so the largest vessels in our fleet will now run on either natural gas or ultra-low sulphur diesel, significantly reducing emissions and costs when operating on natural gas. The *Spirit of Vancouver Island* will undergo the same process this year from the fall of 2018 through the spring of 2019.
- We continued to roll out our vessel class and standardization strategy to achieve cost savings and efficiencies. We have contracted the building of two new hybrid electric diesel minor class vessels scheduled to go into service in the Northern Gulf Islands in 2020.
- BC Ferries purchased a used vessel, the *Northern Sea Wolf*, to serve the new route between Port Hardy and Bella Coola. The vessel was built in 2000 and has a capacity of 35 vehicles and 150 customers and crew.
- The *Northern Sea Wolf* underwent a major upgrade at Esquimalt Drydock Company in Victoria with contracts for Esquimalt Drydock and other local contractors and suppliers totalling over \$20 million for interior and safety upgrades.
- Three new Salish Class vessels joined the BC Ferries fleet and entered service. The first vessel, the *Salish Orca*, entered service on the Comox – Powell River route. The *Salish Eagle* and *Salish Raven* began service in the Southern Gulf Islands. These vessels are the first in our fleet to be dual-fuel capable and can operate on either natural gas or ultra-low sulphur diesel. The Salish Class emit the lowest underwater radiated noise of any ships in our fleet.
- We entered into a five-year supply agreement with Point Hope Maritime Ltd. of Victoria, B.C. for the maintenance of eight of our smaller vessels. We have approximately 20 scheduled dry-dockings for these vessels over the next five years and this strategic partnership ensures a local and secure supply of services. Over the past 10 years, BC Ferries has spent about \$1 billion at local shipyards on dry-dockings and refits, repairs, mid-life upgrades, and life-extension projects.
- We completed a \$12 million upgrade at Prince Rupert Terminal, providing a more comfortable journey for our customers. The upgrade includes a new, wider trestle for loading vehicles, a wider, covered walkway for passengers and a new waiting room for foot passengers.



The concept design for BC Ferries' new Island Class vessels, capable of carrying 47 vehicles. The Island Class ferries will enter service in the Northern Gulf Islands in 2020.





Building a Better BC Ferries

We are focused on being a trusted and valued partner committed to safe, reliable and sustainable operations.

- Won the DuPont Global Safety Award, an award that recognizes excellence in workplace safety across industries globally. BC Ferries' SailSafe program helps us deliver a safer workplace for our employees and a safer environment for our customers.
- BC Ferries was named a Top Employer in B.C. for the second year in a row. This award recognizes companies for providing innovative programs for their employees. BC Ferries has invested in extensive training and development for employees, focusing on career opportunities across the organization.
- For fiscal 2018, the Port of Vancouver recognized us with the Blue Circle Award which distinguishes vessel operators who go above and beyond regulatory requirements to reduce air emissions and have the highest rate of participation in their EcoAction Program.
- We consulted regularly with our 13 Ferry Advisory Committees to share information and identify potential service improvements by gathering community feedback.



- Won the Tourism Vancouver Island FortisBC Award that recognizes an organization for using natural gas in their tourism-related operation. The Salish Class vessels use of natural gas reduces an estimated 9,000 metric tonnes of carbon dioxide equivalent per year, equivalent to removing about 1,900 passenger vehicles off the road annually.
- BC Ferries won the Safety at Sea Employer of the Year Award, recognizing career development, staff investment and support programs for seafarer family and friends.
- In May 2017, the Fleet Maintenance Unit became the second shipyard in Canada to be certified by the Green Marine environmental certification program. BC Ferries has been certified by Green Marine as a ship owner and a terminal operator since 2015 and is one of the largest participating companies.
- In January 2018, BC Ferries was awarded the Rescue of the Year by the Canadian Safe Boating Council. The recognition was for the decisive actions of the *Spirit of Vancouver Island* to deploy a skilled rescue crew, ultimately saving six lives. The crew pulled six people from the ocean water after a boat capsized and two kayakers tipped over.



Giving Back to the Communities We Serve

It is important to us to actively participate in the growth, development and sustainability of the communities in which we operate and live.

- BC Ferries held fares steady on 21 of its 24 routes as of April 1, 2017. The company also announced a \$5 reduction in reservation fees, from \$15 to \$10 if booked seven days in advance. In addition, BC Ferries contributed \$15.7 million to eliminate the balance in the non-northern routes' deferred fuel cost account and the need to recoup these costs from customers in the future.
- Partnered with viaSport to offer \$100,000 in-kind travel to help youth in coastal communities participate in organized sport.
- We committed \$250,000 in funds and materials to Royal Canadian Marine Search & Rescue to provide support for the development of their training centre.
- In June 2017, BC Ferries, Angel Accessibility and Houle Electric worked together to address accessibility challenges for the Cholette family of Cloverdale, B.C. The family set up a crowd funding site for donations to purchase a stair lift for their son, Jack, who has a rare genetic condition requiring the use of a wheelchair. A BC Ferries employee heard about the family and thought of an unused stair lift that had been removed following the completion of an elevator project at Horseshoe Bay terminal. As the stair lift was not being used at another terminal, BC Ferries donated it to the family and several employees volunteered to help with the installation.
- BC Ferries sponsored the BC Bike Race, a 310 km circle tour starting in Vancouver, travelling to Vancouver Island, Powell River, the Sunshine Coast and Whistler. The event brings cyclists and their families from around the world for a seven-day race showcasing the beauty of the communities served by BC Ferries.
- BC Ferries provided complimentary travel support for people evacuating the wildfires in the B.C. Interior in summer 2017. BC Ferries Customer Care team responded to over 2,000 calls inquiring about travel during the wildfire crisis and provided over \$235,000 in complimentary travel to fire and emergency vehicles engaged in the wildfire relief effort and evacuees displaced by the wildfires.
- BC Ferries' Media Charity Golf Classic raised \$60,000 to donate to coastal region branches of the United Way. Over the past 12 years, the annual tournament has raised more than \$720,000 to support programs for children and families.
- BC Ferries offered complimentary vehicle and passenger travel for all Emergency First Responders attending Const. John Davidson's Celebration of Life Ceremony on November 19, 2017. Abbotsford Police Department's Const. John Davidson was tragically killed while on duty on November 6, 2017.
- The BC Ferries' Employee Golf Tournament raised over \$2,700 and donated it to Protein for People, a non-profit that subsidizes food bank purchases of much-needed protein sources such as fish and peanut butter. The BC Ferries' Employee Golf Tournament is funded by the individual employees who participate.
- BC Ferries Coast Busters employee dragon boat team competed in the 2017 Dragon Boat Festival and raised \$8,800 for the BC Cancer Foundation. The team has been participating for four years now, raising a total of nearly \$30,000 to date, and consistently ranks among the top five fundraisers.
- BC Ferries raised more than \$30,000 through the 2017 United Way Workplace Campaign, where employees donate to charities and services that help our communities.
- Continued our BC Ferries Community Investment Program, which offers support for community events, sports and charities through sponsorships, in-kind donations of ferry travel and employee volunteerism.
- With approximately 470 sailings a day, BC Ferries is a continued presence on the waterways and is often a first responder to marine incidents. Our crews performed 29 marine rescues throughout coastal British Columbia in fiscal 2018.
- In support of talented, young musicians, BC Ferries was the title sponsor for the 2017 Pacific Region International Summer Music Academy (PRISMA) Festival, held in Powell River from June 12-24, 2017.

Performance Measures

With a clear focus on safety and reliability to better serve our customers, revitalizing our assets and developing our employees, we made substantial progress last year in building a better BC Ferries.

In support of our vision, mission and strategic goals, we have implemented performance measures to monitor the progress of the business and our commitment to continuous improvement. The following are the actual results for fiscals 2015 through 2017, the target and actual results for fiscal 2018, as well as the target for fiscal 2019:

Employee Safety: employee injury frequency rate x severity rate divided by 1,000

Passenger Safety: number of passenger injuries per one million passengers

Reliability Index: actual round trips divided by scheduled round trips, less weather, medical or rescue related cancellations

Customer Satisfaction: rating on a scale of 1-5, based on three surveys performed during the year

EBITDA: Net earnings adjusted for the impact of regulatory assets and liabilities and before interest, taxes, depreciation and amortization

Regulatory Net Earnings: Net earnings adjusted for the impact of regulatory assets and liabilities

	2015	2016	2017	2018	2019	
	ACTUAL	ACTUAL	ACTUAL	TARGET	ACTUAL	TARGET
Employee Safety Index	0.65	0.48	0.43	0.39	0.46	0.39
Passenger Safety Index	11.90	11.24	9.62	10.68	10.01	9.59
Reliability Index	99.75%	99.72%	99.69%	99.55% - 99.74%	99.83%	99.55% - 99.74%
Customer Satisfaction	4.11	4.14	4.18	4.20	4.16	4.20
EBITDA (\$millions)	255.6	268.5	294.6	290.5	273.8	295.8
Regulatory Net Earnings (\$millions)	41.4	64.8	87.9	70.6	55.3	63.6

Results for fiscal 2018 varied with some better than the targets set and others not meeting the target. We are committed, together with our dedicated employees, to service excellence. The targets for fiscal 2019 for our employee safety index, customer satisfaction rating and reliability index range are held steady at a practical level, while we strive for an improvement in our passenger safety index. The financial results reflect BC Ferries' one-time contribution of \$15.7 million to eliminate the balance in the non-northern routes' deferred fuel cost account and the need to recoup these costs from customers in the future.

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**MANAGEMENT'S DISCUSSION & ANALYSIS
OF FINANCIAL CONDITION AND FINANCIAL PERFORMANCE
FOR THE FISCAL YEAR ENDED MARCH 31, 2018
DATED JUNE 19, 2018**

The following is our discussion and analysis of the financial condition and financial performance for British Columbia Ferry Services Inc. ("BC Ferries" or the "Company") for the year ended March 31, 2018 that has been prepared with information available as of June 19, 2018. This discussion and analysis should be read in conjunction with our audited consolidated financial statements and related notes for the years ended March 31, 2018 ("fiscal 2018") and March 31, 2017 ("fiscal 2017"). These documents are available on SEDAR at www.sedar.com and on our investor webpage at http://www.bcferries.com/investors/financial_reports.html.

Except where indicated, all financial information herein is expressed in Canadian dollars and determined on the basis of International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board (the "IASB").

BUSINESS OVERVIEW

British Columbia Ferry Services Inc. is an independent company providing passenger and vehicle ferry services on the west coast of British Columbia. We operate one of the largest and most complex ferry systems in the world. We provide frequent year-round transportation service, with 35 vessels operating on 24 routes out of 47 terminals spread over 1,600 kilometres of coastline. We also manage ferry transportation services on other remote routes through contracts with independent operators.

Our service is an integral part of British Columbia's coastal transportation system and has been designated by the Province of British Columbia (the "Province") as an essential service for purposes of the provincial Labour Relations Code. This designation means our services are considered necessary for the protection of the health, safety and welfare of the residents of British Columbia.

Our Major Routes, which are our four busiest routes, consist of three regulated routes connecting Metro Vancouver with mid and southern Vancouver Island and one regulated route connecting Horseshoe Bay and Langdale. During fiscal 2018, our Northern Routes consisted of two regulated routes operating on the British Columbia coast north of Port Hardy on Vancouver Island. In fiscal 2019, we will be adding a new route directly connecting Port Hardy and Bella Coola. Our Other Routes consist of 18 regulated routes and 8 unregulated routes primarily serving the northern and southern Gulf Islands and the northern Sunshine Coast.

We provided over 174,000 sailings during fiscal 2018, 2,471 more than in the prior year. We carried 8.7 million vehicles and 22.0 million passengers, an increase of 5.0% and 4.7%, respectively, compared to the prior year, contributing to BC Ferries' strong financial performance. The passenger traffic levels experienced in fiscal 2018 are the highest we have experienced in 20 years and vehicle traffic levels were the highest we have ever experienced. For a discussion of our traffic levels, see "Financial and Operational Overview" below.

Significant events during or subsequent to fiscal 2018 include the following:

Tariffs

- On April 1, 2017, we applied average fare increases below those allowed by the BC Ferries Commissioner (the "Commissioner"). No passenger or vehicle fare increases were implemented on any routes with the exception of the three Major Routes connecting Metro Vancouver with mid and southern Vancouver Island. Average vehicle fare increases of 1.9% were implemented on these three Major Routes, which enabled us to provide promotional fares with significant discounts on many sailings. No increase in passenger fares was implemented on these routes. Also on April 1, 2017, we implemented reductions in reservation fees.

- On April 1, 2018, we applied a fare reduction of 15% on the Northern Routes, the regulated Other Routes and on the Major Route connecting Horseshoe Bay and Langdale. Fares were held constant on the three Major Routes connecting Metro Vancouver with mid and southern Vancouver Island. Also on April 1, 2018, the BC seniors' passenger discount increased from 50% to 100% for travel Monday to Thursday on the Major and Other Routes. The total value of these initiatives over two years is \$98 million. We reached an agreement with the Province whereby we will contribute \$39 million in foregone revenue and the Province will contribute \$59 million in ferry transportation fees towards the fare reductions and the increase to the BC seniors' discount.

Vessels

- On May 16, 2017, our first Salish Class vessel, the *Salish Orca*, commenced regularly scheduled service between Comox and Powell River. On June 21, 2017 and on August 3, 2017, the *Salish Eagle* and the *Salish Raven*, respectively, commenced regularly scheduled service in the Southern Gulf Islands. Each vessel has the capacity to carry approximately 145 vehicles and 600 passengers and crew. Introduction of these vessels enabled the retirement of the 52-year old *Queen of Burnaby* and the 53-year old *Queen of Nanaimo*. (See "Investing in Our Capital Assets" for more detail.)
- On June 1, 2017, we entered into a five-year supply agreement with Point Hope Maritime Ltd. of Victoria, BC for the maintenance of eight of our minor vessels. We have approximately 20 scheduled dry-dockings for these vessels over the next five years and this strategic partnership ensures a local and secure supply of services.
- On December 15, 2017, the *Northern Sea Wolf* arrived in British Columbia after a 10,097 nautical mile journey from Athens, Greece. The vessel, built in 2000, will accommodate approximately 35 vehicles and 150 passenger and crew and will provide direct service between Port Hardy and Bella Coola. The 75-metre used vessel is undergoing extensive upgrades at Esquimalt Drydock Company, a local shipyard, in preparation for the start of regular service planned for late July 2018. (See "Investing in Our Capital Assets" for more detail.)
- On April 2, 2018 and on April 11, 2018, the first steel cuts were made for our two new minor class vessels. These vessels will each have a capacity to carry approximately 47 vehicles and 300 passengers. When these new vessels are placed into service in early 2020, we will be able to retire the 60-year old *North Island Princess* and the 54-year old *Howe Sound Queen*. We intend to deploy the first new vessel to provide service between Powell River and Texada Island and the second new vessel to provide service between Port McNeill, Alert Bay and Sointula. (See "Investing in Our Capital Assets" for more detail.)
- On June 6, 2018, the *Spirit of British Columbia* returned to service on our Tsawwassen – Swartz Bay route following its mid-life upgrade. The mid-life upgrade, which will enable the vessel to be in service for another 25 years, included major upgrades to the customer amenities, and the conversion to dual-fuel so it can operate on liquefied natural gas or ultra-low sulphur marine diesel.

Financing

- On April 28, 2017 and on May 4, 2017, we drew the final \$45 million under our export loan agreement with KfW IPEX-Bank GmbH, to coincide with the contract payment schedule for the *Salish Raven*. The net proceeds from the loan were used to partially finance the purchase of the *Salish Raven*. (See "Liquidity and Capital Resources" for more detail.)

General

- On April 1, 2017, Mark Collins assumed the role of President and CEO. A marine executive for the past 20 years, Mr. Collins' experience includes roles as the President of Rolls Royce Marine Brazil and Italy and Vice President of Global Technical Services, CSL Group. Mr. Collins was previously Vice President of Strategic Planning & Community Engagement at BC Ferries, and was the Vice President, Engineering between 2004 and 2012.
- On July 1, 2017, Alana Gallagher assumed the role of Chief Financial Officer. Ms. Gallagher was previously Treasurer and has been at BC Ferries for 18 years.
- On October 16, 2017, Corrine Storey assumed the role of Vice President and Chief Operating Officer. Ms. Storey was previously Vice President of Customer Services and has been with BC Ferries for 13 years.

CORPORATE STRUCTURE

Coastal Ferry Services Contract

We operate ferry services under a regulatory regime established by the *Coastal Ferry Act* (the "Act"), and under the terms set out in the Coastal Ferry Services Contract ("CFSC") between BC Ferries and the Province. This 60-year services contract, which commenced April 1, 2003, stipulates, among other things, the number of round trips that must be provided for each regulated ferry service route in exchange for specified fees (ferry transportation fees). The CFSC has been amended from time to time. The amendment documents are available on our webpage at: http://www.bcferries.com/about/More_Information.html.

Under the terms of the CFSC, we also receive an annual amount from the Province based on its agreement with the Government of Canada to fulfill the obligation of providing ferry services to coastal British Columbia. The amount of this payment is adjusted annually based on the Consumer Price Index ("CPI") (Vancouver).

The Act defines a performance term as the first performance term or any subsequent four-year period during the term of the CFSC. Performance term four ("PT4") commenced April 1, 2016 and ends on March 31, 2020.

In December 2017, the new provincial government announced a review of the CFSC and the provision of coastal ferry service in British Columbia to ensure that the model is operating in the public interest. The terms of reference for the review are available on the Province's website at www2.gov.bc.ca. The reviewer is to prepare and submit a report to the Minister of Transportation and Infrastructure for government's consideration by June 30, 2018 that will:

- examine BC Ferries' operations, including operating and capital expenditures, business processes, practices and policies to assess whether the services are being provided for in a manner that supports the public interest in affordable fares;
- consider what changes to the price cap and regulatory model would ensure the ferry system is working as efficiently and effectively as possible for all British Columbians and, in particular, ferry users and communities who depend on this essential service; and,
- identify opportunities and recommend actions to enhance ferry service delivery and/or reduce costs without impacting existing service.

Effective April 1, 2014, we implemented the Province's decision to amend its program to reduce the passenger fare discount from 100% to 50% for BC seniors travelling Mondays through Thursdays on the Major and regulated Other Routes. The CFSC was amended to establish the maximum annual amount payable by the Province in respect of senior discounts. Effective April 1, 2016, the CFSC was amended to discontinue direct funding of the seniors' discount and direct the maximum annual amount payable by the Province entirely to ferry transportation fees. Effective April 1, 2018, as part of our fare reduction funding agreement with the Province, the BC seniors' passenger discount of 100% was reinstated for travel Monday to Thursday on the Major and regulated Other Routes. The discount for BC seniors on the Northern Routes has remained unchanged over the years at 33% every day.

Also on April 1, 2018, we applied a fare reduction of 15% on the Northern Routes, the regulated Other Routes and on the Major Route connecting Horseshoe Bay and Langdale. Fares were held constant on the three Major Routes connecting Metro Vancouver with mid and southern Vancouver Island. We reached an agreement with the Province regarding the funding of these initiatives. On March 28, 2018, the CFSC was amended to reflect the agreement and the new annual ferry transportation fees payable by the Province.

Economic Regulatory Environment

The office of the Commissioner was created under the Act on April 1, 2003. The Act has been amended from time to time to expand and broaden the Commissioner's role and regulatory responsibilities. The primary responsibility of the Commissioner is to regulate ferry operators in such a way as to balance the interests of ferry users, taxpayers and the financial sustainability of the ferry operators. The Commissioner establishes price caps for designated ferry route groups for the purpose of regulating tariffs. The Commissioner has the authority to authorize the establishment of deferred fuel cost accounts and to set the terms and conditions for their use, including fuel surcharges or rebates. The Commissioner is also responsible for regulating the reduction of service and discontinuance of routes, monitoring the service provided under the CFSC, authorizing major capital expenditures, conducting performance reviews, regulating ferry transportation services where the Commissioner has determined an unfair competitive advantage exists and approving the customer complaints process.

In September 2015, the Commissioner issued Order 15-03 and Order 15-03A. These orders included the following:

- Establishment of the final price cap increase of 1.9% for each of the four years of PT4;
- Incorporation of an efficiency target (\$27.6 million over the four years of PT4);
- Requirement for a fuel management plan to be submitted prior to the start of PT4 setting out our strategies for fuel procurement, minimizing fuel consumption and the transition to alternate fuels. Our plan was submitted March 30, 2016 and is available on our webpage at: <http://www.bcferries.com/about/fuel-savings-reports.html>;
- Authorization to continue to use fuel cost deferral accounts in PT4;
- Establishment of the set price per litre at 91.5 cents for marine diesel and at 46.4 cents for liquefied natural gas ("LNG") in the first year of PT4; and
- Incorporation of an inflation factor of 2% per year on the price per litre of both marine diesel and LNG for the balance of PT4. (The set price per litre is an input into the determination of fuel surcharges or rebates.)

It was also established that, for price cap calculations, the consolidated route group effective April 1, 2013 will be in effect until March 31, 2020. In the absence of any further amendments, on April 1, 2020, the route group structure in the CFSC will revert to the structure that was in place at March 31, 2013. The structure at that time was comprised of three individual route groups, being the Major Routes, Northern Routes and Minor (regulated Other) Routes.

On April 5, 2017, the Commissioner issued Order 17-03, in which he confirmed his determination that the capital expenditure for the acquisition and modification of a used vessel to be used to provide mid-coast service, including a new seasonal direct ferry service between Port Hardy and Bella Coola, as well as the necessary terminal modifications, is reasonably required.

In November 2017, the Commissioner released a comparative fare analysis prepared by PricewaterhouseCoopers LLP, updating an earlier review conducted in 2012. The report indicates that fares at BC Ferries are generally comparable with similar ferry operators worldwide, and that BC Ferries' cost per nautical mile rankings with other ferry operators have not changed significantly since 2012.

On February 7, 2018, the Commissioner issued Order 18-01 in response to the findings of the review of BC Ferries' annual customer satisfaction tracking survey conducted for the Commissioner by MNP LLP. The order directed BC Ferries to augment our survey to include additional routes and to re-procure our contract with an external service provider to conduct the survey. Our plans to address the recommendations in MNP's report dated October 17, 2017, together with how we will communicate the actions we have taken in response, were submitted to the Commissioner as required by June 1, 2018.

On April 4, 2018, the Commissioner released a Procurement Performance Review prepared by Ernst & Young. The report concludes that BC Ferries' procurement policies and procedures are relatively mature and in line with what would be expected with comparable organizations. The report indicates that procurement risk management, oversight and assurance practices are strong in delivering value-for-money. It also identifies a number of opportunities to align our practices with leading practices and to strengthen contract mechanisms to further mitigate and transfer risk from BC Ferries.

On May 7, 2018, we applied for authorization to temporarily reduce service below the core services levels set out in the CFSC for two designated ferry routes (Swartz Bay to the Southern Gulf Islands and Tsawwassen to the Southern Gulf Islands) on the basis that an extraordinary situation existed, namely, an unanticipated requirement to remove the *Queen of Cumberland* temporarily from service arising from a mechanical failure of the davit for the vessel's rescue boat which resulted in physical injuries to two employees. On May 10, 2018, the Commissioner issued Order 18-02 approving our request to temporarily reduce service below the core services levels from April 18, 2018 until we were able to return the *Queen of Cumberland* to regular service. The order also requires us to supply various reports regarding the incident and our investigation. The *Queen of Cumberland* returned to service on May 18, 2018, which allowed for the return of regular sailing schedules in the Southern Gulf Islands.

The Commissioner's orders and reports are available on the Commissioner's website at www.bcferrycommission.com.

The Effect of Rate Regulation

We are regulated by the Commissioner to ensure, among other things, that our tariffs are fair and reasonable. Under the terms of the Act, the tariffs we charge our customers over a performance term are subject to price caps set by the Commissioner. The Commissioner may, under certain circumstances, allow increases in price caps over the set levels. Certain decisions and orders of the Commissioner may give rise to regulatory assets or liabilities. Regulatory assets generally represent incurred costs that are probable of future recovery in tariffs or fuel surcharges. Regulatory liabilities represent obligations to customers which will be settled through future tariff reductions or fuel rebates.

We transitioned to IFRS effective April 1, 2011. At that time, IFRS did not provide any guidance with respect to accounting for rate-regulated activities.

In January 2014, the IASB issued an interim standard, IFRS 14 *Regulatory Deferral Accounts*, which addresses accounting for rate-regulated activities. However, it does not apply to entities, like ours, that transitioned to IFRS prior to that date. As a result, we are not permitted to recognize in our financial statements the assets and liabilities that result from the regulated price cap setting process, such as our deferred fuel cost accounts. Under IFRS, rather than being charged to regulatory asset or liability accounts on our consolidated statements of financial position, fuel surcharges collected or rebates granted are included in revenue, and increases or decreases in fuel prices from those approved in price caps are included in operating expenses. We are regulated by the Commissioner, and these items are treated as assets and liabilities for regulatory purposes. Reporting for rate-regulated activities provides additional information which we use to assess performance and to make operating decisions.

Regulatory assets and liabilities do not have standardized meaning within IFRS. Our regulatory assets and liabilities should be considered in addition to, but not as a substitute for, measures of financial performance in accordance with IFRS.

We continually assess whether our regulatory assets and liabilities are probable of future recovery by considering such factors as applicable regulatory changes. These regulatory assets and liabilities are considered supplemental disclosures and are detailed in note 27 to our March 31, 2018 audited consolidated financial statements.

If IFRS permitted us to report regulatory assets and liabilities in our financial statements, the effect on our net earnings for the quarters and years ended March 31, 2018 and 2017 would be as follows:

(\$ millions)	THREE MONTHS ENDED MARCH 31		YEARS ENDED MARCH 31		
	2018	2017	2018	2017	
Net (loss) earnings	(41.0)	(40.8)	59.9	77.4	
Changes in net earnings:					
Regulatory asset or liability	Statement line item				
Deferred fuel costs					
Fuel costs under set price	Operations expense	(1.1)	(2.0)	(8.6)	(7.6)
Fuel rebates	Fuel rebates	3.7	3.3	19.4	18.1
Payments from the Province	Ferry service fees	–	–	0.3	0.1
		2.6	1.3	11.1	10.6
Corporate contribution	Operations expense	(15.7)	–	(15.7)	–
Decrease (increase) in total net earnings		(13.1)	1.3	(4.6)	10.6
Adjusted net (loss) earnings		(54.1)	(39.5)	55.3	88.0

Deferred fuel costs: As prescribed by regulatory order, we defer differences between actual fuel costs and regulated fuel costs which were used to develop the regulated price caps. The difference between actual fuel costs (including fuel hedge gains and losses) and the regulated fuel costs (set price) is deferred for settlement in future tariffs. In addition, as prescribed by regulatory order, we collect fuel surcharges or provide fuel rebates from time to time which are applied against deferred fuel cost account balances. We may also receive payments from the Province to be applied against deferred fuel cost account balances.

During fiscal 2018, fuel rebates totalled \$19.4 million, contributing to the deferred fuel cost account receivable balance growing to \$15.5 million. In response to this growing balance, we would typically reduce the fuel rebate to avoid further growth. However, during this same period we were also assessing fare affordability initiatives with the Province. As part of this endeavour we assessed the elimination of the deferral account balance, its impact on future customers and on BC Ferries.

We chose to eliminate the non-northern routes' deferred fuel cost account balance of \$15.7 million, and contribute \$39 million in foregone revenue to hold fares constant on the three Major Routes connecting Metro Vancouver with mid and southern Vancouver Island and reduce fares by 15% on all other routes. As the company continues to be exposed to current volatile fuel prices, changes in the level of fuel rebates or surcharges may be necessary going forward.

FINANCIAL AND OPERATIONAL OVERVIEW

This section provides an overview of our financial and operational performance for the past three fiscal years.

Years ended March 31 (\$ millions)	2018	2017	2016
Total revenue	899.0	859.3	834.6
% increase	4.6%	3.0%	3.2%
Operating expenses	782.7	726.2	709.0
Operating profit	116.3	133.1	125.6
Net finance and other	56.4	55.7	56.0
Net earnings	59.9	77.4	69.6
Other comprehensive gain (loss)	13.5	14.6	(23.8)
Total comprehensive income	73.4	92.0	45.8
As at March 31			
Total assets	2,162.4	2,046.9	1,899.3
Total long-term financial liabilities	1,347.6	1,340.4	1,281.0
Dividends on preferred shares	6.0	6.0	6.0

Our net earnings in fiscal 2018 were \$59.9 million, \$17.5 million lower than in fiscal 2017. In fiscal 2018, our revenues increased \$39.7 million compared to fiscal 2017, mainly as a result of increased traffic levels. In fiscal 2018, our operating expenses increased \$56.5 million, compared to fiscal 2017, primarily due to increases in wages and benefits, maintenance and depreciation costs. We provided 2,962 more round trips than required under the CFSC and 1,190 more round trips compared to the prior year, to accommodate the higher traffic volumes and to implement service enhancements. These additional trips and the introduction of three new vessels resulted in an increase in fuel consumption, labour and training related costs. Also, planned maintenance costs were significantly higher than in the prior year. (See "Revenue and Operational Statistics" and "Expenses" for more detail.)

Other comprehensive income in fiscal 2018 was \$1.1 million lower than in fiscal 2017. The other comprehensive gain of \$13.5 million in fiscal 2018 reflects a \$13.6 million gain for the change in the fair value of our fuel swap contracts and a \$1.8 million gain on the revaluation of our land, partially offset by a \$1.9 million loss on the actuarial valuation of our employee benefit plans.

In fiscal 2017, net earnings increased \$7.8 million compared to fiscal 2016 and reflected the effects of higher traffic levels, higher retail sales, higher ferry transportation fees and social program fees and lower financing costs, partially offset by operating cost increases mainly due to increases in wages and benefits. The other comprehensive gain of \$14.6 million in fiscal 2017 reflected a \$12.1 million gain for the change in the fair value of our fuel swap contracts, a \$3.7 million gain on the revaluation of our land and a \$0.3 million gain on the actuarial valuation of our workers' compensation benefit plan, partially offset by a \$1.5 million loss on the actuarial valuation of our employee benefit plans.

Traffic

In fiscal 2018, we experienced a 5.0% increase in vehicle traffic and a 4.7% increase in passenger traffic compared to fiscal 2017. The passenger traffic levels experienced in fiscal 2018 are the highest we have experienced in 20 years and vehicle traffic levels were the highest we have ever experienced.

In fiscal years 2009 through 2014, we experienced a decline in traffic due to economic uncertainty, the Canadian dollar being near parity with the US dollar, and low economic growth which negatively impacted our commercial and discretionary travel markets. Beginning in late fiscal 2015, we began to experience an increase in traffic, which has continued through fiscal 2018. We believe traffic was favourably impacted by a lower Canadian dollar, increases in tourism and general economic activity in British Columbia.

The following table details the traffic growth we have experienced in the past five fiscal years:

TRAFFIC BY FISCAL YEAR (in thousands)

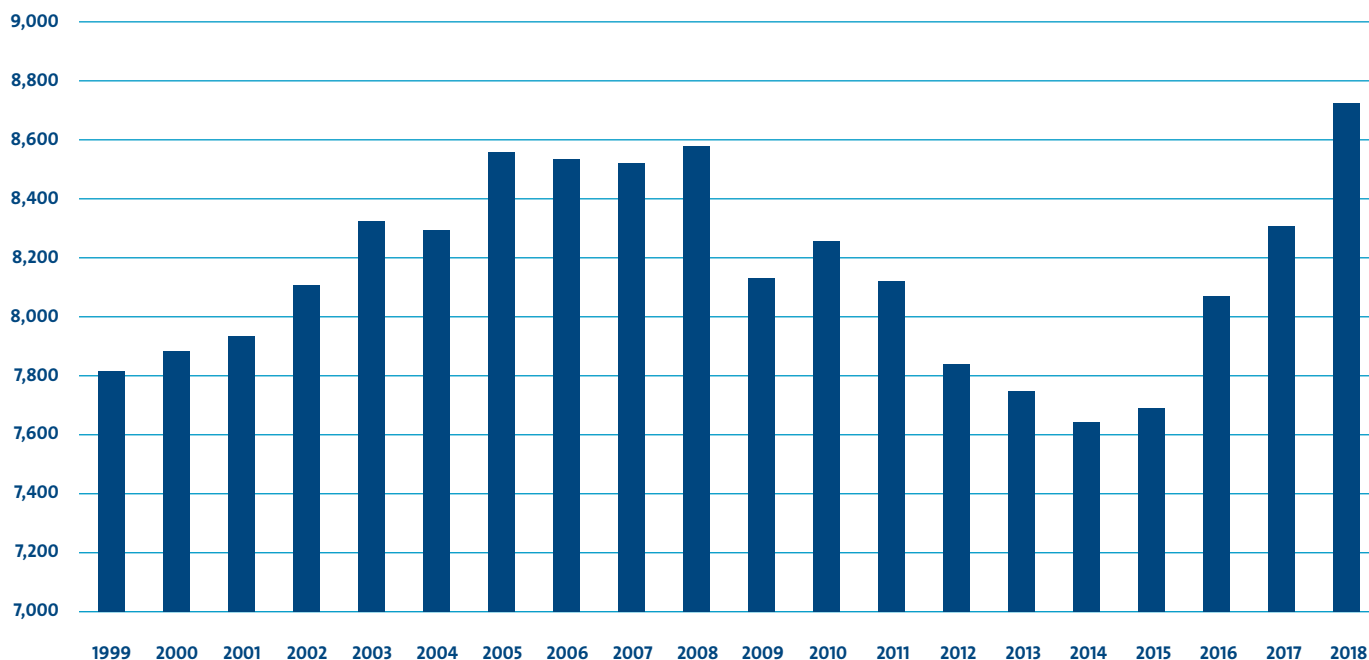
	2014	2015	2016	2017	2018
Vehicle	7,644.3	7,690.9	8,069.5	8,305.8	8,723.4
<i>(Decrease) Increase</i>	<i>(1.3%)</i>	<i>0.6%</i>	<i>4.9%</i>	<i>2.9%</i>	<i>5.0%</i>
Passenger	19,696.7	19,796.0	20,689.1	21,034.8	22,030.2
<i>Increase (Decrease)</i>	<i>(1.1%)</i>	<i>0.5%</i>	<i>4.5%</i>	<i>1.7%</i>	<i>4.7%</i>

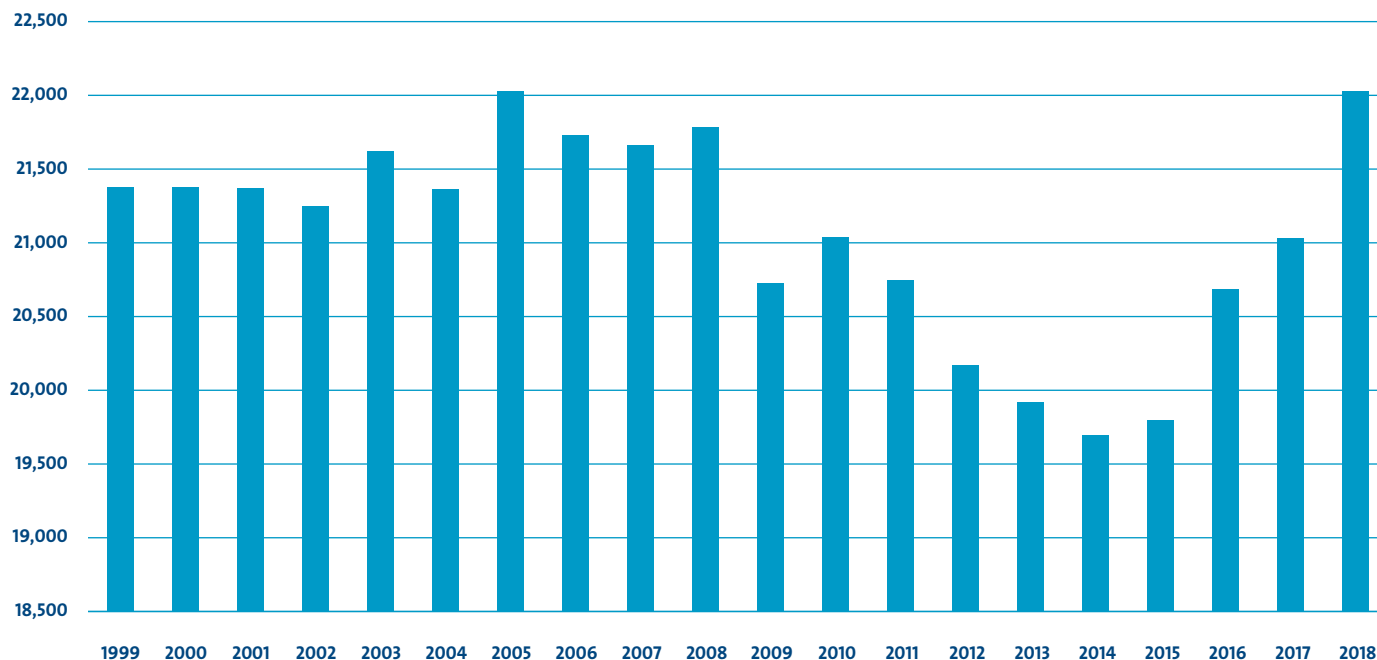
In fiscal 2017, traffic improved despite being negatively impacted by more days of unfavourable weather in the last half of fiscal 2017 compared to the same period in the prior year. In addition, annual traffic levels are affected by the timing of Easter. There were no Easter holiday weekends falling in fiscal 2017 while traffic levels were positively impacted in fiscal 2016 by two Easter holiday weekends.

We offered a variety of pricing promotions throughout fiscal 2018, fiscal 2017 and fiscal 2016. We believe these pricing promotions played a part in shifting some discretionary traffic to off-peak sailings, and, to a small degree, an increase in traffic each year compared to the prior year.

The following graphs illustrate our annual vehicle and passenger traffic levels for the past 20 fiscal years:

Vehicles (in thousands)



Passengers (in thousands)**Cost Management and Labour Relations**

We continue to take proactive measures to contain and manage our expenses as prudently as possible without compromising safe operations. To improve our customer experience and to accommodate the higher traffic volumes, we provided 1,190 additional round trips and introduced three new vessels. These initiatives resulted in an increase in fuel consumption, labour and training related costs.

Wages, benefits and fuel expenses are our largest expense, representing approximately 76% of total operations, maintenance and administration costs. These labour and fuel costs are primarily driven by the level of service. We continuously review all operational costs for efficiencies.

The majority of our employees are members of the BC Ferry & Marine Workers' Union (the "Union"). In fiscal 2016, we announced the ratification of a Memorandum of Agreement that was reached with the Union. This agreement provides certainty for our employees, helps ensure uninterrupted ferry service for our customers and marks 17 years of labour stability. The terms of the new Collective Agreement provide for wage increases aggregating 8.55% over the five-year term of the agreement ending October 31, 2020, which is a 1.71% increase on average per year.

Safety & Security

Safety is our highest priority. Maintaining a safe environment for our customers and employees requires our continued focus and diligence. A significant damage, injury or illness event could have an adverse effect on the lives of our employees and customers. Deliberate, malicious acts could cause operational disruption, death, injury or property damage. The occurrence of a major incident or mishap could negatively affect our ability to meet operational service requirements, the environment, staff morale, our reputation and our financial position and results of operations. The effectiveness of policies and procedures, equipment, maintenance, training, supervision, facility design and security measures reduces the risk to passenger and employee safety and/or property damage.

We have an internal control framework with defined control objectives for information and related technology, which guides our governance and control processes. This assists us in ensuring the security, confidentiality and integrity of our information. Our prime data centre facility is in a location to mitigate risk in the event of a major incident such as an earthquake. Our current infrastructure site has been expanded to house our pre-production infrastructure and serve as our production environment for disaster recovery in the unlikely event that the data centre production services are interrupted.

We have significant food and beverage sales, both on our vessels and at our terminals, and there is a risk of a foodborne illness contracted from contaminated products purchased from our food services. Our food storage, handling, preparation and cooking procedures are aligned with the hazard analysis critical control point methodology which is a preventive approach to ensuring food safety.

Our 24-hour operations and security centre ("OSC") officially began operations in 2009 and is a central location for monitoring day-to-day operations and providing incident management support. The primary purpose of the OSC is to collect information from throughout the Company, and to provide enhanced situational awareness and assessments, increased security monitoring and a coordinated response during any incidents. Security initiatives are in place to counter intentional attacks and we are in regular contact with government security agencies to ensure we have the latest information.

We have a sound conventional insurance program designed to mitigate the financial impact of a major incident; however, there can be no guarantee that the insurance coverage will be sufficient to cover all such incidents.

On September 6, 2017, we received the DuPont Global Safety Award, which recognized BC Ferries' achievements and commitment to safety excellence through our safety program ("SailSafe"), a joint initiative of the company and the B.C. Ferry and Marine Workers' Union. The DuPont Safety and Sustainability Awards recognize outstanding initiatives across all industries worldwide aimed at enhancing workplace safety, sustainability and operational effectiveness.

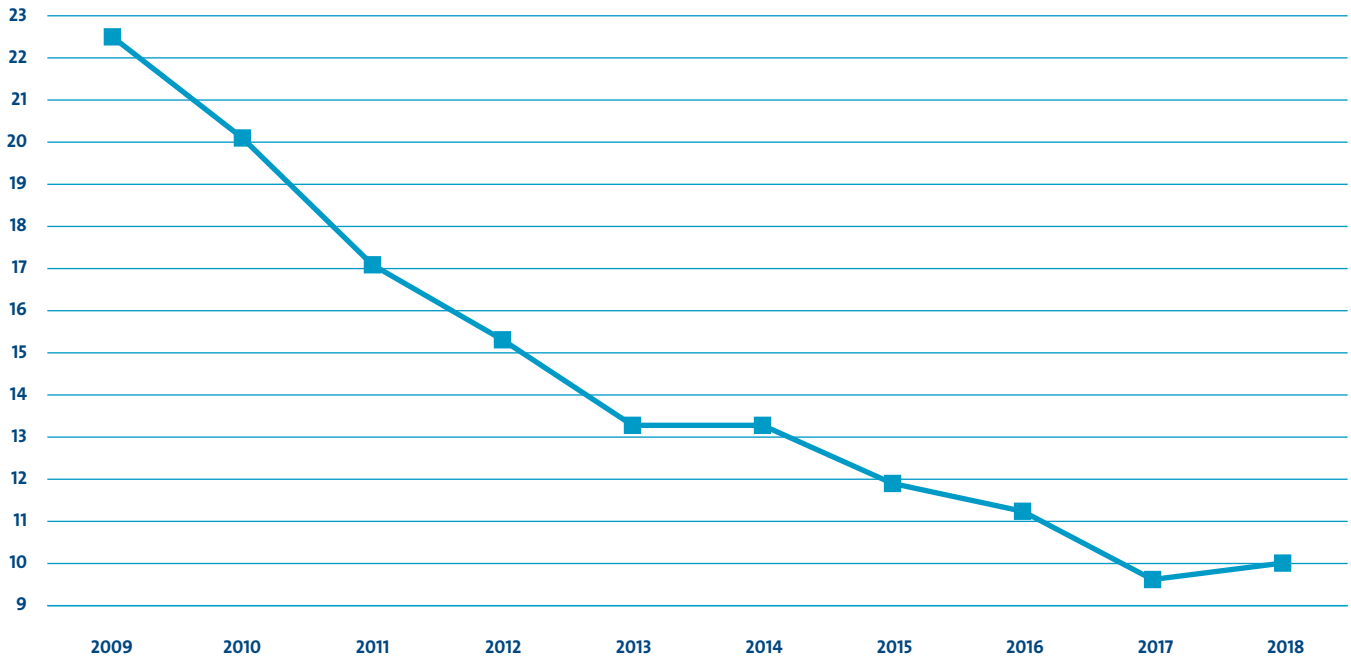
SailSafe, launched in fiscal 2007, is designed to achieve world-class safety performance. SailSafe embodies safety as a normal part of all business activities and ensures that safety is kept as the primary concern in the minds of our employees. SailSafe is driven by our employees, who play a vital part in identifying areas and methods for enhancing current safety practices. In addition to their normal duties, over 400 employees are also engaged in identifying areas for improvement, developing plans and implementing new or revised processes. We continue to work towards ensuring safety becomes completely ingrained in every activity undertaken, every day, throughout our business.

As part of the SailSafe program, we upgraded our safety management system ("SMS") including an operational risk assessment and management process. The SMS focuses on occupational and operational safety and ensures an avenue for auditing, reporting, investigating and tracking of policies, procedures and incidents to prevent future incidents and evaluate trends enabling the ability to identify changes to risk in specific areas.

In fiscal 2018, we carried 22.0 million passengers. The injuries to passengers increased from 202 to 220 compared to fiscal 2017. These passenger injuries consisted mainly of slips, trips or falls and occurred primarily on the vessels. Passenger injuries of 220 is an injury rate of .00001% or 10.01 injuries per one million passengers. Overall, our investments in safety have yielded significant positive results as injuries to passengers have declined 52.8% over the last 10 years. The number of injuries per 1 million passengers for fiscal years 2009 through 2018 can be seen on the following page:

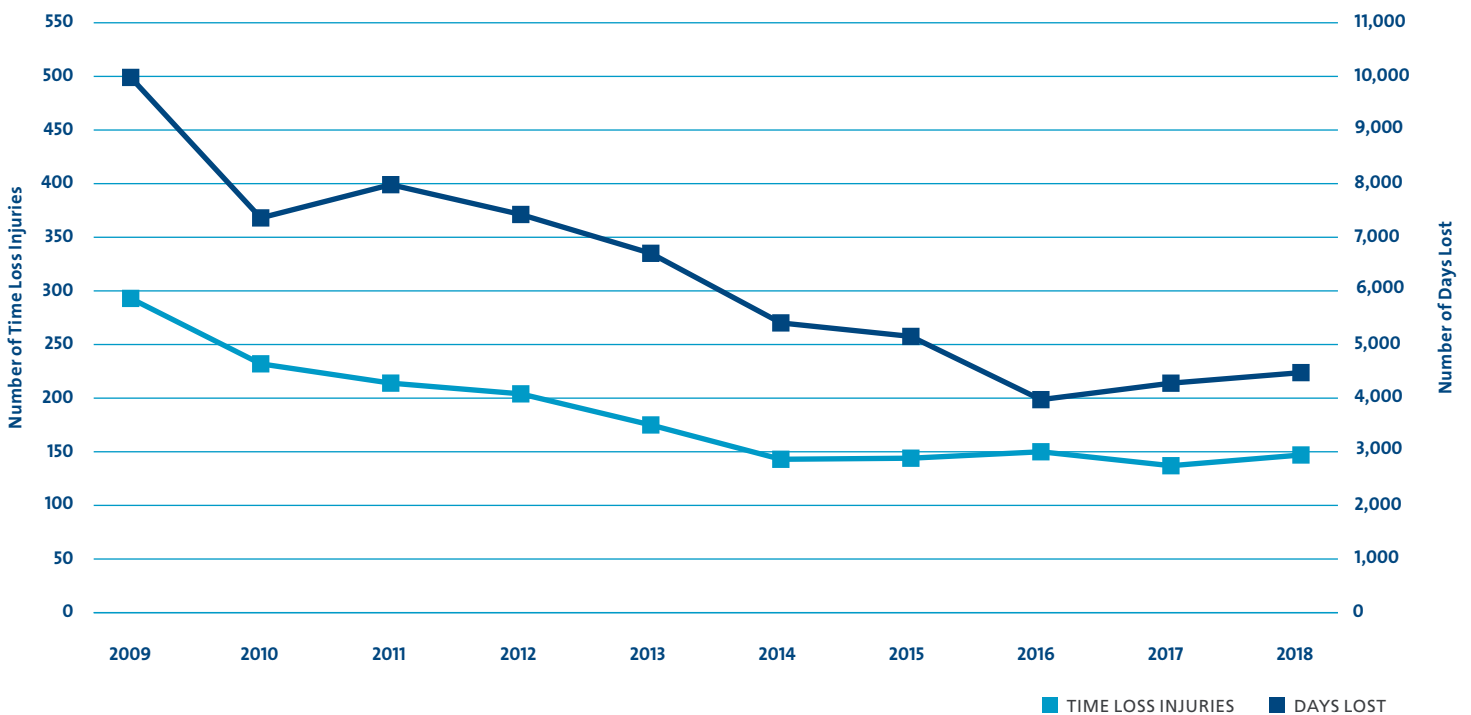
Passenger Safety Index

Number of Injuries Per One Million Passengers



In fiscal 2018, the number of time loss injuries to employees increased from 137 in fiscal 2017 to 147. Overall since 2009, the number of time loss injuries we experience each year has dropped by 49.8% and the number of days lost due to injury has declined by over 5,500. The results for fiscal 2009 through fiscal 2018 are below:

Employee Safety Performance



On April 18, 2018, we experienced a mechanical failure of a davit for the *Queen of Cumberland's* rescue boat which resulted in physical injuries to two employees. There are investigations underway by WorkSafeBC, the Transportation Safety Board and our own internal safety department. Any remediation plans related to this incident will be informed by these reports.

We adhere to a program of internal and external safety audits designed to verify our compliance with our safety management system. We first received the Certificate of Recognition ("COR") from WorkSafeBC in fiscal 2014. A COR recognizes companies that go beyond the legal requirements of the *Workers' Compensation Act* and the Occupational Health & Safety Regulations by taking a best practices approach to implementing health, safety and return to work programs. A COR requires recertification every three years. As a result of receiving the COR, WorkSafeBC provided us with rebates of approximately \$0.6 million of assessed premiums in each year from 2013 to 2017. During fiscal 2018, the COR audit resulted in a 92% score in Health and Safety and 93% score in Injury Management. In the first quarter of fiscal 2019, we expect to receive confirmation of renewal of the COR.

In addition to the COR rebate and effective for January 1, 2017, WorkSafeBC reduced our net premium rate, resulting in approximately \$2 million in premium savings per year, in recognition of our SailSafe program and its focus on safety and reducing time loss injuries.

Environment

We are committed to safeguarding the environment. Our operations are subject to federal, provincial and local environmental laws and regulations dealing with various operations, including solid and liquid waste management, air quality and oil spill response.

We comply with environmental laws and regulations and actively search for ways to improve our environmental performance to help us become an industry leader in environmental management. If we were to be involved in an environmental accident or to be found in material violation of applicable law and regulations, we could be responsible for material clean-up costs, repair of property damage, and fines or other penalties. Our environmental policy provides a framework for setting environmental targets and encouraging best practices.

Our "SeaForward" program is an initiative that brings together our existing environmental activities, conservation efforts, community investments and new sustainability endeavours. Our initial focus for the program includes increasing composting and recycling, the tracking of whale sightings in association with the BC Cetacean Sightings Network, and our employees actively participating in the Great Canadian Shoreline Clean-up.

We continue to improve our training programs, including training our staff in environmental awareness and first response to an oil spill. In fiscal 2018, we added environmental processes to our SMS to ensure improved monitoring of environment spills and, in fiscal 2018, immediately addressed 29 minor environmental incidents compared to 13 in the prior year. Our aging vessels can experience mechanical issues from time-to-time that may result in small oil leaks. In fiscal 2018, the 52-year old *Queen of Burnaby* and the 53-year old *Queen of Nanaimo* were decommissioned. In fiscal 2019, the 45-year old *Nimkish* will be replaced by the *Northern Sea Wolf*. The 54-year old *Howe Sound Queen* and the 60-year old *North Island Princess* are in our capital plan to be replaced in 2020.

We joined Green Marine in 2014 and were certified in two areas of operations, as a ship owner and terminal operator by an independent verifier in May 2015. Green Marine is a globally-recognized and voluntary industry sustainability initiative for ship operators, ports, terminals and shipyards. Green Marine participants try to reduce their environmental footprint by undertaking concrete and measurable actions. In 2017, we also received certification as a shipyard, making us one of three organizations with participation in three different areas of operations (shipyard, ship owner and terminal operator). Environmental performance is annually benchmarked through the program's comprehensive self-evaluation guides and the results are verified by an accredited external verifier. Our level of achievement for each Green Marine performance indicator is published annually on the Green Marine website at <https://www.green-marine.org/certification/results/>.

We participate in the Enhancing Cetacean Habitat Observation Program ("ECHO"), established by Port of Vancouver, in collaboration with government agencies, First Nations, marine industry users, non-government organizations and scientific experts, to better understand and manage the potential impacts to cetaceans (whales, porpoises and dolphins) from commercial vessel activities. The long-term goal of ECHO is to develop mitigation measures that will lead to a quantifiable reduction in potential threats to cetaceans, which include acoustic disturbance, physical disturbance and environmental contaminants. Since 2015, we have undertaken two noise measurement projects in addition to voluntary transiting the ECHO program's underwater listening station to help the port gather the baseline of ambient noise in the Salish Sea.

We constantly look for clean and innovative technology to reduce fuel consumption and emissions on our vessels. Both LNG and the marine diesel we currently use meet all current domestic and international emissions regulations. We have implemented a wide variety of fuel-saving measures ranging from operating our vessels more efficiently to installing new, more fuel-efficient engines on some of our vessels and fuel monitoring systems on others, and designing and building our new vessels to meet or exceed current environmental standards. Our cable ferry, the *Baynes Sound Connector*, consumes approximately 50% less fuel compared to the previous vessel providing the service.

We are also actively pursuing alternative fuel options for new vessels and vessels undergoing major retrofits because we believe alternate fuels would reduce emissions as well as costs. Our three Salish Class ferries, which entered service in fiscal 2018, are dual-fuel capable and are operated as much as possible on LNG. The Salish Class ferries were the first passenger vessels in the world to fuel LNG on an open vehicle deck via delivery truck. We expect the mid-life upgrade, including conversion to dual-fuel, of the *Spirit of British Columbia* and the *Spirit of Vancouver Island* to reduce CO₂ emissions by 12,500 tonnes annually, the equivalent of taking approximately 2,500 vehicles off the road per year, by using natural gas. Our new minor class vessels will initially operate on marine diesel fuel with stored energy (battery) capability installed to provide the ship's service power. The stored energy capability will be expandable for a possible zero-emission operation (the battery would supply the ship's full power requirement) in the future.

We continue to expand our composting program and to replace chemical products with more environmentally-friendly solutions. We use biodegradable hydraulic oils and recycle beverage containers, cardboard, newsprint, plastics, wood, metal, spent fluorescent tubes, batteries, aerosol spray cans, old upholstery foam and used cooking oil. We transfer vessels to shore-power while berthed overnight at several of our terminals, promoting anti-idling and increasing waste diversion. We expanded our shore-power program to additional terminals by upgrading the current shore power installations and adding new shore-power installations where necessary to provide sufficient capacity to provide power to the vessels.

We have introduced other initiatives to further mitigate our environmental impact. We have a sewage and wastewater treatment system so that wherever possible, the vessels convey sewage to a terminal through pump-ashore infrastructure. Where terminal facilities were not available, small vessels were fitted with holding tanks, with truck pump-off. In all other cases, the vessels have been fitted with federally compliant marine sanitation devices. We have treatment plants at four of our terminals, while at another seven, sewage is collected and transferred to treatment plants operated by local governments.

Training

We were named one of B.C.'s Top Employers (2018) for the second year in a row. This is an annual competition organized by the editors of Canada's Top 100 Employers and recognizes workplaces for offering progressive and forward-thinking programs for employees. In conjunction with the Union and our employees, we established Sailsafe, a comprehensive safety program, including a health and wellness component, and invest heavily in extensive training and development opportunities.

Skilled trades are essential to keeping our operations safe and efficient. Camosun College is the largest provider of trades training, including marine trades, on Vancouver Island. We have invested in the SailSafe Simulator at Camosun College's new trades facilities to guarantee access to the best training tools. The SailSafe Nautical Simulation lab is a 12-station teaching facility that allows trainees the experience of navigating in local waters, in a range of conditions, while interacting with other vessel traffic operated by their classmates. We also have a cadet program that includes participants from the British Columbia Institute of Technology, Georgian College of Ontario, and the Memorial University of Newfoundland.

In fiscal 2018, we provided over 28,000 personal training days, an increase of 17% over fiscal 2017. This includes training on the Salish Class vessels as well as job specific, simulation and safety training.

Operational training focused on many programs, including new hire orientation, oil spill response, Foodsafe, prevention of violence in the workplace and LNG. Training is provided on-line and in the classroom as well as through practicing exercises and drills.

Our Simulator Training Centre program provides training to operational crew in many areas including operations skill, navigation tools, communication and team decision making. Our signature course is Bridge Operations Skills and Systems, for which we received a Lloyd's List Safety Training award for outstanding commitment in training our employees ashore and at sea. It focuses on gaining, maintaining and enhancing shared bridge team situational awareness and allows us to construct simulation activities and scenarios to customize the education.

Our award-winning Standardized Education and Assessment ("SEA") program leverages technology and e-learning to enhance hands-on training in a phased, auditable and sustainable manner. Our SEA program has customized programs specific to the job, vessel, route or terminal. There are now 51 job positions supported by SEA materials and education. Our SEA program provides all employees with easy access to resources and materials and assists in planning and tracking employee career progression and succession.

We developed a comprehensive training plan for familiarization with the new equipment on the Salish Class vessels. This plan includes LNG training, manufacturer's equipment training and SEA and operational training for all employees working on a Salish Class vessel. A web-based LNG safety awareness program provided training to all employees involved with the Salish Class vessels, with additional advanced LNG training for deck and engineering crews. By the time all three Salish Class vessels commenced regular service in fiscal 2018, more than 5,000 days of training had been completed. This LNG training program is also being provided to employees involved with the Spirit Class vessels as we convert the vessels to dual-fuel and in fiscal 2018, almost 1,000 days of training had been completed.

Customer Service

Our long-term vision incorporates operational and financial sustainability, environmental and community well-being goals and a focus on enhancing the customer experience. Our strategic planning process captures internal and external factors as well as direct input from our community engagement process.

In fiscal 2018, our on-time performance rate was 89.0%, with a fleet reliability score of 99.83%. This reliability score means that only 0.2% of sailings in fiscal 2018 were cancelled due to mechanical issues related to the vessels or terminals, or crew availability. Our 2017 Customer Service Satisfaction Tracking Surveys indicated that 87% of customers surveyed (compared to 88% in 2016) reported being satisfied with their overall trip experience. A copy of the full report is available at http://www.bcferrys.com/about/cst_archive.html.

We will continue to survey our customers to understand and to identify ways to enhance their experience. We have a customer service enhancement program that targets training for all customer-facing employees on three key attributes of friendliness, communication and listening skills, and professionalism. We are striving to make every individual customer interaction a safe, positive and satisfying experience. In fiscal 2018, we implemented a Transport Canada regulation that addresses safety concerns by restricting passengers from remaining in their vehicles on closed car decks. Where possible, we accommodate customers with special circumstances that need to remain in their cars. We also introduced a smoke-free environment in all of our terminals and vessels to support the health and wellness of our customers and our employees.

We have an active public consultation and community engagement program and continue to work closely with 13 ferry advisory committees ("FAC") that represent the ferry-dependent communities we serve. These committees are appointed in cooperation with local governments, the Islands Trust and First Nations and discuss day-to-day operations, planned improvements, broader policy issues and strategic planning.

In fiscal 2018, we actively engaged and will continue to engage with stakeholders to improve service and better align customer needs with sailing schedules, as well as balance seasonal service, capacity and demand with operating efficiencies, through the use of surveys, open houses, public meetings, community working groups, FAC and meetings with community leaders. Following a broad public engagement, we revised schedules for these routes: Horseshoe Bay – Langdale, Horseshoe Bay – Snug Cove, and Earls Cove – Saltery Bay. The revised schedules will provide the service our customers have requested: on-time departures, increased capacity, transit connections and later sailings out of Horseshoe Bay.

We consulted with stakeholders and asked for their input on such areas as amenities, lounge configuration, car deck arrangement, accessibility and tourism features of two new minor class vessels which will join the fleet by 2020. These vessels will be the first two of this class to be built. Feedback and operational experience will be incorporated into the design of the vessels to ensure high levels of safety, customer service, environmental leadership and reliability.

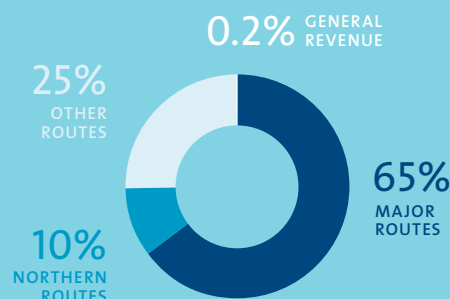
We are consulting with stakeholders and asking for their input on the future of Horseshoe Bay and Swartz Bay terminals. The visioning process is the first of three phases of terminal redevelopment. It will be followed by involving communities in a detailed design process over the next two to four years.

Revenue and Operational Statistics

The following discussions of revenue are based on IFRS results, with reference to the impacts of rate regulation (See "The Effect of Rate Regulation").

Total revenues and selected operational statistics over the past three fiscal years are shown in the tables below.

In fiscal 2018, the greatest portion of our revenues, 65%, was earned on our Major Routes. Revenue from the Northern Routes contributed 10% and revenue from Other Routes contributed 25%.



	2018	2017	2016
Operational Statistics			
Vehicle traffic	8,723,435	8,305,842	8,069,489
% increase	5.0%	2.9%	4.9%
Passenger traffic	22,030,228	21,034,756	20,689,087
% increase	4.7%	1.7%	4.5%
On-time performance	89.0%	89.5%	90.8%
Number of round trips	79,082.0	77,892.0	76,871.5
Capacity provided (AEQs)	15,165,616	15,210,705	14,635,207
AEQs carried	9,889,671	9,437,585	9,152,873
Capacity utilization	65.2%	62.0%	62.5%

In fiscal 2018, vehicle and passenger traffic increased 5.0% and 4.7%, respectively, compared to fiscal 2017. Overall, we believe traffic continued to be positively impacted by favourable economic activity in British Columbia and the lower Canadian dollar. We believe our vehicle fare pricing promotions also had a positive impact on both passenger and vehicle traffic.

In fiscal 2017, vehicle and passenger traffic increased 2.9% and 1.7%, respectively, compared to fiscal 2016. We believe traffic in fiscal 2017 was favourably impacted by the lower Canadian dollar, continued increases in tourism and general economic activity in British Columbia, partially offset by the impact of more days of unfavourable weather in the last half of fiscal 2017 compared to the same period in the prior year and no Easter holiday weekends falling in fiscal 2017. Traffic levels in fiscal 2016 were positively impacted by two Easter holiday weekends.

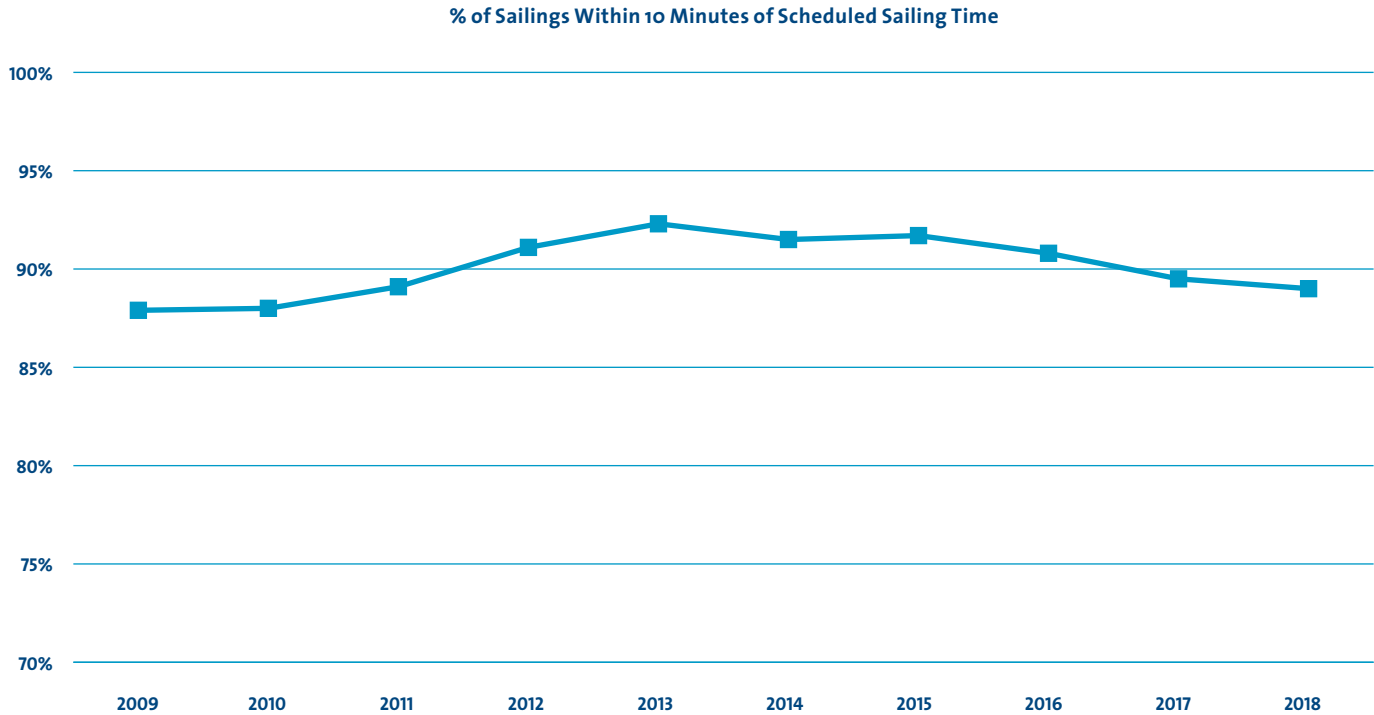
Traffic has also been positively impacted by our travel centre, conveniently located in the tourist sector of downtown Vancouver. Using an integrated marketing approach, we are able to leverage our core business to drive incremental ferry traffic as well as generate commissions from the related services.

From time to time, we utilize promotional fares designed to stimulate growth in traffic or to direct traffic towards our less popular sailings and/or to ensure we are in compliance with approved price cap orders. The utilization of promotional fares is one factor that may cause the average vehicle and passenger tariff rate to be under or over the allowed price cap in any one period. Under the Act, the average vehicle and passenger tariffs cannot be over the price cap for more than four consecutive quarters.

In fiscal 2018, we offered \$8.7 million in discounts to passengers travelling on the Major Routes during the summer, over Thanksgiving, Christmas and during spring break. We believe that discounts to passenger and vehicle fares had a positive impact on both passenger and vehicle traffic. This is approximately \$1.5 million higher than in the prior year. We also believe these pricing promotions played a part in shifting some traffic to off-peak sailings, resulting in higher overall capacity utilization. The promotions are described in the following Major, Northern and Other Route sections.

The on-time performance results for fiscal 2009 through fiscal 2018 are below:

Fleet On Time Performance



On-time performance on the Major and regulated Other Routes is defined as the percentage of our sailings departing within 10 minutes of the scheduled time. On-time performance on the Northern Routes is defined as the percentage of our sailings arriving no later than 10 minutes after the scheduled time. In each case, on-time performance can be impacted by delays due to weather, vessel substitution, terminal dock maintenance or closures and periods of high traffic demand. Meeting customer service expectations in a safe and reliable manner is the principal factor guiding our focus on on-time performance.

In fiscal 2017, on-time performance decreased from 90.8% to 89.5% compared to the prior year, primarily due to the impact from increased traffic demand and delays due to weather. In fiscal 2018, on-time performance decreased from 89.5% to 89.0% compared to the prior year. On-time performance on the regulated Other Routes declined in fiscal 2018, primarily due to the impact from increased traffic demand and delays due to weather, which offset improvement in on-time performance on the Major Routes. Our initiatives to improve on-time performance include adjusting and/or expanding sailing schedules, adjusting crewing schedules and refining vehicle loading processes during peak periods.

An automobile equivalent (“AEQ”) is our standard unit of measure for an approximation of one car length. AEQs are calculated by using a conversion factor for each vehicle type. For example, a passenger vehicle would be one AEQ while a bus would be three AEQs. The change in AEQs from one period to the next may not be proportionate to the change in vehicle traffic, due to variations in the mix of vehicle types (the relative number of buses, commercial vehicles and passenger vehicles) and actual size of vehicles carried.

Vehicle capacity provided, measured in AEQs, is the available vehicle deck space on a vessel multiplied by the number of round trips. The CFSC stipulates, among other things, the minimum number of round trips to be provided for each regulated ferry service route in exchange for ferry transportation fees. The number of round trips provided can be positively or negatively impacted by cancellations due to weather, vessel substitution, terminal dock closures and extra round trips made in response to high demand, or by changes to the number of trips stipulated by the CFSC.

In fiscal 2017, we provided 1,020.5 additional round trips compared to fiscal 2016 and 2.3% more trips than the annual minimum required under the CFSC, mainly due to the increase in traffic demand. Also in fiscal 2017, only a single ramp berth was available for use during the 2½ months of berth construction at Langdale Terminal. To accommodate demand during this time, an alternative service was provided with two vessels using only their main car decks. The upper car decks, although unavailable, are included in the metric for AEQ capacity provided. If we adjusted for this event, AEQ capacity provided would have been 14,939,429 or 2.1% higher, rather than 3.9% higher, in fiscal 2017 than in fiscal 2016. In fiscal 2018, we provided 1,190.0 additional round trips compared to fiscal 2017 and 2,962 more than required under the CFSC, mainly due to the increase in traffic demand. Overall, capacity provided in fiscal 2018, after adjusting for the extra unavailable capacity provided during construction at Langdale, was 1.5% higher than in fiscal 2017.

Capacity utilization in a period is calculated by dividing the AEQs carried during the period by the AEQ capacity provided on the vessels. Capacity utilization is impacted by the number of vehicles carried, the mix of vehicle types, the size of the vessels utilized and the number of round trips in each period.

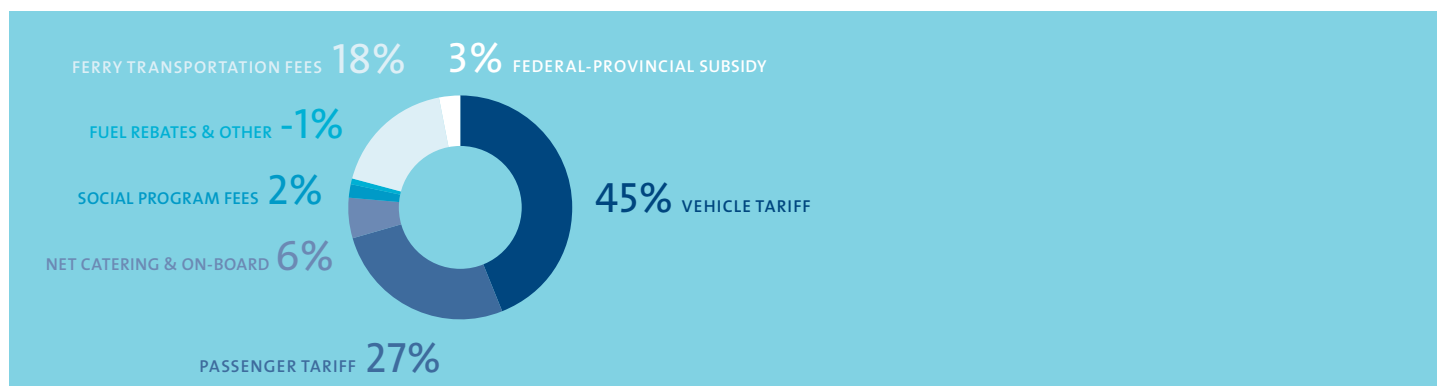
In fiscal 2017, capacity utilization decreased 0.5% compared to the prior year as a result of an increase in capacity provided from additional round trips, mainly offset by a higher number of AEQs carried due to higher traffic levels. If we adjusted for the vessels' extra unavailable vehicle capacity provided during construction at Langdale, capacity utilization during fiscal 2017 would have been 63.1%, rather than 62.0%. In fiscal 2018, capacity utilization increased from the normalized 63.1% to 65.2% compared to the prior year, primarily as a result of a higher number of AEQs carried due to higher traffic levels, partially offset by an increase in capacity provided from additional round trips.

This table provides revenue details for the past three fiscal years.

REVENUE

Years ended March 31 (\$ millions)	2018	2017	2016
Direct Route Revenue			
Vehicle tariff	399.0	380.3	360.9
Passenger tariff	241.2	228.4	218.4
Fuel rebates	(19.4)	(18.1)	(6.4)
Net catering & on-board	57.6	52.9	49.7
Social program fees	17.3	16.9	25.0
Other revenue	10.0	9.3	9.0
Total Direct Route Revenue	705.7	669.7	656.6
Indirect Route Revenue			
Ferry transportation fees	161.2	157.9	147.4
Federal-Provincial subsidy	29.8	29.2	28.7
Total Route Revenue	896.7	856.8	832.7
Other general revenue	2.3	2.5	1.9
Total Revenue	899.0	859.3	834.6

REVENUE SOURCES



Vehicle tariffs (which include reservation fee revenue) and passenger tariffs account for the majority of our revenues. Our year-over-year tariff revenues are impacted by factors such as changes in overall traffic levels, traffic types, and tariff rates.

Catering and on-board services, which includes retail sales, is our second largest source of direct revenue and provides a gross margin of approximately 60%, which contributes favourably to our net earnings and helps to keep fares affordable. Catering, retail and other on-board services are impacted by traffic, price, service quality and product offerings.

In fiscal 2016, tariff increases were 3.9% on average on our Major and regulated Other Routes and 2.0% on average on the Northern Routes. In fiscal 2017, we implemented tariff increases of 1.9% on average, as allowed by the Commissioner's Order 15-03 dated September 16, 2015, by which price cap increases for the four year performance term ending March 31, 2020 were established. In fiscal 2018, we implemented average fare increases below those allowed by the Commissioner. No increases in vehicle fares or passenger fares were implemented on the Horseshoe Bay - Langdale route, the regulated Other Routes, or the Northern Routes. Vehicle fares were increased on average by 1.9% on three of the Major Routes: Tsawwassen - Swartz Bay, Tsawwassen - Duke Point and Horseshoe Bay - Departure Bay. No increase in passenger fares was implemented on these routes. In fiscal 2018 as part of our tariff changes, we also reduced reservation fees.

In fiscal 2017, reservation fee revenue was reduced by \$3.1 million to record GST payable on reservation fee revenue for fiscal years 2014 through 2017, based on CRA audit findings and in fiscal 2018, reservation fee revenue was reduced by \$1.0 million to record GST payable. We strongly disagree with CRA's position and have filed an appeal.

Surcharges and/or rebates are implemented as a direct result of rising and declining fuel prices. In fiscal 2016, due to lower fuel prices, we implemented a fuel rebate of 1% on our Major and regulated Other Routes, which partially mitigated the impact of the tariff increase. In fiscal 2017, we implemented a fuel rebate of 1.9% on the Northern Routes and increased fuel rebates from 1% to 2.9% on our Major and regulated Other Routes. These fuel rebates continued through fiscal 2018. Prior to April 1, 2016, no rebates or surcharges were in place on our Northern Routes.

A history of fuel surcharges in effect for fiscal 2016 through to the current date is below:

DATE RANGE	% SURCHARGE (REBATE)	APPLICABLE ROUTES
April 1, 2015 – March 31, 2016	(1.0%)	Major and regulated Other Routes
April 1, 2015 – March 31, 2016	0.0%	Northern Routes
April 1, 2016 – Present	(2.9%)	Major and regulated Other Routes
April 1, 2016 – Present	(1.9%)	Northern Routes

For the purpose of rate regulation, surcharges and/or rebates are applied to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" for more detail.)

In fiscal 2017, social program fees decreased \$8.1 million and ferry transportation fees increased \$10.5 million, to compensate for the change from 100% to 50% discount and the discontinuance of direct funding for seniors' discounts. In fiscal 2018, the Province contributed an additional \$15 million towards the provision of a new seasonal mid-coast ferry service. Of this, \$3 million was directed to ferry transportation fees on the Northern Routes with the remainder to be directed to ferry transportation fees on the Northern Routes in fiscal 2019 and 2020.

Year to year changes in revenue and operational statistics for the Major, Northern and Other Routes are discussed separately below.

YEAR TO YEAR COMPARISON OF REVENUES AND OPERATIONAL STATISTICS 2018-2017

MAJOR ROUTES

Our Major Routes are our four busiest routes, carrying approximately 60% of our total vehicle traffic and 65% of our total passenger traffic.

	2018	2017
Operational Statistics		
Vehicle traffic	5,181,363	4,973,289
% increase	4.2%	2.6%
Passenger traffic	14,258,286	13,670,182
% increase	4.3%	1.6%
On-time performance	82.8%	80.6%
Number of round trips	13,257.5	13,381.0
Capacity provided (AEQs)	8,257,703	8,339,982
AEQs carried	6,090,940	5,874,018
Capacity utilization	73.8%	70.4%

In fiscal 2018, vehicle and passenger traffic increased 4.2% and 4.3%, respectively, compared to fiscal 2017. We believe traffic continued to be positively impacted by favourable economic activity in British Columbia and the lower Canadian dollar. We believe our vehicle fare pricing promotions also had a positive impact on both passenger and vehicle traffic.

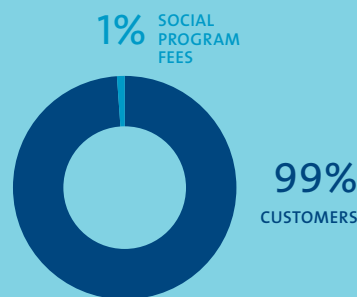
In fiscal 2018, on-time performance on the Major Routes improved 2.2% compared to the prior year, with all routes showing improvement.

We face particular on-time challenges on the routes using Horseshoe Bay terminal. The configuration of the terminal limits our operational flexibility, particularly during periods of high traffic. Our initiatives to continue to improve on-time performance at this terminal have included adjusting and/or expanding sailing schedules, adjusting crewing schedules, changing operational procedures and refining vehicle loading processes during peak periods. These initiatives helped to improve on-time performance on the routes using Horseshoe Bay terminal. The on-time performance on the Horseshoe Bay – Departure route improved 3.1% (from 78.7% to 81.8%) and the Horseshoe Bay – Langdale route improved 0.4% (from 74.3% to 74.7%) in fiscal 2018 compared to the prior year. In fiscal 2017, improvements were offset by a decrease in the on-time performance on the Duke Point – Tsawwassen route, mainly as a result of a 7.1% increase in vehicle traffic compared to the prior year.

If we adjusted for the extra unavailable capacity provided during construction at Langdale in fiscal 2017, capacity utilization during fiscal 2017 would have been 72.8% (AEQs carried of 5,874,018 and capacity provided of 8,068,706), rather than 70.4%. In fiscal 2018, capacity utilization increased from the normalized 72.8% to 73.8% compared to the prior year as a result of a higher number of AEQs carried due to higher traffic levels partially offset by an increase in capacity provided from additional round trips.

We provide drop-trailer service on two of our Major Routes, where commercial customers can drop their trailers off at one terminal and pick them up at the other with our drivers loading and unloading the commercial trailers on and off the ferry with a hostling unit. This service improves our overall productivity by utilizing otherwise unused capacity.

Fiscal 2018 revenue from our Major Routes consisted of 99% from customers and 1% in social program fees from the Province.



REVENUE

Years ended March 31 (\$ thousands)	2018	2017	Increase (Decrease)
Direct Route Revenue			
Vehicle tariff	334,360	321,354	13,006
Passenger tariff	194,998	185,317	9,681
Fuel rebates	(15,667)	(14,790)	(877)
Net catering & on-board	51,101	46,983	4,118
Social program fees	8,714	8,658	56
Parking	5,339	4,929	410
Other revenue	4,117	3,849	268
Total Direct Route Revenue	582,962	556,300	26,662
Indirect Route Revenue			
Ferry transportation fees	–	–	–
Total Route Revenue	582,962	556,300	26,662

In fiscal 2018, the average tariff revenue (tariff revenue divided by traffic volume) per vehicle decreased \$0.51 or 0.8% to \$64.72 compared to the prior year. This was a result of promotional fares offering significant discounts of up to 48% on more than 3,300 sailings along with the reduction in reservation fees. This more than offset the modest increase of 1.9% in vehicle fares. There was no increase in passenger fares. Average tariff revenue per passenger increased \$0.12 or 0.9% to \$13.68 compared to the prior year as a result of the impact of the change in the proportion of traffic on routes with higher versus lower tariffs. The increase in traffic levels and the changes in average fares during fiscal 2018 resulted in a total tariff revenue increase of \$22.7 million compared to the prior year.

In fiscal 2017, we implemented a fuel rebate increase from 1% to 2.9%. These fuel rebates continued through fiscal 2018. For regulatory purposes, these amounts are applied to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" for more detail.)

All vessels that provide service on our Major Routes have a gift shop and options for food service. In fiscal 2018, net revenue from catering and on-board sales increased 8.8% compared to the prior year as a result of both higher passenger traffic and higher average sales per passenger. Food sales remain strong, providing approximately 73% of total catering and on-board revenue. Sales of quality apparel continue to grow and comprise over 11% of total catering and on-board revenue. Cost of goods sold is approximately 40% of total sales.

Social program fees are reimbursements from the Province of discounts provided on fares for students travelling to and from school, persons with disabilities and persons travelling under the Ministry of Health Travel Assistance Program ("MTAP"). In fiscal 2018, social program fees increased compared to the prior year, mainly as a result of an increase in the usage of the MTAP program partially offset by a decrease in the number of students travelling.

Revenue from parking increased 8.3% in fiscal 2018 compared to prior years, as a result of higher traffic levels and proportionately higher usage.

Other revenue increased 7.0% in fiscal 2018 compared to the prior years, mainly as a result of an increase in retail commissions.

All ferry transportation fees were allocated to the Northern and regulated Other Routes.

NORTHERN ROUTES

During fiscal 2017 and fiscal 2018, our Northern Routes consisted of two regulated routes operating on the British Columbia coast north of Port Hardy on Vancouver Island.

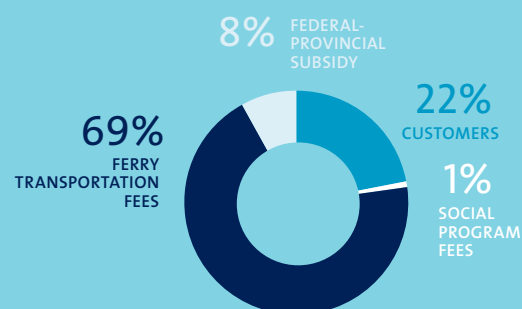
	2018	2017
Operational Statistics		
Vehicle traffic	32,166	31,120
% increase	3.4%	6.9%
Passenger traffic	89,666	86,304
% increase	3.9%	6.7%
On-time performance	88.5%	88.4%
Number of round trips	252.5	233.5
Capacity provided (AEQs)	58,551	54,429
AEQs carried	39,460	38,009
Capacity utilization	67.4%	69.8%

In fiscal 2018, vehicle traffic increased 3.4% and passenger traffic increased 3.9% compared to the prior year. We believe traffic continued to be positively impacted by favourable economic activity in British Columbia and the lower Canadian dollar.

In fiscal 2018, on-time performance was essentially on par with the prior year.

In fiscal 2018, capacity utilization on these routes was 2.4% lower than in the prior year, primarily as a result of increased capacity provided due to an increase in the number of round trips partially offset by a higher number of AEQs carried.

Fiscal 2018 revenue from our Northern Routes consisted of 22% from customers and 78% from the Province (1% social program fees, 69% ferry transportation fees, and 8% from payments under the Federal-Provincial subsidy agreement).



REVENUE

Years ended March 31 (\$ thousands)	2018	2017	Increase (Decrease)
Direct Route Revenue			
Vehicle tariff	9,143	8,633	510
Passenger tariff	7,736	7,240	496
Fuel rebates	(373)	(333)	(40)
Net catering & on-board	1,509	1,383	126
Social program fees	1,109	1,016	93
Stateroom rental	1,691	1,533	158
Hostling & other	237	209	28
Total Direct Route Revenue	21,052	19,681	1,371
Indirect Route Revenue			
Ferry transportation fees	62,284	59,070	3,214
Federal-Provincial subsidy	7,642	7,481	161
Total Route Revenue	90,978	86,232	4,746

No fare increases were implemented on our Northern Routes in fiscal 2018. Average tariff revenue (tariff revenue divided by traffic volume) per vehicle increased \$6.90 or 2.5% to \$284.31 compared to the prior year. This increase is mainly as a result of a shift in the mix of traffic types to those with higher versus lower tariffs and the vehicle promotional discounts offered during the prior year. Average tariff revenue per passenger increased \$2.39 or 2.8% to \$86.28 compared to the prior year. The increase in traffic levels and the shift in traffic during fiscal 2018 resulted in a total tariff revenue increase of \$1.0 million compared to the prior year.

In fiscal 2017, we implemented a fuel rebate of 1.9%, which continued through fiscal 2018.

Net revenue from catering and on-board services increased 9.1% in fiscal 2018 compared to the prior year as a result of higher passenger levels and higher average sales per passenger.

In fiscal 2018, social program fees increased 9.2% compared to the prior year, mainly as a result of an increase in the usage of the MTAP program.

Stateroom rental revenue increased 10.3% in fiscal 2018 compared to the prior year, due to increased utilization and higher passenger levels.

In fiscal 2018, ferry transportation fees received from the Province increased 5.4% compared to the prior year as a result of additional funding from the Province for the provision of additional services.

The Federal-Provincial subsidy increased by the change in the annual CPI (Vancouver).

OTHER ROUTES

Our Other Routes primarily serve the northern and southern Gulf Islands and the northern Sunshine Coast. One of the 18 regulated routes and all eight of the unregulated routes are operated under contract by alternative service providers. We receive fees from the Province for the provision of contracted services on these routes, which are included in the ferry transportation fees discussed below. Operational statistics for the unregulated routes are not incorporated in the following analysis.

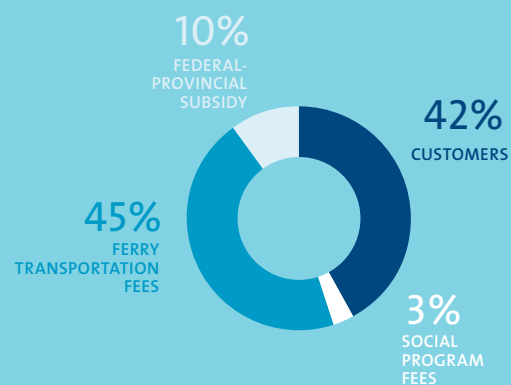
	2018	2017
Operational Statistics		
Vehicle traffic	3,509,906	3,301,433
% increase	6.3%	3.4%
Passenger traffic	7,682,276	7,278,270
% increase	5.6%	1.7%
On-time performance	90.2%	91.2%
Number of round trips	65,572.0	64,277.5
Capacity provided (AEQs)	6,849,362	6,816,294
AEQs carried	3,759,271	3,525,558
Capacity utilization	54.9%	51.7%

In fiscal 2018, vehicle traffic increased 6.3% and passenger traffic increased 5.6% compared to the prior year. We believe traffic continued to be positively impacted by favourable economic activity in British Columbia and the lower Canadian dollar.

In fiscal 2018, on-time performance decreased 1.0% from the prior year, primarily due to the impact from increased traffic demand, vessel substitutions and delays due to weather.

In fiscal 2018, capacity utilization on these routes was 3.2% higher compared to the prior year, primarily due to a higher number of AEQs carried partially offset by an increase in capacity provided, mainly due to an increase in the number of round trips.

Fiscal 2018 revenue from our Other Routes consisted of 42% from customers and 58% from the Province (3% social program fees, 45% ferry transportation fees, and 10% from payments under the Federal-Provincial subsidy agreement).



REVENUE

Years ended March 31 (\$ thousands)	2018	2017	Increase (Decrease)
Direct Route Revenue			
Vehicle tariff	55,509	50,318	5,191
Passenger tariff	38,488	35,850	2,638
Fuel rebates	(3,346)	(2,945)	(401)
Social program fees	7,509	7,253	256
Net catering & on-board	3,256	2,950	306
Parking & other	319	349	(30)
Total Direct Route Revenue	101,735	93,775	7,960
Indirect Route Revenue			
Ferry transportation fees	98,924	98,874	50
Federal-Provincial subsidy	22,141	21,677	464
Total Route Revenue	222,800	214,326	8,474

No fare increases were implemented on the regulated Other Routes in fiscal 2018. Average tariff revenue (tariff revenue divided by traffic volume) per vehicle increased \$0.57 or 3.8% to \$15.82 compared to the prior year, reflecting an increase in the proportion of traffic on routes with higher versus lower tariffs, an increase in the proportion of higher tariff vehicle types, and the impact of pricing promotions in the prior year. In fiscal 2018, average tariff revenue per passenger increased \$0.08 or 1.7% to \$5.01 compared to the prior year mainly as a result of an increase in the proportion of higher versus lower passenger fares. These changes in average tariff revenue resulted in total tariff revenue increase of \$7.8 million compared to the prior year.

On April 1, 2016, we implemented a fuel rebate increase from 1% to 2.9%. These fuel rebates continued through fiscal 2018.

In fiscal 2018, social program fees increased 3.5% compared to the prior year, mainly as a result of an increase in the number of students travelling and the increased usage of the MTAP program.

Net revenue from catering and on-board services increased 10.4% in fiscal 2018 compared to the prior year, mainly as a result of higher passenger traffic.

The Federal-Provincial subsidy increased by the change in the annual CPI (Vancouver).

EXPENSES

Expenses for the past three fiscal years are summarized in the tables below:

Years ended March 31 (\$ millions)	2018	2017	2016
Operating expenses			
Operations	496.8	467.2	449.6
Maintenance	87.6	74.2	79.4
Administration	38.4	35.8	34.5
Total operations, maintenance & administration	622.8	577.2	563.5
% increase	7.9%	2.4%	3.0%
Depreciation and amortization	159.9	149.0	145.5
Total operating expenses	782.7	726.2	709.0

To improve our customer experience and to accommodate the higher traffic volumes, we provided 1,190 additional round trips and introduced three new vessels in fiscal 2018. These initiatives resulted in an increase in fuel consumption, labour and training related costs. We continue to take proactive measures to contain and manage expenses while operating a sustainable, safe and reliable service.

Our fiscal 2018 total operations, maintenance and administration expenses increased \$45.6 million from fiscal 2017. In fiscal 2018, wages, benefits and fuel expenses totalled \$474.5 million or 76% of total operations, maintenance and administration costs. These labour and fuel costs are primarily driven by the level of service. We continuously review all costs for efficiencies that can be realized without compromising safety and the customer experience.

Years ended March 31 (\$ millions)	2018	2017	2016
Net finance and other expenses			
Finance expense	60.7	58.8	60.6
Less: finance income	(5.5)	(4.7)	(4.6)
Net finance expense	55.2	54.1	56.0
Loss on disposal and revaluation of property, plant and equipment, and intangible assets	1.2	1.6	–
Total net finance and other expenses	56.4	55.7	56.0

Year over year changes are described below:

YEAR TO YEAR COMPARISON OF EXPENSES 2018 – 2017

The \$29.6 million increase in operations expenses from fiscal 2017 to fiscal 2018 consists of:

- \$17.7 million increase in wages and benefits costs, mainly due to staffing for the additional round trips provided, a wage rate increase of 1.5% effective April 1, 2017 in accordance with the Collective Agreement with the Union, an increase in overtime, and an increase in hours spent on training activities;
- \$2.6 million increase in contracted services, which includes terminal redevelopment planning, security and traffic control costs;
- \$2.0 million increase in fuel expense, reflecting an increase of a \$1.6 million or 1.6% increase in fuel consumption and \$0.4 million or 0.4% due to higher fuel prices;
- \$1.7 million increase in costs primarily due to a hydraulic issue with a controllable pitch propeller on the *Spirit of Vancouver Island* which resulted in emergency drydocking;
- \$1.6 million increase in crew deployment costs as a result of training activities;
- \$1.6 million comprised of increases in parts and supplies, mainly resulting from increased traffic volumes; and
- \$2.4 million increase in other costs including credit card fees, promotional advertising and computer software licences.

The \$13.4 million increase in maintenance costs compared to the prior year is as a result of the cyclical nature of vessel refit activity, unplanned vessel maintenance and timing of repairs to our terminals.

The \$2.6 million increase in administration costs is mainly the result of higher wages and benefits partially resulting from filling positions that were vacant in the prior year.

Depreciation and amortization increased \$10.9 million, reflecting new capital assets that have entered service. (See "Investing in our Capital Assets" below for details of capital asset expenditures in fiscal 2018.)

Net finance and other expenses increased by \$0.7 million from fiscal 2017 to fiscal 2018 mainly due to:

- \$1.1 million increase in interest on KfW loans, reflecting interest on the additional KfW loans for the Salish Class vessels; and
- \$0.6 million increase in amortization of debt issue costs;

partially offset by:

- \$0.8 million increase in interest on investments; and
- \$0.4 million decrease in loss on asset disposals.

YEAR TO YEAR COMPARISON OF EXPENSES 2017 – 2016

The \$17.6 million increase in operations expenses from fiscal 2016 to fiscal 2017 consists of:

- \$14.0 million increase in wages and benefits costs, mainly due to the April 1, 2016 rate increase of 1.5% under the Collective Agreement and an increase in overtime and in hours spent in training activities;
- \$2.6 million increase in contracted services, which includes vessel replacement and traffic control costs;
- \$1.1 million increase in crew deployment costs as a result of training activities; and
- \$2.5 million comprised of increases in parts and supplies, insurance claims, credit card fees, training supplies and computer software licences;

partially offset by:

- \$2.6 million decrease in fuel expense, reflecting a decrease of \$5.3 million or 5.0% due to lower fuel prices, partially offset by a \$2.7 million or 2.6% increase in fuel consumption primarily a result of additional round trips provided on the Major Routes.

The \$5.2 million decrease in maintenance costs compared to the prior year resulted from the cyclical nature of vessel refits and the timing of repairs to our terminals.

The \$1.3 million increase in administration costs is mainly the result of increased computer software licencing costs, training supplies and advertising costs.

Depreciation and amortization increased \$3.5 million, reflecting new capital assets that have entered service.

Net finance and other expenses decreased by \$0.3 million from fiscal 2016 to fiscal 2017 mainly due to:

- \$1.3 million increase in interest capitalized; and
- \$0.5 million decrease in interest on KfW loans, reflecting \$24.0 million in principal repayments;

partially offset by:

- \$1.6 million increase in loss on disposal and revaluation of property, plant and equipment and intangible assets, primarily due to asset impairment recorded in fiscal 2017.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity and Capital Resources

We fund our operations and capital acquisitions with cash flow generated from operations, as well as bank financing and debt issues. Our financial position could be adversely affected if we fail to arrange sufficient and cost-effective financing to fund, among other things, capital expenditures and the repayment of maturing debt. This is subject to numerous factors, including the results of our operations, our financial position, conditions in the capital and bank credit markets, ratings assigned by rating agencies and general economic conditions.

We deem liquidity risk to be low at this time and we do not foresee the need to access the capital markets in the near term.

We expect our cash requirements, in the near term, will be met through operating cash flows, funding under government programs and by accessing our credit facility from time to time. At March 31, 2018, our unrestricted cash and cash equivalents and other short-term investments totalled \$70 million and \$114 million, respectively (at March 31, 2017 - \$72 million and \$116 million, respectively). Our unrestricted cash and cash equivalents include cash on hand and fixed rate instruments with a maturity of three months or less. Other short-term investments include fixed rate instruments with a maturity of more than three months.

Over the last five years, our capital expenditures averaged \$191 million annually. Over the next five years, we expect the average to increase to approximately \$380 million annually (excluding external funding) as we proceed with the replacement and upgrade of our aged vessels and make significant improvements at our terminals serving our Major Routes, as well as making investments in information technology.

On March 21, 2017, the Government of Canada approved funding of up to \$15.1 million under the New Building Canada Fund towards a new seasonal direct ferry service between Port Hardy and Bella Coola. In addition to the \$15.1 million, in fiscal 2017, the Government of Canada also approved funding of up to \$45.4 million under the New Building Canada Fund towards the purchase of two new minor class vessels and major upgrade of our Langdale terminal. In total, up to \$60.5 million in funding under the New Building Canada Fund has been approved. In fiscal 2018, we recorded \$14.9 million in funding; comprising \$3.1 million for the New Minor Class vessel project and \$11.8 million for the *Northern Sea Wolf* project.

We are party to a credit agreement with a syndicate of Canadian banks that is secured under the Master Trust Indenture (May 2004) ("MTI"). Under this credit agreement, we have available a revolving facility in the amount of \$155 million. Our \$155 million credit facility was renewed on March 19, 2018 to extend the maturity date of the facility from April 2022 to April 2023. The facility is available to fund capital expenditures and for other general corporate purposes. At March 31, 2018, March 31, 2017 and March 31, 2016 there were no draws on this credit facility.

We target maintaining a strong investment-grade credit rating to allow capital market access at reasonable interest rates. On January 16, 2018, DBRS upgraded our Issuer Rating and Senior Secured Bonds Rating from "A" with a positive trend to "A (high)" with a stable trend. DBRS states that the upgrades "acknowledge the proven operating resilience and reliable management demonstrated by the Company, having weathered challenging macroeconomic conditions while maintaining satisfactory financial metrics and successfully returning to growth". At March 31, 2018, our credit rating with Standard & Poor's was "AA-" with a positive outlook and with DBRS was "A (high)" with a stable trend.

Our debt service coverage (earnings before interest, taxes, depreciation, amortization, and rent) is required to be at least 1.25 times the debt service cost under the credit agreement. We must also ensure that our leverage ratio (total borrowings as a percentage of total borrowings plus shareholders equity) does not exceed 85%. At March 31, 2018, we achieved a debt service coverage ratio of 2.79 and a leverage ratio of 72.5%.

Long-Term Debt

Our long-term debt at March 31 of the last three years is summarized below:

(\$ millions)	EFFECTIVE INTEREST RATE	PRINCIPAL OUTSTANDING AS AT MARCH 31		
		2018	2017	2016
Senior Secured Bonds				
6.25%, due October 2034	6.41%	250	250	250
5.02%, due March 2037	5.06%	250	250	250
5.58%, due January 2038	5.62%	200	200	200
4.70%, due October 2043	4.75%	200	200	200
4.29%, due April 2044	4.45%	200	200	200
12 Year Loans				
Tranche A, due March 2020	5.17%	15	23	30
Tranche B, due March 2020	2.00%*	23	22	22
Tranche A, due June 2020	5.18%	17	24	32
Tranche B, due June 2020	2.02%*	23	23	23
2.95% Loan, due January 2021	3.08%	27	36	45
2.09% Loan, due October 2028	2.70%	40	44	–
2.09% Loan, due January 2029	2.68%	41	45	–
2.09% Loan, due January 2029	2.70%	41	–	–
		1,327	1,317	1,252

*Floating rate as at March 31, 2018

In 2004, we entered into the MTI, a copy of which is available at www.SEDAR.com. The MTI established common security and a set of common covenants for the benefit of our lenders. Our financing plan encompasses an ongoing program capable of accommodating a variety of corporate debt instruments and borrowings ranking *pari passu*. We do not currently view common share equity as a potential source of capital and have no intention of offering common shares to the public or other investors.

Of the five senior secured bond offerings outstanding to date, all have interest payable semi-annually. The bonds are redeemable in whole or in part, at our option.

We have entered into three 12-year amortizing loan agreements with KfW, each of which is secured under the MTI. Two of these loans have a Tranche A at a fixed interest rate of 4.98%, payable quarterly. These agreements deferred the principal payments for three years to a second tranche (Tranche B) on which interest is payable at a floating rate and the principal is due at maturity (March 2020 and June 2020). The third loan is at a fixed interest rate of 2.95%, payable semi-annually.

On November 12, 2015, we executed an export loan agreement with KfW IPEX-Bank GmbH, a German export credit bank. This loan agreement is secured under the MTI and allows for three loans of up to \$45 million each. These amortizing loans will be repaid over a 12-year term and bear interest at 2.09% per annum. In fiscal 2017, we drew down a total of \$90 million, to coincide with the contract payment schedules for the purchase of the *Salish Orca* and the *Salish Eagle*. During the quarter ended June 30, 2017, we drew down the third and final \$45 million, to coincide with the contract payment schedule for the *Salish Raven*. The net proceeds were used to partially finance the purchase of these vessels.

Terminal Leases

We entered into a master agreement with the BC Transportation Financing Authority ("BCTFA") effective March 31, 2003 as part of the restructuring of our Company. In return for the transfer of ownership interest in all ferry terminals from the former British Columbia Ferry Corporation to the BCTFA at the time of the corporate restructuring, we received recognition of prepayment of rent under terminal leases.

The leases grant us exclusive access and use of ferry terminal properties for a period of 60 years commencing April 1, 2003. The leases are renewable for an additional period of 20 years at a total cost of \$20 per lease provided the CFSC is renewed. We must manage, maintain and develop the terminals at our own cost.

Since the original transfer, a total of \$11.7 million of additional lands at Horseshoe Bay, Swartz Bay and Departure Bay have been added to the existing terminal leases in exchange for highway improvements.

If we fail to meet our obligations under the terminal leases or default under the CFSC, the BCTFA may, at its option, re-enter and take possession of the ferry terminal properties and, at its option, terminate the leases. The BCTFA has entered into an acknowledgement agreement with the Trustee under the MTI which sets out certain limitations on the use of this option. We mitigate this performance risk by monitoring and managing all other risks and ensuring we have mitigation plans for them.

Finance Lease

In September 2010, agreements which constitute a finance lease, for space in our corporate office building in downtown Victoria took effect following the completion of construction of the new building.

The initial term of the lease was 15 years, with four renewal options of five years each. We advanced \$24.5 million to the developer of the property for a term of 15 years, secured by a second mortgage on the property. The loan agreement provides for interest equal to one-half of the net cash flow from the property, subject to minimum and maximum percentage rates of interest. Over the term of the loan, interest is expected to approximate the market rate when the loan was made. Incidental to the loan, we were granted an option to purchase up to 50% of the owner's equity interest in the new building. The purchase option expires at the end of the loan term.

Other Long-Term Liabilities

Other long-term liabilities consist primarily of accrued post-retirement, post-employment benefits and incentive funding. We have received \$5.3 million of a total contribution of \$6.0 million from FortisBC Energy Inc. as part of the NGT incentive funding for the Salish Class vessels and expect to receive the remaining \$0.7 million in fiscal 2019. The contribution is dependent upon the purchase of at least 3 million gigajoules of LNG over a 10-year period and will be applied towards the purchase of these vessels. We have also received \$1.9 million of a total contribution of up to \$10.0 million from FortisBC Energy Inc. as part of the NGT incentive funding to help offset incremental capital costs associated with the conversion of the Spirit Class vessels to utilize LNG. The contribution is dependent upon the purchase of at least 10 million gigajoules of LNG over a 10-year period and will be applied towards the cost of converting the vessels. Based on our projected LNG consumption, we expect to meet the consumption requirements of these contribution agreements.

Sources & Uses of Cash

Our liquidity needs are met through a variety of sources, including cash generated from operations, issuance of bonds, and borrowings under our credit facility. Our primary uses of funds are operational expenses, capital asset acquisitions and upgrades, and payments on our long-term debt.

Sources and uses of cash and cash equivalents for fiscal 2018 and 2017 are summarized in the table below:

Years ended March 31 (\$ millions)	2018	2017	INCREASE (DECREASE)
Cash and cash equivalents, beginning of period	72.0	79.1	(7.1)
Cash from operating activities:			
Net earnings	59.9	77.4	(17.5)
Items not affecting cash	222.2	210.3	11.9
Changes in non-cash operating working capital	(6.1)	(1.1)	(5.0)
Net interest paid	(60.1)	(60.2)	0.1
Cash generated by operating activities	215.9	226.4	(10.5)
Cash generated by financing activities	1.0	54.7	(53.7)
Cash used in investing activities	(219.0)	(288.2)	69.2
Net decrease in cash and cash equivalents	(2.1)	(7.1)	5.0
Cash and cash equivalents, end of period	69.9	72.0	(2.1)

For fiscal 2018, cash generated by operating activities decreased \$10.5 million compared to the prior year, primarily due to a decrease in net earnings, reflecting the impact of higher operating expenses mainly due to additional trips provided, higher vessel maintenance and new vessels entering service, partially offset by higher revenues from increased traffic levels.

Cash generated by financing activities in fiscal 2018 was \$1.0 million. This amount consisted of our new \$45.3 million loan with KfW IPEX-Bank GmbH, mostly offset by: \$35.3 million in repayment of other KfW loans; \$1.6 million repayment of finance lease obligations; \$6.0 million in dividends paid on preferred shares; and \$1.4 million in deferred financing costs.

Cash generated by financing activities in fiscal 2017 was \$54.7 million. This amount consisted of our two new loans with KfW IPEX-Bank GmbH totalling \$90.1 million, partially offset by: \$24.9 million in repayment of other KfW loans; \$1.5 million repayment of finance lease obligations; \$6.0 million in dividends paid on preferred shares; and \$3.0 million in deferred financing costs.

Cash used in investing activities in fiscal 2018 decreased by \$69.2 million compared to the prior year, mainly due to a \$13.2 million decrease in cash used for capital expenditures; a \$55.4 million decrease in cash used for short-term investing; and a \$0.6 million change in debt service reserves. (See "Investing in Our Capital Assets" below for detail of significant capital expenditures.)

FOURTH QUARTER RESULTS

The following provides an overview of our financial performance and selected operational statistics comparing the three months ended March 31, 2018 to the same period in the prior year.

The fourth quarter reflects a seasonal reduction in traffic levels which we utilize to perform upgrades and major maintenance and refit programs as well as to undertake mandatory inspections on the majority of our vessels.

	2018	2017	INCREASE (DECREASE)
Operational Statistics			
Vehicle traffic	1,691,983	1,606,426	85,557
5.3% increase			
Passenger traffic	3,984,543	3,809,323	175,220
4.6% increase			
On-time performance	95.1%	93.7%	1.4%
Number of round trips	18,861.0	18,881.5	(20.5)
Capacity provided (AEQs)	3,423,665	3,681,797	(258,132)
AEQs carried	1,932,721	1,840,539	92,182
Capacity utilization	56.5%	50.0%	6.5%

Vehicle traffic increased 5.3% and passenger traffic increased 4.6% in the fourth quarter of fiscal 2018 compared to the same quarter in fiscal 2017.

We believe the increase was partially due to unfavourable weather in the fourth quarter of fiscal 2017. Also, traffic levels were positively impacted by half of the Easter holiday weekend falling in the fourth quarter of fiscal 2018, compared to no Easter holiday weekend in the fourth quarter of fiscal 2017.

Capacity utilization in the three months ended March 31, 2018 increased by 6.5% over the same period in the prior year, mainly as a result of an increase in the AEQs carried and in the higher capacity provided in the prior year during the construction at Langdale Terminal as discussed previously. If we adjusted the fourth quarter in the prior year, removing the additional available vehicle capacity, capacity utilization during the fourth quarter would have increased 2.6% due to higher AEQs carried.

Three months ended March 31 (\$ millions)	2018	2017	VARIANCE	
			\$	%
Total revenue	168.3	157.5	10.8	6.9%
Operating expenses	196.1	183.3	(12.8)	(7.0%)
Operating loss	(27.8)	(25.8)	(2.0)	(7.8%)
Net finance and other	13.2	15.0	1.8	12.0%
Net loss	(41.0)	(40.8)	(0.2)	(0.5%)

Our net loss in the quarter was \$0.2 million larger than in the same quarter of fiscal 2017. The net loss in the three months ended March 31, 2018 reflects an increase in net operating expenses and a reduction in reservation fee revenue of \$1.0 million to record GST payable on reservation fee revenue partially offset by higher traffic levels and increase in finance income. The net loss in the three months ended March 31, 2017 reflects lower traffic levels, higher fuel rebates, lower social program fees, an increase in net operating expenses and finance expenses and a reduction in reservation fee revenue of \$3.1 million to record GST payable on reservation fee revenue for fiscal years 2014 through 2017, based on CRA audit findings.

Revenue

Our total revenues for the fourth quarter of fiscal 2018 increased by \$10.8 million or 6.9% compared to the same quarter in the prior year, as shown in the following table:

Three months ended March 31 (\$ millions)	2018	2017	INCREASE (DECREASE)	
			\$	%
Direct Route Revenue				
Vehicle tariff	74.1	68.3	5.8	8.5%
Passenger tariff	41.5	38.0	3.5	9.2%
Fuel rebates	(3.6)	(3.4)	(0.2)	5.9%
Net catering & on-board	9.6	8.8	0.8	9.1%
Social program fees	4.1	3.9	0.2	5.1%
Other revenue	2.2	2.1	0.1	4.8%
Total Direct Route Revenue	127.9	117.7	10.2	8.7%
Indirect Route Revenue				
Ferry transportation fees	32.5	32.0	0.5	1.6%
Federal-Provincial subsidy	7.5	7.3	0.2	2.7%
Total Route Revenue	167.9	157.0	10.9	6.9%
Other general revenue	0.4	0.5	(0.1)	(20.0%)
Total Revenue	168.3	157.5	10.8	6.9%

Average tariff revenue per vehicle (excluding the GST assessed on reservation fee revenue) decreased \$0.54 or 1.2% in the quarter compared to the same period in the prior year mainly as a result of changes in the proportion of traffic on routes with higher versus lower tariffs. Average tariff revenue per passenger increased \$0.45 or 4.5% in the quarter compared to the same period in the prior year reflecting the impact of passenger fare promotions offered in the prior year. The increase in traffic levels and the change in average tariffs resulted in a \$6.2 million increase in tariff revenue (excluding the GST assessed on reservation fee revenue).

During fiscal 2017 and fiscal 2018, we had a fuel rebate of 2.9% in place on our Major and regulated Other Routes and a fuel rebate of 1.9% in place on our Northern Routes.

Revenue from net catering and on-board services increased in the quarter compared to the same period in the prior year as a result of both higher passenger traffic and higher average sales per passenger.

Social program fees increased in the quarter compared to the same period in the prior year mainly as a result of higher MTAP usage.

Expenses

Our operating and net finance and other expenses for the fourth quarter of fiscal 2018 and fiscal 2017 are shown in the following tables:

Three months ended March 31 (\$ millions)	2018	2017	INCREASE (DECREASE)	
			\$	%
Operating expenses				
Operations	120.3	113.2	7.1	6.3%
Maintenance	24.9	21.0	3.9	18.6%
Administration	10.1	10.4	(0.3)	(2.9%)
Total operations, maintenance & administration	155.3	144.6	10.7	7.4%
Depreciation and amortization	40.8	38.7	2.1	5.4%
Total operating expenses	196.1	183.3	12.8	7.0%

The increase in operations costs of \$7.1 million for the quarter ended March 31, 2018 compared to the same period in the prior year is due to:

- \$4.0 million increase in wages and benefits mainly due to wage rate increases in accordance with the Collective Agreement and higher benefit premium rates;
- \$1.0 million increase in parts and supplies and contracted services;
- \$0.9 million increase in fuel costs (\$1.0 million in higher fuel prices offset by \$0.1 million in lower fuel usage). (For purposes of rate regulation, \$1.1 million of fuel expenses in the quarter were recorded in deferred fuel cost accounts.); and
- \$1.2 million increase in other expenses including computer licences, credit card fees and promotional costs.

The increase in maintenance costs of \$3.9 million reflects the cyclical nature of vessel refits.

Administration costs were at a similar level as the same period in the prior year.

The increase in depreciation and amortization of \$2.1 million reflected the new capital assets that have entered service.

Three months ended March 31 (\$ millions)	2018	2017	(INCREASE) DECREASE	
			\$	%
Net finance and other expenses				
Finance expense	14.8	14.8	–	–
Less: finance income	(1.6)	(1.2)	0.4	(33.3%)
Net finance expense	13.2	13.6	0.4	2.9%
Loss on disposal and revaluation of property, plant and equipment, and intangible assets	–	1.4	1.4	–
Total net finance and other expenses	13.2	15.0	1.8	12.0%

Net finance expense in the quarter was \$0.4 million lower compared to the same period in the prior year, primarily due to a \$0.4 million increase in finance income as a result of interest received on a higher level of investments.

There was no loss on disposal and revaluation of property, plant and equipment and intangible assets in the quarter while the same period in the prior year had asset impairment of \$1.4 million.

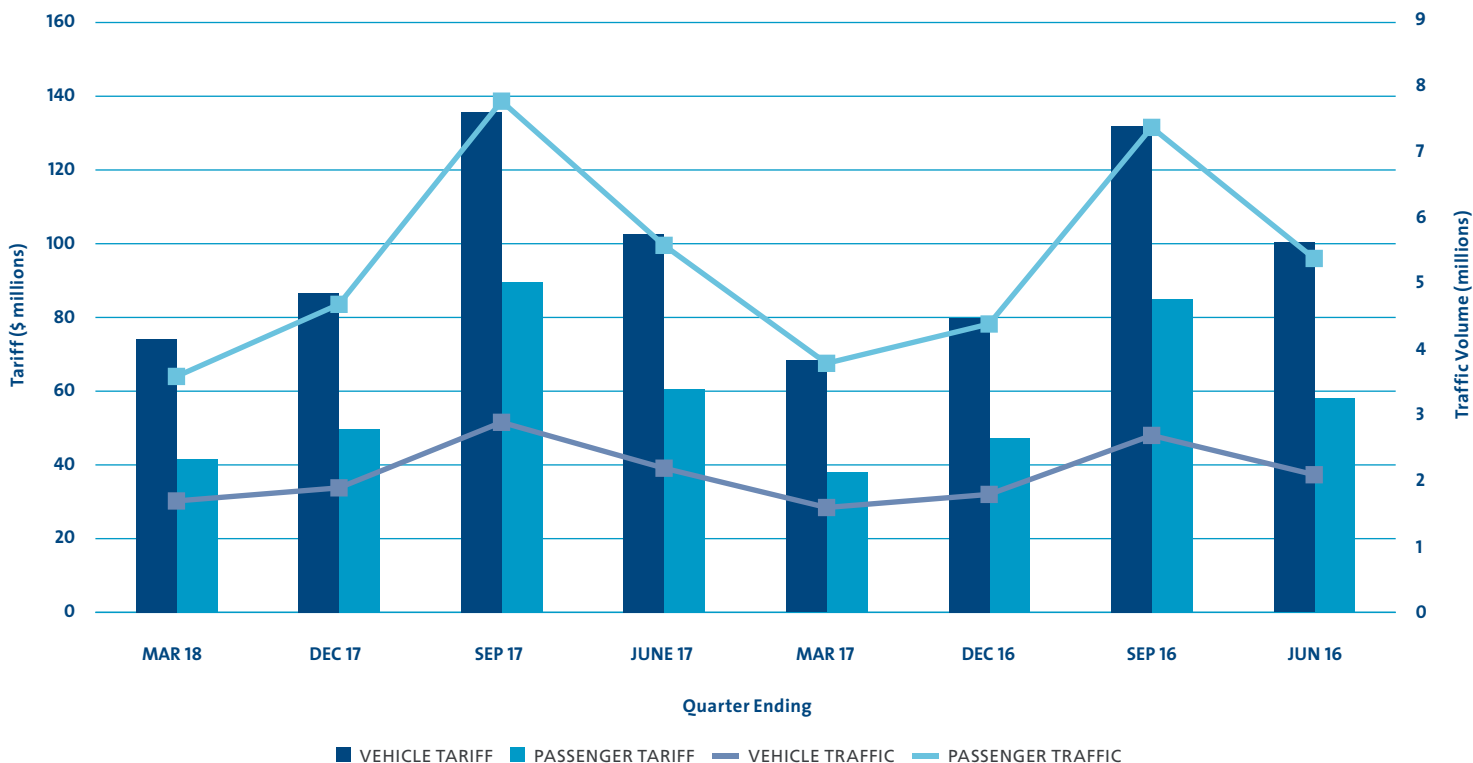
SUMMARY OF QUARTERLY RESULTS

The table below compares earnings by quarter for the most recent eight quarters:

Quarter Ended (unaudited) (\$ millions)	MAR 18	DEC 17	SEP 17	JUN 17	MAR 17	DEC 16	SEP 16	JUN 16
Total revenue	168.3	195.3	309.5	225.9	157.5	183.7	298.9	219.2
Operating (loss) profit	(27.8)	–	112.6	31.5	(25.8)	9.8	108.5	40.6
Net (loss) earnings	(41.0)	(14.8)	98.4	17.3	(40.8)	(4.0)	95.2	27.0

Quarterly results are affected by the seasonality of leisure travel patterns. The second quarter, covering the summer period, experiences the highest traffic levels and the highest net earnings. The third and fourth quarters reflect a seasonal reduction in traffic. We utilize these periods to perform upgrades and major maintenance and refit programs, as well as to undertake mandatory inspections on the majority of our vessels.

The following graph demonstrates the seasonality of our revenue and shows the relationship of traffic volume and tariff revenue over the most recent eight quarters:



INVESTING IN OUR CAPITAL ASSETS

We have established a formal project governance framework and guidelines to ensure that capital investments meet our functional and business needs. This framework is the structure under which capital projects are identified, managed, monitored and delivered as effectively and efficiently as possible. It ensures we take a disciplined approach to capital investment by outlining the key principles, techniques and tools for managing and monitoring capital projects through the various stages of the project lifecycle.

Our capital asset planning is supported with formal business cases for all capital projects, project management principles, and clear assignment of accountabilities to project managers, project owners and project sponsors. We require regular project reporting to monitor scope, schedule, budget and project risks at an individual project level and report against the capital expenditure budget. This regular reporting is used to prepare a summary report which is presented to a capital planning and budget committee on a monthly basis and to the Board of Directors on a quarterly basis.

Capital Expenditures

Our 12-year capital plan, covering fiscal 2015 through 2026, consists of over \$3 billion which includes replacing 14 aged vessels which will be, on average, over the age of 50 years at the time of their replacement. The plan also includes mid-life upgrades for the Spirit Class vessels along with upgrades and modifications for other vessels, significant improvements at our terminals, and renewal of our information technology infrastructure.

We have one of the largest ferry fleets in the world. The typical life span of vessels is approximately 45 years. We are currently operating 35 vessels with an average age of 31 years and, of these, 11 are 45 years old or older.

As vessels approach their planned retirement dates, we are reviewing the condition of these vessels to determine potential candidates for life extension rather than replacement. Our strategy for these new vessels includes design optimization, interoperability, and standardization of vessels across the fleet, to the extent possible, to provide more flexibility to respond to changes in the market demand and traffic forecasts. Operational experience will be incorporated into the design of the vessels to ensure high levels of safety, environmental leadership, reliability and to enhance the customer experience. We plan to adopt alternative fuel sources, such as LNG and batteries, where economically and technically feasible.

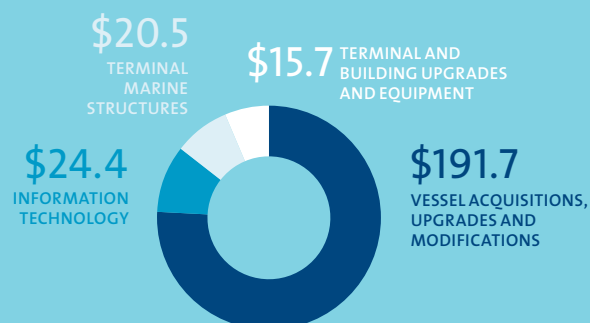
Both LNG and the marine diesel we currently use meet all domestic and international emissions regulations. We believe a move to LNG would reduce costs and emissions. LNG is forecast to remain less expensive than the ultra-low sulphur diesel we currently use and has significantly less emissions. We believe LNG is a viable option for some of our future new vessels and, as noted below, our three new Salish Class vessels have the capability to run on LNG. We also analyze LNG as an option for existing vessels undergoing major retrofits (such as our Spirit Class vessels as discussed below) and intend to pursue the option where it is feasible.

In total, we have been approved for up to \$60.5 million in funding under the New Building Canada Fund. In fiscal 2018, we recorded \$14.9 million in funding; comprising \$3.1 million for the New Minor Class vessel project and \$11.8 million for the *Northern Sea Wolf* project.

Total capital expenditures during fiscal 2016 through fiscal 2018 are shown in the table below:

Capital expenditures by fiscal year (\$ millions)	2018	2017	2016
Vessel upgrades & modifications	110.1	71.2	85.8
Terminal marine structures	20.5	22.9	24.3
Information technology	24.4	30.9	31.9
Terminal building upgrades & equipment	15.7	12.8	10.8
Total (without new vessels)	170.7	137.8	152.8
New vessels	81.6	105.9	28.4
Total (including new vessels)	252.3	243.7	181.2

Capital expenditures in the 12 months ended March 31, 2018 totalled \$252.3 million:



Capital expenditures, net of external funding recorded, in the 3 and 12 months ended March 31, 2018 comprised the following:

March 31, 2018 (\$ millions)	3 MONTHS	12 MONTHS
Spirit Class mid-life upgrades	18.2	67.3
New Salish Class vessels	0.2	54.7
Major overhauls and inspections	16.2	39.4
<i>Northern Sea Wolf</i> and terminal modifications	10.6	25.6
Customer experience program	3.1	12.0
Hardware upgrades	3.2	8.5
Trestle and dolphin upgrades at Prince Rupert terminal	1.0	10.0
New Minor Class vessels	0.3	7.3
Departure Bay – holding compound remediation	2.1	3.7
Various other projects	6.1	23.8
	61.0	252.3

Spirit Class Mid-Life Upgrades

In March 2016, we awarded contracts totalling \$140 million to Remontowa Ship Repair Yard S.A. to conduct the mid-life upgrades, including major upgrades to customer amenities, and conversion to dual-fuel, of our two largest vessels, the *Spirit of Vancouver Island* and the *Spirit of British Columbia*. On May 5, 2018, the *Spirit of British Columbia* arrived in Canada from Gdansk, Poland, after undergoing its mid-life upgrade. The *Spirit of British Columbia* returned to service on June 6, 2018 and the *Spirit of Vancouver Island* is expected to depart for Poland for its mid-life upgrade, after the 2018 summer season. The mid-life upgrades will enable the vessels to be in service for another 25 years. We expect the conversion of these vessels to result in substantial savings, as LNG costs are considerably less than marine diesel. We also expect the conversion to result in significant environmental benefits, such as reducing carbon dioxide emissions from our vessels. FortisBC has committed to provide us with up to \$10 million in incentive funding to help offset incremental capital costs associated with the conversion of the Spirit Class vessels to utilize LNG.

New Salish Class Vessels

In July 2014, we entered into contracts with Remontowa Shipbuilding S.A. of Gdansk, Poland to build three new Salish Class vessels. The contracts, with a total value of \$165 million, formed the majority of the total project budget of \$206 million. This project is now complete. The new vessels are dual-fuel capable, designed to run primarily on LNG with marine diesel fuel as a backup. These vessels set a new standard of efficiency with standardized bridges, engine rooms and life-saving equipment, moving us to a higher safety standard and improving interoperability. On May 16, 2017, the *Salish Orca* replaced the 52-year old *Queen of Burnaby* and commenced regularly-scheduled service between Comox and Powell River. On June 21, 2017 and August 3, 2017, the *Salish Eagle* and the *Salish Raven*, respectively, commenced regularly-scheduled service in the Southern Gulf Islands. Introduction of these vessels enabled the retirement of the 53-year old *Queen of Nanaimo*. FortisBC has committed to provide us with up to \$6 million in incentive funding to help offset incremental capital costs associated with the Salish Class vessels.

Major Overhauls and Inspections

Capital expenditures in respect of major overhauls and inspections of components of hull, propulsion and generators for 13 vessels were completed in fiscal 2018 or underway at March 31, 2018.

Northern Sea Wolf

On April 7, 2017, we finalized an agreement to acquire a 75-metre used vessel to provide a new seasonal direct ferry service between Port Hardy and Bella Coola. On April 5, 2017, in response to our application, the Commissioner confirmed his determination that the capital expenditure for the acquisition and modification of a used vessel to provide mid-coast service, including a new seasonal direct ferry service between Port Hardy and Bella Coola, as well as the necessary terminal modifications, is reasonably required. Also on April 5, 2017, the Province contributed an initial \$15 million towards the provision of this service for the period ending March 31, 2020. On March 21, 2017, the Government of Canada approved funding of up to \$15.1 million from the New Building Canada Fund of which we recorded \$11.8 million in fiscal 2018. On December 15, 2017, the *Northern Sea Wolf* arrived in British Columbia after a 10,097 nautical mile journey from Athens, Greece. The vessel is undergoing extensive upgrades at Esquimalt Drydock Company, a local shipyard, in preparation for regular service commencing in the summer of 2018. Capital expenditures consisted primarily of payments to acquire the vessel, to upgrade the vessel and modify our terminal marine structures.

Customer Experience Program

Our customer experience program, which includes the Fare Flexibility and Digital Experience Initiative, will replace our aged website, reservation system and e-commerce platform and upgrade our point-of-sale. This program will give customers an opportunity to purchase travel in advance at discounted rates on select sailings on reservable routes and allow us to respond in a more timely fashion to changing customer demands. Our customer experience program will introduce improved transaction processing and online booking with more choices in fares. During fiscal 2018, we implemented our new reservations system as well as enhancements to our customer relationship management system.

Hardware Upgrades

Hardware upgrades include the replacement of aged computers, servers, printers, routers, closed-circuit cameras, antennas, digital signage and handheld units for inventory management.

Prince Rupert Terminal

The existing marine structures were replaced with a new trestle and three new dolphins at the Prince Rupert terminal. This project completed and went into service in January 2018.

Minor Class Vessel Replacements

On April 13, 2017, we entered into design and build contracts with Damen Shipyard Group of Netherlands, totalling \$60 million for the construction of two minor class vessels. The Government of Canada has approved funding of up to \$28.3 million under the New Building Canada Fund toward these vessels. The first steel cut for the first and second vessels took place on April 2, 2018 and on April 11, 2018, respectively. These vessels will each have a capacity of up to 300 passengers and approximately 47 vehicles. When these new vessels are placed into service in early 2020, it will allow us to retire the 60-year old *North Island Princess* and the 54-year old *Howe Sound Queen*. We intend to deploy the first new vessel to provide service between Powell River and Texada Island and the second new vessel to provide service between Port McNeill, Alert Bay and Sointula. In fiscal 2018, expenditures were \$10.4 million primarily consisting of installment payments made based on the contract, less \$3.1 million in funding from the New Building Canada Fund.

Departure Bay

At Departure Bay, a project to reinstate the structural integrity of the terminal holding compound and the underground utilities is underway and expected to complete during the first quarter of fiscal 2019.

OUTLOOK

Financial

We expect positive net earnings in fiscal 2019, reflecting increases in discretionary traffic due to favourable economic conditions including the low Canadian dollar and tourism, and partially offset by fare reductions.

On April 1, 2018, we applied a 15% fare reduction on the Northern Routes, the regulated Other Routes and on one Major route (Horseshoe Bay – Langdale). Fares remained unchanged on the three Major Routes connecting Metro Vancouver with mid and southern Vancouver Island. Also on April 1, 2018, the BC seniors' passenger discount increased from 50% to 100% for travel Monday to Thursday on the Major and Other Routes. The total value of these initiatives over two years is \$98 million. We reached an agreement with the Province whereby we will contribute \$39 million in foregone revenue and the Province will contribute \$59 million in ferry transportation fees towards the fare reductions and the increase to the BC seniors' discount.

We expect an increase in total revenue in fiscal 2019, reflecting higher traffic levels, net catering and retail revenues and ferry transportation fees, partially offset by fare reductions.

We are considering future pricing promotions. These promotions give us the opportunity to test variable pricing and will provide information on traffic trends, customer responses and impacts to operations for the Fare Flexibility and Digital Experience Initiative. This initiative will change the way we price fares. It will give customers an opportunity to purchase travel in advance at discounted rates, on select less-popular sailings on reservable routes. We expect it will help shift traffic to sailings that typically run with lower capacity utilization.

We expect a modest increase in total expenses in fiscal 2019, reflecting higher wage and benefit costs resulting from the implementation of the Collective Agreement, introduction of a new route and other route changes, partially offset by lower vessel maintenance costs and savings from operating the *Spirit of British Columbia* and the Salish Class vessels on LNG. We continue to manage our costs prudently without compromising safe operations.

Major Investments

The lack of resiliency in our fleet may impact our ability to continue to provide reliable service, particularly on the Major Routes where we do not have a spare vessel. With the exception of one minor route vessel, at any point in time, all vessels are either in-service or undergoing refit. As traffic increases, our busy season is extending further into the spring and fall. This reduces the time that a vessel can be removed from service for its required maintenance. If the increase in traffic continues and there is no replacement vessel available, it will become more difficult to ensure that vessels receive their required maintenance. Also, if an unplanned event makes it necessary to remove a vessel from service for a period of time, our ability to continue to meet traffic demand would be constrained. This would negatively impact our customers and the communities we serve. The disruption to service as a result of a lack of resilience in our system is more critical than ever because of the continuing increase in traffic that we have been experiencing. We are addressing this issue in our 12-year capital plan. Our capital plan, covering fiscal 2015 through 2026, consists of over \$3 billion which includes replacing 14 aged vessels, executing mid-life upgrades for the Spirit Class vessels as well as undertaking upgrades and modifications for other vessels, making significant improvements at our terminals, and renewing our information technology infrastructure.

Minor Class Vessel Replacements

On April 13, 2017, we executed a \$60 million design and build contract with Damen Shipyard Group of Netherlands, for the construction of two minor class vessels. These vessels will each have a capacity of up to 300 passengers and approximately 47 vehicles. When these new vessels are placed into service in 2020, it will allow us to retire the 60-year old *North Island Princess* and the 54-year old *Howe Sound Queen*, subject to satisfying regulatory requirements.

Bowen Class Vessel Replacements

Planning is underway to replace the *Bowen Queen*, the *Mayne Queen* and the *Powell River Queen*, all of which were built in 1965 and carry approximately 60 vehicles. The new vessels will be built based on our standardization and interoperability principles that will enable further advances in operational efficiencies.

Major Vessel Replacements

Planning is underway to design and build new major vessels which will allow us to retire the 54-year old *Queen of New Westminster*, three 42-year old C-Class vessels, the *Queen of Alberni*, the *Queen of Cowichan*, and the *Queen of Coquitlam*.

Terminals

At our Richmond maintenance facility, planning is underway to upgrade and redevelop the facilities to replace aging infrastructure and increase operating efficiency. The multi-year project to seismically upgrade the site, modernize infrastructure and build a centralized shop and life raft servicing centre is in its design stage.

The Langdale terminal development plan involves upgrades designed for the safety and convenience of our customers. In fiscal 2017, the Government of Canada approved funding to a maximum of \$17.1 million under the New Building Canada Fund towards this major upgrade.

Over the next 10 years, an estimated capital investment of \$0.5 billion is expected to be required at the terminals serving the Major Routes, including Horseshoe Bay, Swartz Bay, and Tsawwassen terminals. Careful consideration, extensive detailed design and consultation with stakeholders, regulatory and board approval will be completed before these projects proceed.

We face particular on-time challenges on the routes using Horseshoe Bay terminal. Our initiatives to improve on-time performance have included adjusting and/or expanding sailing schedules, adjusting crewing schedules and refining vehicle loading processes during peak periods. These initiatives have helped somewhat to improve on-time performance, however, significant reconfiguration of the terminal layout will be necessary to optimize functionality to improve loading and unloading times and improve on-time performance to an acceptable level.

Service Enhancements

On March 8, 2017, we executed an amendment to the CFSC that includes a new seasonal direct ferry service between Port Hardy and Bella Coola beginning in the summer of 2018. On December 15, 2017, the *Northern Sea Wolf* arrived in British Columbia after a 10,097 nautical mile journey from Athens, Greece. The *Northern Sea Wolf* is undergoing extensive upgrades at Esquimalt Drydock Company, a local shipyard, in preparation for regular service commencing in the summer of 2018. This vessel already fits in our major northern berths while several smaller terminals required modification to accommodate the new vessel.

Our customer experience program, which includes the Fare Flexibility and Digital Experience Initiative, will replace our aged website, reservation system and e-commerce platform and upgrade our point-of-sale. This program will allow us to respond in a more timely fashion to changing business needs and to better support marketing, travel services and flexible pricing initiatives. In the last quarter of fiscal 2018, we implemented our new reservations system as well as enhancements to our customer relationship management system. Our customer service program will introduce improved transaction processing and online booking with more choices in fares.

We believe our information technology systems must be significantly improved to evolve our business model. The rigid technology systems we currently use limit our ability to design attractive and relevant pricing. The Fare Flexibility and Digital Experience Initiative will provide customers with enhanced fare choices and a more intuitive online and mobile booking experience. In addition, new demand forecasting and inventory management capabilities will allow us to better match customer demand with capacity which will help limit sailing waits and improve capacity utilization.

Summary

We continue to explore strategies to create an affordable and sustainable ferry system beyond fiscal 2018 by optimizing our service on routes, standardizing our vessels, optimizing our fuel consumption, and reducing our environmental impact. We also continue to look for ways to improve the customer experience, diversify our revenue sources, increase operational efficiencies, and leverage opportunities for federal infrastructure funding and provincial incentive funding to renew our fleet and terminals.

Ferry traffic levels are affected by a number of factors, such as the economic conditions, transportation costs (including vehicle gasoline prices and ferry fares), the value of the Canadian dollar, tourism levels, disposable personal income, demographics, and population growth. Traffic levels are also impacted by short-term factors such as weather conditions and local events.

We remain confident that as long as the Canadian dollar stays low relative to the U.S. dollar and oil prices do not increase significantly, the fundamentals impacting our traffic will remain favourable, and we should continue to see traffic growth in the near-term.

FINANCIAL RISKS AND FINANCIAL INSTRUMENTS

Exposure to credit risk, liquidity risk and market risk arises in the normal course of our business. Our exposure to credit risk is limited to the carrying value on our statements of financial position for cash, short-term investments, derivative assets and trade and other receivables. While there is a risk that a third party may fail to meet its obligations under the terms of a financial instrument, we do not believe that it is a significant risk. We manage credit exposure related to financial instruments by dealing with high credit quality institutions, in accordance with established policy and parameters and by an ongoing review of our exposure to counterparties.

We manage liquidity risk through daily monitoring of cash balances, the use of long-term forecasting models and the maintenance of a credit facility and debt service reserves. (See "Liquidity and Capital Resources" for more detail.)

We manage market risk arising from the volatility in foreign currency, interest rate, and fuel price exposures in part through the use of derivative financial instruments including forward contracts, swaps and options. We do not utilize derivative financial instruments for trading or speculative purposes.

Fuel Price

Our exposure to fuel price risk is associated with the changes in the Canadian market price of marine diesel fuel and natural gas. Fuel costs have fluctuated significantly over the past few years, and there is uncertainty of the cost of fuel in the future.

High levels of fuel pricing could translate into significant fuel surcharges and result in unprecedented total tariff levels. Although there is uncertainty of the extent of the impact of fuel surcharges on future ferry traffic levels, there is a risk of a decline in ferry traffic levels as a result of increasing customer costs resulting from the implementation of fuel surcharges.

Risk mitigation: To mitigate the effect of volatility in fuel prices on our earnings, we use deferred fuel cost accounts together with fuel surcharges or rebates as required. (See "The Effect of Rate Regulation" for more detail.) We may enter into hedging instruments, in accordance with our Financial Risk Management Policy, in order to reduce fuel price volatility and add a fixed component to the inherent floating nature of fuel prices. Fuel price hedging instruments are used solely for the purpose of reducing fuel price risk, not for generating trading profits. Fuel forward contracts are only entered into when there is a reasonable likelihood that the hedge will result in a net procurement cost per litre less than or equal to the set price per litre established by the Commissioner. At March 31, 2018, we had \$54.6 million (notional value) in fuel forward contracts for marine diesel related to 2019 and 2020. At March 31, 2018, we had no fuel forward contracts for LNG. Realized gains and losses resulting from fuel forward contracts are recognized as a component of fuel costs.

Derivatives

We hedge our exposure to fluctuations in fuel prices, foreign currency exchange rates and interest rates from time to time through the use of derivative instruments. At March 31, 2018, we held six foreign exchange forward contracts with a carrying and fair value receivable of \$58 thousand and with a notional value of \$1.7 million, while at March 31, 2017 we held one such contract with a carrying and fair value liability of \$5 thousand and with a notional value of \$0.9 million. There were no interest rate forward contracts in place at March 31, 2018 or at March 31, 2017.

At March 31, 2018, we held fuel forward contracts for marine diesel with a carrying and fair value asset of \$12.5 million and with a notional value of \$54.6 million. At March 31, 2017, we held fuel forward contracts for marine diesel with a carrying and fair value asset of \$1.6 million and with a notional value of \$42.7 million and liability of \$1.0 million and with a notional value of \$24.0 million. At March 31, 2018, with the application of hedge accounting, the unrealized gain of \$13.6 million was recognized in other comprehensive income. At March 31, 2017, with the application of hedge accounting, the unrealized gain of \$12.1 million was recognized in other comprehensive income. The fair value of commodity derivatives would reflect only the value of the commodity derivatives and not the offsetting change in value of the underlying future purchase of fuel.

The fair values would reflect the estimated amounts we would receive or pay should the derivative contracts be terminated at the stated dates. For regulatory purposes, any realized gains or losses related to fuel commodity swaps would be charged to our deferred fuel cost accounts. (See "The Effect of Rate Regulation" for more detail.)

Non-Derivative Financial Instruments

The carrying and fair values of non-derivative financial instruments at March 31, 2018, and 2017 are as follows:

(\$ millions)	2018		2017	
	CARRYING VALUE	FAIR VALUE	CARRYING VALUE	FAIR VALUE
Financial Assets				
Cash and cash equivalents	69.9	69.9	72.0	72.0
Restricted short-term investments	32.3	32.3	32.4	32.4
Other short-term investments	114.3	114.3	115.6	115.6
Trade and other receivables	26.3	26.3	15.3	15.3
Long-term loan receivable	24.5	24.5	24.5	24.5
	267.3	267.3	259.8	259.8
Financial Liabilities				
Accounts payable and accrued liabilities	77.2	77.2	55.2	55.2
Interest payable on long-term debt	18.5	18.5	18.5	18.5
Long-term liability	7.8	7.8	5.3	5.3
Long-term debt, including current portion	1,314.4	1,614.1	1,304.8	1,597.8
	1,417.9	1,717.6	1,383.8	1,676.8

The fair value of all financial instruments included above, with the exception of long-term debt, approximate their carrying amounts due to the nature of the item and/or the short time to maturity.

The carrying value of long-term debt is measured at amortized cost using the effective interest rate method. The fair value of long-term debt, the value if incurred at March 31 of each year, is calculated by discounting the future cash flow of each debt issue at the estimated yield to maturity for the same or similar issues, or by using available quoted market prices.

BUSINESS RISK MANAGEMENT

We continue to employ a variety of commonly-accepted methodologies to identify, assess and mitigate risks. We have processes in place to manage risks that inevitably arise in the normal course of business. We have an integrated approach to managing risk, involving our Board of Directors and our employees.

Our Board of Directors is responsible for ensuring we have the appropriate policies, procedures and systems in place to identify and manage the principal risks of our business. Management keeps the Board and its Committees apprised of changing risks and the processes and systems used to mitigate them. The individual Committees of the Board regularly consider and review internal processes for managing those risks that are specific to the areas of our business for which they have oversight responsibility, and obtain assurance from management and internal audit, as appropriate, regarding the adequacy of the associated risk management processes.

Individual business units are responsible for considering risk exposures at all levels within their unit and for considering the possible impact such risks may have on other areas. To ensure we focus on safety as our first priority, all operational meetings are expected to start with safety as the first item on the agenda.

A culture that promotes the management of risk as part of each employee's daily activities is integral to our program. One way we promote this culture is through our SailSafe program. Employees are provided with a risk-based ALERT tool that can facilitate change in the specific task or process or within other areas of the Company if the risk is applicable to other aspects of operations. We have an online operational risk register to promote awareness of risk issues and facilitate continuous and consistent risk management.

There will always be inherent risk resulting from our business operations and we endeavor to minimize the risk to as low as reasonably practicable. As part of our risk management strategies, we have considered many items such as profitability levels, cash generating potential, cash utilization requirements including debt repayment schedules and future capital expenditures, and working capital requirements. We have taken measures to allow us to adapt to changes in the economic environment and ensure a viable, profitable future. We do not believe that material uncertainties exist in regards to our future as we believe our risk mitigation strategies are sufficient.

Customer Demand

Our vehicle and passenger traffic levels in fiscal 2018, as compared to the prior year, increased 5.0% and 4.7%, respectively. In fiscal 2018, we believe traffic continued to be positively impacted by favourable economic activity in British Columbia and the lower Canadian dollar.

Many factors affect customer demand, including current economic conditions, the value of the Canadian dollar, levels of tourism, emerging transportation choices, consumer sentiment, threats to health and safety from outbreak of disease or security risks, demographics and population growth. The cost of transportation, including the price of fuel at the pump and ferry fares (including the implementation and removal of fuel surcharges or rebates), disposable personal income and weather conditions may have an effect on discretionary travel and levels of tourism.

We are uncertain as to the individual or cumulative impact these items may have on our revenue. No assurance can be given as to the level of traffic on our system and the resulting tariff revenues.

Risk mitigation: We are constrained by the CFSC, which stipulates, among other things, the minimum number of round trips that must be provided for each regulated ferry route. Recognizing our ability to reduce capacity is constrained by the CFSC, we continually monitor traffic demand and leading indicators to meet requirements in an efficient and effective manner. We respond to increases in traffic demand by adding extra sailings and capacity where possible. We also offer a variety of pricing promotions targeted to shifting some discretionary traffic to less popular sailings.

Vessel planning strategies are in place with the goal of standardization so we can better respond to changes in customer demand. We also regularly review and update our short and long-term financial and operating plans to ensure appropriate alignment of expenses with revenue.

Major Capital Projects

We have several major capital projects underway, including preparations for the mid-life upgrade of the *Spirit of Vancouver Island*, the building of two new Minor Class vessels, modification of the *Northern Sea Wolf* and the necessary terminal modifications, the Fare Flexibility and Digital Experience Initiative and the Automated Customer Experience Program. Risks associated with the cost, schedule and the technical scope of major projects, as well as the implementation and sustainment of them, could cause critical systems or assets to be unavailable for use.

Risk mitigation: A project governance framework is in place to guide all corporate projects. We ensure each project has executive sponsorship, a project owner and a project analyst. As well, each major project has a steering committee and associated governance to ensure business alignment with desired outcomes.

We require regular project reporting to monitor scope, schedule, budget and project risks at an individual project level and report against the capital expenditure budget. This regular reporting is used to prepare a summary report which is presented to a capital planning and budget committee on a monthly basis and to the Board of Directors on a quarterly basis.

Economic Regulatory Environment

We cannot predict what changes the Province may make to the Act or to other legislation, nor can we predict how the Commissioner's interpretation and administration of the Act may change over time. Such changes may impact our profitability.

Effective March 1, 2018, a new Commissioner was appointed for a term ending March 1, 2024. Commissioner Order 15-03 established final price cap increases of 1.9% for each of the four years of PT4, being the four-year period ending on March 31, 2020. There remains uncertainty in the Commissioner's future price cap rulings.

Risk mitigation: We strive to maintain regular and open communications and positive relationships with the Province, the Commissioner and local Ferry Advisory Committees that represent the interests of the communities we serve. We have the opportunity to apply to the Commissioner under section 42 of the Act for an extraordinary price cap increase or other relief if the introduction of new safety or other regulations impose a new, unexpected and significant cost burden.

Human Resources

Our ability to attract, train and retain employees with the requisite skill and capabilities to operate in the marine industry is key to our success. Shortages of critical skills are emerging in some areas in which we operate.

Risk mitigation: We provide internal training and development opportunities and support external training for advancement. We have invested in the SailSafe Simulator at Camosun College's trades facilities to guarantee access to the best training tools. We have a cadet program which includes participants from the British Columbia Institute of Technology, Georgian College of Ontario, and the Memorial University of Newfoundland. We have increased our level of social media collaboration and developed on-board career fairs to both inform the public of career possibilities and to connect with potential employees. We were named one of B.C.'s Top Employers (2017) and (2018). This award recognizes workplaces for offering progressive and forward-thinking programs for employees and aids in attracting employees to our Company.

Vessel Repair Facilities

We have a vessel repair facility in Richmond where we perform maintenance and refit work on our vessels; however, our facility does not have a dry-dock. There are only two shipyards with dry-docks in British Columbia that can accommodate large vessels. One of these shipyards dominates the vessel repair market, especially for large vessels.

The overall demand for ship repair and ship building facilities has been increasing with the national ship procurement strategy. As a result, ship repair labour and dry-docking availability may become over-subscribed in the coming years.

The inability to acquire timely and cost-effective ship repair services has the potential to cause operational disruption which, in turn, has the potential to have an adverse effect on results of operations, cash flow and financial results.

Risk mitigation: We plan our vessel maintenance to minimize the number of out-of-service periods and to maximize the maintenance performed by our own staff. We have also established long-range maintenance plans for all vessels, which enable us to plan and reserve space with ship repair facilities well in advance. Further, when regulations permit, in-water surveys are performed on vessels, potentially eliminating the requirement for dry-docking. In fiscal 2018, we entered into a five-year supply agreement with Point Hope Maritime Ltd. of Victoria, BC for the maintenance of eight of our minor vessels. We are in the process of doing a detailed design to redevelop our maintenance facility to provide a more efficient operation and to maintain our internal ship repair capability. Alternatives to using local facilities are also explored.

Security of Information

Deliberate or inadvertent release of confidential or sensitive information, whether in paper or electronic format, could have an adverse effect on the lives of our employees and customers, as well as negatively impact our reputation. A significant loss of confidential management information could also negatively impact our financial position and results of operations.

Risk mitigation: Governance is in place for ensuring information privacy. Our information security policy has been developed and implemented. Standard procedures for access and use of private data have been implemented. Multiple levels of technology controls are in place and networks, websites and databases are monitored by dedicated information technology security staff to detect potential issues. Information technology projects are delivered using the 'security by design' principle. Security scans by trusted and qualified vendors are conducted on a regular basis.

Communication to employees of their responsibility to protect private information is ongoing and a formal awareness and training program is in place.

First Nations

First Nations issues normally arise in British Columbia when a company seeks governmental approvals for its activities. Canadian courts have said that governments must consult with First Nations before granting any approval that could potentially affect Aboriginal interests, even when the extent and nature of those interests has not been formally proved in court or recognized in a treaty. Governments can involve a company in the consultation process with First Nations, which must be appropriate to the strength of the Aboriginal right and the potential severity of the impact on that right. Potential Aboriginal rights are especially significant in British Columbia because most of the Province is subject to far-reaching claims of Aboriginal rights and title, including in coastal areas where we operate. These claims could have importance if we seek new property rights or approvals from government.

Risk mitigation: Under the master agreement (see "Liquidity and Capital Resources – Terminal Leases" for more detail), the Province retains its liability, to the extent any exists, for the acts and omissions of the Province that occurred prior to our possession of the ferry terminal properties leased under the Terminal Leases and will reimburse us for any damages we suffer as a result. The Province will reimburse us for damages suffered if there is a final court decision or a treaty settlement that recognizes or confers upon an Aboriginal group a proprietary or other interest in the ferry terminal properties should that right or interest interfere with our quiet enjoyment of the ferry terminal properties as set out in the Terminal Leases.

ACCOUNTING PRACTICES

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and financial performance is based upon our consolidated financial statements, which have been prepared in accordance with IFRS.

Our significant accounting policies are contained in note 1 to our consolidated financial statements. Certain of these policies involve critical accounting estimates because they require us to make particularly subjective or complex judgements about matters that are inherently uncertain and because of the likelihood that materially different amounts could be reported under different conditions or using different assumptions. These judgements, estimates and assumptions are subject to change as new events occur, as more experience is acquired, as additional information is obtained, and as the general operating environment changes.

We believe the following are the most critical accounting policies, estimates, and judgements that we have used in the preparation of our financial statements:

Retirement Liability

We sponsor a plan that provides a post-retirement benefit for eligible long-service employees. The valuation of this plan is estimated based on complex actuarial calculations using several assumptions. These assumptions are determined by management with significant input from our actuary. The valuation of the obligation depends on such assumptions as discount rate, number of employees, projected salary increases, retirement age, average years of service and termination rates. An actuarial valuation of the plan at March 31, 2017, was obtained and the accrued benefit obligation estimated at \$20.9 million. The retirement liability was increased and the actuarial loss of \$1.9 million was recognized in other comprehensive income during fiscal 2018. The main drivers of the increase in the liability were a higher annual increase in salaries and a higher number of employees than previously estimated. The liability included in accrued employee future benefits in our financial statements at March 31, 2018, was \$20.2 million (\$18.9 million at March 31, 2017).

Depreciation and Amortization Expense

Our capital assets, including assets under finance leases, are depreciated or amortized on a straight-line basis at varying rates. Depreciation and amortization rates require the use of estimates of the useful lives of the assets and of salvage value to be realized upon asset retirement.

We annually review asset lives in conjunction with our longer-term asset deployment, replacement and upgrade strategies. When we determine that asset lives do not reflect the expected remaining period of benefit, we make prospective changes to the remaining period over which they are depreciated or amortized. Estimates of useful life are monitored routinely through maintenance and refit programs, ongoing long-term fleet management and comparable vessels in use internally and externally.

Salvage value for vessels is monitored through secondary markets. Our expectation is that decommissioned vessels will be sold at a nominal salvage price into world markets to buyers who will keep them in active service.

There are a number of uncertainties inherent in estimating our asset lives and residual value and changes in these assumptions could result in material adjustments to our financial statements.

As disclosed in note 1 to our financial statements, we review and evaluate our long-lived assets for impairment when events or changes in circumstances indicate that the related amounts may not be recoverable.

For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows that are largely independent of the cash flows from other assets or groups of assets. If the carrying value is greater than the recoverable amount, the excess is charged to net earnings. Impairment losses are evaluated for potential reversals and are only reversed to the extent an asset's carrying amount does not exceed the carrying amount that would have been determined had no impairment been recognized.

Price caps for each route group, as defined in the CFSC with the Province are set by the Commissioner based on the principle that the costs necessary to provide the service system-wide are recovered.

Hedging Relationships

We utilize derivative financial instruments to manage market risk against the volatility in foreign currency, interest rate, and fuel price exposures. We do not utilize derivative financial instruments for trading or speculative purposes. At the inception of each hedge, we determine whether or not to apply hedge accounting.

When applying hedge accounting, we document all relationships between hedging instruments and hedged items, as well as our risk management objectives and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the statement of financial position or to specific firm commitments or forecast transactions. We also assess, both at the hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items. When derivatives are designated in a cash flow hedging relationship, the effective portion of changes in the fair value of the derivatives is recognized in other comprehensive income. Gains or losses on derivatives used in cash flow hedges of forecast purchases of non-financial assets are reclassified from equity (accumulated other comprehensive income) and are included in the initial carrying amount of the non-financial asset acquired. Gains or losses on derivatives for hedging relationships related to other cash flow hedges are reclassified from other accumulated comprehensive income to net earnings or loss when the hedged item affects net earnings or loss. Realized and unrealized gains or losses associated with derivative instruments which have been terminated or cease to be effective prior to maturity are recognized in net earnings in the period in which they have been terminated or cease to be effective.

Asset Retirement Obligations

When it can be reasonably determined, we recognize the fair value of a liability for any legal obligations associated with the retirement of long-lived assets when those obligations result from the acquisition, construction, development or normal operation of the assets. A corresponding asset retirement cost is added to the carrying amount of the related asset and depreciated or amortized to expense on a systematic and rational basis.

Certain of our vessels contain undetermined amounts of asbestos. We may be required to handle and dispose of the asbestos in a manner required by regulations. It is our intention to sell decommissioned vessels into world markets to buyers who will keep them in active service. Under these circumstances, asbestos remediation would become the responsibility of the new owner.

No amount has been recorded for asset retirement obligations relating to these assets as it is not possible to make a reasonable estimate of the fair value of any such liability due to the indeterminate magnitude, likelihood, or financial impact, if any, of this issue. In addition, there is a reasonable expectation that retired assets may be sold to a responsible secondary market at a nominal salvage price, and furthermore, because we are a regulated entity, any significant asset retirement costs that cannot be mitigated by the responsible sale of the retired asset, would be recoverable through future tariffs.

Adoption of New Accounting Standards

There are no relevant changes in accounting standards applicable to our fiscal year beginning April 1, 2017.

Future Accounting Changes

The following is a discussion of accounting changes that will be effective for us in future accounting periods:

IFRS 15 *Revenue from Contracts with Customers* replaces IAS 18 *Revenue* and IAS 11 *Construction Contracts*, providing guidance on the amount and/or timing of recognition of revenue. IFRS 15 is effective for us April 1, 2018 and we will use the modified retrospective with cumulative effect method of adoption. We have assessed the recognition of our revenues under IFRS 15, using the five-step model. There is no change in our revenue recognition to the majority of our revenues. IFRS 15 requires us to recognize revenue from the expected breakage (a customer's unexercised, contractual rights to receive future services which have not been exercised but for which the customer has made a non-refundable prepayment) when the likelihood of the customer exercising their remaining rights becomes remote. At April 1, 2018, we will recognize breakage revenue from our prepaid stored value card as an increase to retained earnings and a decrease to deferred revenue. Also at April 1, 2018, we will recognize an increase to deferred revenue and decrease to retained earnings to reflect a timing change in revenue recognition for a third party travel voucher. We do not expect the application to have a significant impact on our consolidated financial statements, other than additional disclosure.

IFRS 9 *Financial Instruments* (2014) introduces a new expected credit loss model for calculating impairment, and incorporates guidance on the classification and measurement of financial assets and the final general hedge accounting requirements originally published in IFRS 9 (2013). Mandatory adoption of IFRS 9 (2014) for us is April 1, 2018 with retrospective application. We adopted IFRS 9 *Financial Instruments* (2013) in fiscal 2015, and as such, will only be impacted by the expected credit loss model when we adopt IFRS 9 (2014). This model applies to our trade receivables and long-term loan receivable. We have determined that we will need to establish an expected credit loss for our trade receivables. We do not expect the application of IFRS 9 to have a significant impact on our consolidated financial statements, other than additional disclosure, as we have an existing provision for impairment.

IFRS 16 *Leases* introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all assets with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. The mandatory effective date for us is April 1, 2019. Early adoption is permitted if IFRS 15 *Revenue from Contracts with Customers* has also been applied. We have elected to early adopt IFRS 16 for the annual reporting period beginning on April 1, 2018, using the modified retrospective with cumulative effect method and applying the following practical expedients on initial application:

- use of the modified retrospective approach with no restatement of prior periods;
- application only to contracts that were previously identified as leases;
- use of a single discount rate to a portfolio of leases; and
- electing to not recognize leases for which the underlying asset is of low value.

Our audited consolidated financial statements for the year ended March 31, 2018 disclosed our future lease commitments of \$2.3 million, representing 16 leases. Based on this and our analysis, we do not expect the application of IFRS 16 to have a significant impact on our consolidated financial statements, other than additional disclosure.

On February 7, 2018, the IASB published Amendments to IAS 19 *Employee Benefits* which requires entities to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the period after a plan amendment, curtailment or settlement. It also requires that any reduction in surplus, even amounts not previously recognized due to an asset ceiling limitation, be recognized in profit or loss as part of past service cost of a gain or loss on settlement. The amendments are effective for us on April 1, 2019. Early adoption is permitted. We are reviewing the amendments to determine the potential effects. We do not expect the application of this standard to have a significant impact on our consolidated financial statements.

CORPORATE STRUCTURE AND GOVERNANCE

National Instrument 58-101 *Disclosure of Corporate Governance Practices* (the "NI 58-101") and a related National Policy 58-201 *Corporate Governance Guidelines* (the "Guidelines") issued by the Canadian Securities Administrators require reporting issuers to disclose annually their approach to corporate governance with reference to specific matters. See Schedule A for the disclosure required by NI 58-101.

Forward Looking Statements

This report contains certain "forward looking statements". These statements relate to future events or future performance and reflect management's expectations regarding our growth, results of operations, performance, business prospects and opportunities and industry performance and trends. They reflect management's current internal projections, expectations or beliefs and are based on information currently available to management. Some of the market conditions and factors that have been considered in formulating the assumptions upon which forward looking statements are based include traffic, the Canadian Dollar relative to the US Dollar, fuel costs, construction costs, the state of the local economy, fluctuating financial markets, demographics, tax changes, and the requirements of the Coastal Ferry Services Contract.

Forward looking statements included in this document include statements with respect to:

- traffic levels;
- our short-term and long-range business plans;
- our asset renewal programs for vessels and terminals; and
- our pricing promotions, underwater radiated noise, Salish Class vessels, the *Northern Sea Wolf*, Spirit Class mid-life upgrades, and minor vessel replacements.

In some cases, forward looking statements can be identified by terminology such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "predict", "potential", "continue" or the negative of these terms or other comparable terminology. A number of factors could cause actual events or results to differ materially from the results discussed in the forward looking statements. In evaluating these statements, prospective investors should specifically consider various factors including, but not limited to, the risks and uncertainties associated with: vendor non-performance; capital market access; interest rate, foreign currency, fuel price, and traffic volume fluctuations; the implementation of major capital projects; security, safety, and environmental incidents; confidential or sensitive information breaches; changes in laws; vessel repair facility limitations; economic regulatory environment changes; tax changes; and First Nation claims.

Actual results may differ materially from any forward looking statement. Although management believes that the forward looking statements contained in this report are based upon reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward looking statements. These forward looking statements are made as of the date of this report, and British Columbia Ferry Services Inc. assumes no obligation to update or revise them to reflect new events or circumstances except as may be required by applicable law.

Non-IFRS Measures

In addition to providing measures prepared in accordance with IFRS, we present certain financial measures that do not have any standardized meanings prescribed by IFRS and therefore are unlikely to be comparable to similar measures presented by other companies. These include, but are not limited to, net earnings adjusted for the effect of rate regulation. These supplemental financial measures are provided to assist readers in determining our ability to generate cash from operations and improve the comparability of our results from one period to another. We believe these measures are useful in assessing operating performance of our ongoing business on an overall basis.

SCHEDULE A

Corporate Structure and Governance Board of Directors

British Columbia Ferry Services Inc. ("BC Ferries" or the "Company") is a company incorporated in British Columbia which is subject to the *Business Corporations Act – British Columbia* and the *Coastal Ferry Act – British Columbia* ("CFA"). The board of directors ("board") of BC Ferries is appointed by the Company's sole voting shareholder, B.C. Ferry Authority ("BCFA" or the "Authority"), a corporation without share capital established by the CFA.

During the fiscal year ended March 31, 2018, the board was composed of the following directors:

Chair: Donald P. Hayes

Members: Jane M. Bird, Bruce A. Chan, Jan K. Grude, John A. Horning, Brian G. Kenning, Gordon M. Kucec,
Sarah A. Morgan-Silvester and P. Geoffrey Plant (vice chair)

Jan K. Grude was elected a director effective June 23, 2017 and Jane M. Bird ceased to be a director effective February 23, 2018.

The directors are stewards of BC Ferries and set the strategic direction of the Company. The board exercises its stewardship responsibilities by overseeing the conduct of the business, supervising management, which is responsible for the day-to-day conduct of the business, and endeavouring to ensure that all major issues affecting the business and affairs of the Company are given proper consideration.

The board governance manual articulates the governance framework under which the board fulfills its stewardship responsibilities. The manual assembles in one document the essential elements for providing an appropriate level of governance for the organization. It includes, among other things, terms of reference for the board, chair, directors, committees and committee chairs, and serves as a practical guide for the board and management in fulfilling their respective duties and responsibilities. The governance manual is the product and responsibility of the board.

The board is committed to the principles of independence and accountability. The board has adopted policies and practices that ensure it has the capacity, independent of management, to fulfill the board's responsibilities, make objective assessments of management, and assess the merits of management initiatives. The board's Governance & Nominating Committee has an ongoing responsibility to ensure that the board's governance structures and processes continue to enable the board to function independently.

The board and management recognize that there is a need for the board to meet regularly without management in attendance. It is the board's general practice to conduct a portion of every board and committee meeting with no members of management in attendance.

The board and its committees each have the authority to retain, at the Company's expense, any outside advisor that it determines to be necessary to permit it to carry out its duties.

The recruitment of directors is undertaken with the objective of ensuring the board is composed of qualified directors with a range of relevant expertise and experience. In addition, the board is committed to the principle that a majority of directors, including the chair, should be independent of the Company.

Under guidelines adopted by the board, a director is independent if he or she has no direct or indirect material relationship with the Company. For this purpose, a "material relationship" is a relationship that could, in the view of the board, be reasonably expected to interfere with the exercise of a director's judgment. Members of the board's Audit & Finance Committee are subject to additional independence requirements consistent with the definition of independence in National Instrument 52-110 *Audit Committees*.

The board is responsible for determining whether directors are independent pursuant to the definition of independence adopted by the board. To do this, the board requires members to disclose their relationships with the Company and its subsidiaries. These disclosures are made annually and are reviewed by the chair of the board, the chair of the Governance & Nominating Committee and the corporate secretary, and are reported to the Governance & Nominating Committee and the board. If it has been previously determined that a director is independent of the Company but circumstances arise which could result in a determination that he or she is no longer independent, the director must promptly advise the board.

All of the directors of the Company in the fiscal year were determined by the board to be independent pursuant to the definition of independence adopted by the board.

Directorships

The following are directors of a reporting issuer (or the equivalent) in Canada or a foreign jurisdiction, other than BC Ferries:

Brian G. Kenning: Director, West Fraser Timber Company Ltd.
 Director, Maxar Technologies Inc.
 Director, Adventus Real Estate Investment Trust

Sarah A. Morgan-Silvester: Director, Canadian Western Bank

Orientation and Continuing Education

The Company has a variety of orientation and education programs in place for directors. These programs are aimed at increasing the directors' familiarity with the operation of the Company and its governance practices.

All new directors are provided with the opportunity to participate in an orientation program. The orientation program is tailored to the individual director's needs and areas of interest. The program generally involves a half- to full-day session, usually held prior to a new director attending his/her first board meeting, during which the new director is briefed by members of senior management and receives information about the business and operations of BC Ferries and board governance practices, including the duties and obligations of directors. The board governance manual is made available to all directors. This manual provides a comprehensive overview of the roles and responsibilities of the board, its committees, and the contributions expected by each director.

The board recognizes the importance of ongoing director education and the need for each director to take personal responsibility for this process. To facilitate ongoing education, presentations are made to directors from time to time on matters of particular importance or emerging significance to the Company. As well, attendance by directors at seminars, courses or conferences of relevance to their position as directors of the Company may be arranged. Directors are expected to maintain ongoing familiarization with the operations of BC Ferries through regular system-wide ferry travel. This, together with visits to other facilities and operations of BC Ferries, serves to enhance the directors' ongoing knowledge and understanding of the Company.

Responsibility for ensuring that orientation and ongoing education are provided to directors rests with the chair of the board. The Governance & Nominating Committee has responsibility for reviewing the orientation and education programs to ensure they are effective and meet the needs of directors.

Ethical Business Conduct

The board has established a Code of Business Conduct and Ethics (the "Code") for the Company. The Code is posted on the Company's intranet website for Company personnel, and is available for public view on the Company's internet site and on SEDAR. The board has also adopted a Corporate Disclosure and Securities Trading Policy and a Corporate Communications Policy, both of which are also posted on the Company's intranet and internet sites.

As part of the Company's disclosure controls process, in conjunction with quarter-end financial reporting, appropriate managers are required to confirm their compliance with the Code, the Corporate Disclosure and Securities Trading Policy and the Corporate Communications Policy.

As part of the communication process for the reporting of any questionable accounting and auditing matters, a secure telephone line and a secure e-mail address, each monitored by the executive director of internal audit, as well as a secure e-mail address monitored by the chair of the Audit & Finance Committee, have been established. This has been communicated to Company personnel by intra-Company information bulletin and BC Ferries' newsletter for personnel. The contact particulars are also posted with the Code on the Company's intranet site.

The board, through the Audit & Finance Committee, monitors compliance with the Code through reports received quarterly from management, the external auditor, and the internal auditor.

Directors and officers are required to review the Code annually, and acknowledge their support and understanding of the Code by signing an annual disclosure statement.

The Code requires that directors and officers disclose potential conflicts of interest at the time of their appointment and immediately upon a conflict of interest or potential conflict of interest arising. Such disclosures are communicated to and reviewed by the chair of the board, the chair of the Governance & Nominating Committee and the corporate secretary, and are reported to the Governance & Nominating Committee and the board.

Nomination of Directors

The board nominates qualified candidates to the Authority for election as directors of the Company, and also recommends to the Authority the size of the board.

The Governance & Nominating Committee has responsibility for the director nomination process. The committee is composed entirely of directors who are independent within the meaning of independence adopted by the board, and operates under terms of reference adopted by the board.

Prior to each search for a nominee to the board, the Governance & Nominating Committee, in consultation with the board chair, develops the potential criteria that will guide the selection process, including the preferred skills, experience and expertise, as well as the specific priorities for diversity of background that will be the focus of the particular search. Once approved by the board, the selection criteria are confirmed with the Authority, and potential candidates for nomination are then sought by the Governance & Nominating Committee with the assistance of an external recruitment firm.

The Governance & Nominating Committee, in collaboration with the chair of the board, makes recommendations to the board on suitable candidates for nomination. These recommendations reflect the board's succession plan, and the talents and backgrounds of the existing directors and that of the nominees, including knowledge of or presence in the communities served by BC Ferries, as well as the diversity priorities established for the particular director search. Upon having made a decision on prospective directors, the board forwards its nominations to the Authority.

As required by the CFA, the Authority selects nominees for election to the board in such a way as to ensure that, as a group, the directors are qualified candidates who hold all of the skills and all of the experience needed to oversee the operation of BC Ferries in an efficient and cost-effective manner. The Authority has established a profile recommended by the board, which sets out the key skills and experience that the directors individually and collectively should possess to meet this legislative requirement ("Skills Profile"). This profile is reviewed regularly by the board and the Authority to ensure continued alignment of the skills and experience represented on the board with the key operational and strategic objectives of the Company for which the directors collectively have oversight responsibility.

Board Diversity Policy

The board holds the view that a diverse board makes prudent business sense and makes for better corporate governance.

The board seeks to maintain a composition of talented and dedicated directors with a diverse mix of expertise, experience, skills and backgrounds that is reflective of the nature of the business environment in which the Company operates, and the people and the communities it serves. For purposes of board composition, diversity includes, but is not limited to, business and other experience, skills, education, gender, age, ethnicity, aboriginal status, and geographic location.

The selection of candidates for nomination to the board is based on merit against objective criteria. Within that overriding emphasis, the board seeks to fill vacancies among its members by considering candidates that have skills and experience consistent with the Skills Profile, and bring additional diversity of background.

The board, through the Governance & Nominating Committee, regularly reviews the diversity achieved on the board, and this review informs the diversity priorities that are set each time a search is conducted for a new director. In setting these priorities, the level of representation of women on the board is specifically considered, with the objective being a balanced gender distribution.

The renewal process for the board has been structured in a manner that fosters regular action to further the board's diversity priorities. A succession plan is in place for the board which, at maturity, envisages directors serving a maximum of two four-year terms. Under the plan, the terms of the directors are staggered, with the objective that each year there will be one new director appointed and one existing director re-appointed. This plan helps ensure an appropriate balance on the board between the experienced perspective of long term directors and new perspectives that bring fresh insights. With one director replaced annually, the plan also affords the opportunity to make timely progress in achieving the board's diversity priorities, generally without the need to increase the overall size of the board. From time to time, the board may seek a temporary increase in the size of the board to enable the early recruitment of one or more specific candidates as a means of enhancing or sustaining key skills, experience and/or the diversity objectives of the board.

Executive Compensation

The Human Resources & Compensation Committee is responsible for reviewing and making recommendations to the board on executive compensation.

Executive Compensation Plan

The CFA requires that the compensation of certain executive officers of BC Ferries be set and administered within a remuneration limit prescribed by an executive compensation plan. The Authority is responsible under the CFA for approving such a plan and any amendments thereto.

An executive compensation plan describes the philosophy for executive compensation and the maximum remuneration that the individuals whose compensation is governed by such plan can receive in any fiscal year. The remuneration limits set out in an executive compensation plan are established with the assistance of an independent third-party compensation expert and with reference to the CFA, which requires that the remuneration under an executive compensation plan be consistent with the remuneration provided to individuals who, in organizations in Canada that are of a similar size and scope to BC Ferries, perform similar services or hold similar positions, and not be greater than the remuneration that provincial public sector employers in British Columbia provide to individuals who, in those organizations, perform similar services or hold similar positions.

An executive compensation plan applies to the individuals holding the positions of, or acting in a similar capacity or performing similar functions to, the Chief Executive Officer ("CEO") or an Executive Vice President of BC Ferries. Pursuant to *Miscellaneous Statutes Amendment Act No. 3 - 2010* ("Bill 20"), an individual who held such a position on the date Bill 20 received first reading in 2010 is excluded from the provisions of an executive compensation plan for so long as that individual remains in that executive position with BC Ferries.

The Company's current executive compensation plan is available for public view on the Authority's website (www.bcferryauthority.com). The plan governs the remuneration of BC Ferries' President & CEO, Chief Financial Officer and Chief Operating Officer.

Executive Compensation Process

The executive officers of the Company participate in a salary holdback compensation plan which is designed to link their compensation with the achievement of specific annual operating objectives that are important to supporting the Company's overall business strategy. By its nature, the plan responds to the Company's pay-for-performance philosophy. Under the plan, a maximum salary is established for each participant, a portion of which is held back each fiscal year and payable upon achievement of pre-approved objectives and targets.

On an annual basis, the board, led by the Human Resources & Compensation Committee, sets the performance requirements for the President & CEO and evaluates his performance against those requirements. Similarly, the Human Resources & Compensation Committee leads the board in an annual evaluation of the performance of each of the other executive officers with respect to their achievement of performance objectives set by the President & CEO. The amount, if any, of the salary holdback earned by the President & CEO and the other executive officers is determined based on the evaluation results and, where applicable, the available room under the total remuneration limit set for the position in an executive compensation plan. Changes, if any, to the compensation of the executive officers are made in consideration of the individuals' performance, leadership skills, retention risk, and value to achieving corporate strategy, and in conjunction with market compensation data from appropriate comparator organizations. All changes in compensation are made in accordance with an executive compensation plan, as applicable.

On an annual basis, the President & CEO formally assesses the development of each of the other executive officers. The President & CEO uses these assessments to design and update succession plans for all executive officer positions, including the position of President & CEO. These plans are reviewed by the Human Resources & Compensation Committee on an annual or more frequent basis. With respect to all executive officers, succession planning is an important issue that receives ongoing and regular attention by the board and the President & CEO.

Director Compensation

The CFA requires that the compensation of directors of BC Ferries be set and administered within a remuneration limit prescribed by a directors' compensation plan. The Authority is responsible under the CFA for approving a directors' compensation plan and any amendments thereto. The remuneration provided under a directors' compensation plan must be consistent with the remuneration that organizations in Canada that are of a similar size and scope to BC Ferries provide to their directors, and must not be greater than the remuneration that provincial public sector organizations in British Columbia provide to their directors.

The Company's current compensation plan for directors was developed with the assistance of an independent third-party compensation expert and is available for public view on the Authority's website.

The Governance & Nominating Committee reviews director compensation regularly and provides advice to the board on any amendments to the directors' compensation plan to be recommended to the Authority.

Protocol Agreement

The Authority and BC Ferries have entered into a protocol agreement which clarifies and confirms their respective roles and responsibilities in relation to the authority of BCFA as shareholder of BC Ferries and the matters set forth in the CFA respecting the appointment and remuneration of BC Ferries' directors and the remuneration of certain executive officers of the Company.

Board Committees

The board has developed guidelines for the establishment and operation of committees of the board. The committee structure and membership is reviewed and confirmed by the board on an annual basis.

Mandates

In the fiscal year ended March 31, 2018, the board had five committees, each of which operated according to a specific mandate established by the board. The committees and their mandates are described below.

Audit & Finance Committee

The Audit & Finance Committee is appointed by the board to assist the board in fulfilling its oversight responsibilities in matters related to finance, audit and enterprise risk. The committee has the mandate to:

- review the financial reports and other financial information provided by the Company to its security holders;
- review the annual operating and capital budgets, modifications thereto, and details of any proposed financing;
- monitor the integrity of the financial reporting process and the system of internal controls that the board and management have established;
- monitor the management of the principal risks that could impact the financial reporting of the Company, and the Company's compliance with legal and regulatory requirements as they relate to the Company's financial statements;
- review and approve the audit plan, process, results, and performance of the Company's external auditor and the internal audit department (the internal auditor) while providing an open avenue of communication between the board, management, external auditor, and the internal auditor; and
- assess the qualifications and independence of the external auditor, and recommend to the board the nominations of the external auditor and the compensation to be paid to the external auditor.

The committee has the authority to conduct any investigation appropriate to fulfilling its responsibilities, and it has direct access to the Company's external auditor as well as anyone in the organization. The committee has the authority to retain such legal, accounting, and other advisors or experts it deems necessary in the performance of its duties.

Each of the members of the committee has been determined by the board to be independent within the meaning of independence adopted by the board.

All members of the committee are financially literate within the meaning of National Instrument 52-110 *Audit Committees*, that is, each has the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the Company's financial statements.

Since April 2, 2003, all recommendations of the committee to nominate or compensate an external auditor have been adopted by the board.

The aggregate fees billed by the Company's external auditor in each of the last two fiscal years were:

Year ended March 31 (\$ thousands)	2018	2017
External Auditor billings		
Audit and audit related	176.6	176.4
Tax services	2.3	2.3
Accounting advisory	–	1.4
	178.9	180.1

Pursuant to its terms of reference, the committee must pre-approve retaining the external auditor for any non-audit service to be provided to the Company or its subsidiaries, provided that no approval shall be provided for any service that is prohibited under the rules of the Canadian Public Accountability Board or the Public Company Accounting Oversight Board, or the Independence Standards of the Chartered Professional Accountants of Canada.

Before retaining the external auditor for any non-audit service, the committee must consider the compatibility of the service with the external auditor's independence. The committee may pre-approve retaining the external auditor for the engagement of any non-audit services by establishing policies and procedures to be followed prior to the appointment of the external auditor for the provision of such services. To date, no such policies and procedures have been established. In addition, the committee may delegate to one or more members the authority to pre-approve retaining the external auditor for any non-audit services to the extent permitted by applicable law.

Safety, Health, Environment & Security Committee

The Safety, Health, Environment & Security Committee is appointed by the board to assist the board in fulfilling its oversight responsibilities in matters related to safety, health, environment and security. The committee has the mandate to:

- exercise due diligence over the safety, health, environmental and security operations of the Company;
- develop, review, and make recommendations, as required, on matters related to the Company's safety, health, environmental and security policies and practices; and
- monitor compliance with government regulations and with the Company's commitment to excellence in matters of safety, health, environment and security.

Governance & Nominating Committee

The Governance & Nominating Committee is appointed by the board to assist the board in fulfilling its oversight responsibilities with respect to ensuring that the corporate governance system of BC Ferries is effective. The committee has the mandate to:

- review, assess, and make recommendations regarding the effectiveness of the policies and practices of the board;
- ensure the board's continuing ability to fulfill its legislative mandate;
- implement effective due diligence over the operations of the Company;
- make recommendations on the skills, experience and expertise that board members collectively and individually should have in order to oversee the operation of BC Ferries in an efficient and cost-effective manner;
- establish and implement effective processes for identifying and recommending suitable candidates for nomination as directors of BC Ferries; and
- make recommendations on the remuneration of directors of BC Ferries.

Human Resources & Compensation Committee

The Human Resources & Compensation Committee is appointed by the board to assist the board in fulfilling its oversight responsibilities regarding the human resources and compensation strategies and policies of BC Ferries. The committee has the mandate to:

- regularly review, at a strategic level, the approach taken to manage the Company's human resources, including the recruitment, retention, motivation and engagement of employees, in the interests and success of the Company;
- regularly review the succession and development plans for the President & CEO and executive management; and
- review and recommend to the board a total compensation philosophy for the President & CEO and executive management that, subject to the CFA, attracts and retains executives, links total compensation to financial and operational performance, and provides competitive total compensation opportunities at a reasonable cost, while enhancing the ability to fulfill the Company's overall business strategies and objectives.

Strategic Projects Committee

The Strategic Projects Committee is appointed by the board to assist the board in fulfilling its oversight responsibilities with respect to specific capital projects of BC Ferries as designated by the board from time to time. For the projects under its purview, the committee has the mandate to:

- in respect of projects which have not yet been approved by the board, review and provide advice to the Audit & Finance Committee and the board on whether the Company should proceed with the projects and, where approval to proceed is recommended, provide advice on the schedule, scope and budget for such projects; and
- in respect of projects which have been approved by the board, and as so directed by the board:
 - review the governance structure for the projects;
 - regularly review and monitor progress against scope and budget, as well as material changes in the schedule and risk profile of the projects;
 - review and recommend to the Audit & Finance Committee and the board any changes in authorized scope and budget of the projects; and
 - upon project completion, ascertain whether the projects have met their objectives.

Composition

The memberships of the committees in the fiscal year ended March 31, 2018 are set out below. The board chair serves as a non-voting ex-officio member of each of the committees.

DIRECTOR	BOARD COMMITTEES YEAR ENDED MARCH 31, 2018				
	AUDIT & FINANCE	SAFETY, HEALTH, ENVIRONMENT & SECURITY	GOVERNANCE & NOMINATING	HUMAN RESOURCES & COMPENSATION	STRATEGIC PROJECTS
Donald P. Hayes	• (ex-officio)	• (ex-officio)	• (ex-officio)	• (ex-officio)	• (ex-officio)
Jane M. Bird ¹		• (chair)	•	•	
Bruce A. Chan	•	•			•
Jan A. Grude ²	•		•		•
John A. Horning	•			• (chair)	•
Brian G. Kenning	• (chair)			•	
Gordon M. Kucec		•	•		• (chair)
Sarah A. Morgan-Silvester	•	•		•	
P. Geoffrey Plant	•	•	• (chair)		

Notes:

1. Jane M. Bird ceased to be a director and a member of the Safety, Health, Environment & Security Committee, the Governance & Nominating Committee and the Human Resources & Compensation Committee effective February 23, 2018.

2. Jan K. Grude was appointed a member of the Audit & Finance Committee, the Governance & Nominating Committee and the Strategic Projects Committee effective August 18, 2017.

Assessments

As part of its dedication to best governance practices, the board is committed to regular assessments of the effectiveness of the board, the board chair, committees, committee chairs, and individual directors. The board, on the recommendation of the Governance & Nominating Committee, has implemented a process for such assessments consisting of a review facilitated by an independent consultant every second year. The process aims to ensure that the individual directors continue to contribute effectively to the board's performance, and that the board and its committees continue to function effectively.

The last facilitated review was completed in February 2017. The consultant engaged by the board to conduct the review obtained the directors' views on matters related to the effectiveness of the board through the use of questionnaires and individual discussions with each director. The evaluation included an assessment of the performance of the board as a whole with respect to best practices in board governance, as well as a director self-assessment and peer review related to best practices for board directors. The peer review results for each director were shared with the respective director, the chair of the board and the chair of the Governance & Nominating Committee, and discussions on the results were held between the individual directors and the board chair. The results of the board evaluation were provided to the board, together with the consultant's recommendations for action. The results and the recommendations arising from the board evaluation have and will continue to inform the deliberations and decisions of the board.

The performance of the board as a whole, and the performance of individual directors, is also assessed regularly throughout the year. This occurs primarily through discussions between the individual directors and the board chair.

BC Ferries management is responsible for presentation and preparation of the annual consolidated financial statements, management's discussion and analysis (MD&A) and all other information in this annual report.

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards. The consolidated financial statements and information in the MD&A necessarily include amounts based on management's informed judgements and best estimates. The financial information presented elsewhere in this annual report is consistent with that in the consolidated financial statements.

To meet its responsibility for reliable and accurate financial statements, management has established systems of internal control that are designed to provide reasonable assurance that assets are safeguarded from loss and that reliable financial records are maintained. These systems are monitored by management and by internal auditors. In addition, the internal auditors perform appropriate tests and related audit procedures.

The consolidated financial statements have been examined by KPMG LLP, independent chartered accountants. The external auditors' responsibility is to express a professional opinion on the fairness of management's consolidated financial statements. The auditors' report outlines the scope of their examination and sets forth their opinion.

The Board of Directors, through its Audit & Finance Committee, oversees management's responsibilities for financial reporting and internal control. The Audit & Finance Committee meets with the internal auditors, the independent auditors and management to discuss auditing and financial matters and to review the consolidated financial statements and the independent auditors' report. The Audit & Finance Committee reports its findings to the Board for consideration in approving the consolidated financial statements for issuance.



MARK F. COLLINS

President & Chief Executive Officer



M. ALANA GALLAGHER

Vice President, Finance & Chief Financial Officer

Victoria, Canada

June 29, 2018

TO THE SHAREHOLDERS OF BRITISH COLUMBIA FERRY SERVICES INC.

We have audited the accompanying consolidated financial statements of British Columbia Ferry Services Inc., which comprise the consolidated statements of financial position as at March 31, 2018 and March 31, 2017, the consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

MANAGEMENT'S RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of British Columbia Ferry Services Inc. as at March 31, 2018 and March 31, 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.



Chartered Professional Accountants

Victoria, Canada

June 19, 2018

BRITISH COLUMBIA FERRY SERVICES INC.
Consolidated Statements of Financial Position (Expressed in thousands of Canadian dollars)

As at March 31	2018	2017
ASSETS		
Current assets		
Cash and cash equivalents (note 3)	69,913	72,032
Restricted short-term investments (note 10(f))	32,276	32,426
Other short-term investments	114,259	115,582
Trade and other receivables (note 15(a))	26,258	15,319
Prepaid expenses	8,434	7,454
Inventories (note 4)	31,584	28,257
Derivative assets (note 15(c))	12,530	1,604
	295,254	272,674
Non-current assets		
Loan receivable (note 12)	24,515	24,515
Land lease (note 5)	29,771	30,230
Property, plant and equipment (note 6)	1,713,080	1,621,802
Intangible assets (note 7)	99,802	97,673
	1,867,168	1,774,220
Total assets	2,162,422	2,046,894
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	77,233	55,173
Interest payable on long-term debt (note 8)	18,537	18,458
Deferred revenue	32,034	20,705
Derivative liabilities	–	1,048
Current portion of long-term debt (note 8,10)	34,594	30,939
Current portion of accrued employee future benefits (note 11(d))	3,000	1,400
Current portion of obligations under finance lease (note 8,12)	1,652	1,582
Provisions (note 9)	60,372	55,711
	227,422	185,016
Non-current liabilities		
Accrued employee future benefits (note 11(d))	21,299	20,913
Long-term debt (note 8,10)	1,279,775	1,273,860
Obligations under finance lease (note 8,12)	38,769	40,423
Other liabilities (note 13)	7,750	5,250
	1,347,593	1,340,446
Total liabilities	1,575,015	1,525,462
EQUITY		
Share capital (note 18)	75,478	75,478
Contributed surplus	25,000	25,000
Retained earnings	477,955	424,020
Total equity before reserves	578,433	524,498
Reserves (note 20(a))	8,974	(3,066)
Total equity including reserves	587,407	521,432
Total liabilities and equity	2,162,422	2,046,894

Commitments (note 6 and note 16)

Contingencies (note 17)

See accompanying notes to the consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Comprehensive Income (Expressed in thousands of Canadian dollars)

Years ended March 31	2018	2017
Revenue		
Vehicle and passenger fares	640,234	608,713
Ferry service fees (note 25)	178,540	174,871
Net retail (note 21)	60,071	55,139
Federal-Provincial Subsidy Agreement (note 26)	29,782	29,158
Fuel rebates (note 27)	(19,386)	(18,068)
Other income	9,777	9,470
Total revenue	899,018	859,283
Expenses (note 22)		
Operations	496,753	467,300
Maintenance	87,615	74,165
Administration	38,399	35,804
Depreciation and amortization	159,916	148,952
Total operating expenses	782,683	726,221
Operating profit	116,335	133,062
Net finance and other expenses (note 23)		
Finance expenses	60,679	58,759
Finance income	(5,495)	(4,651)
Net finance expense	55,184	54,108
Loss on disposal and revaluation of property, plant and equipment and intangible assets	1,178	1,588
Net finance and other expenses	56,362	55,696
NET EARNINGS	59,973	77,366
Other comprehensive income (note 20(b))		
Items not to be reclassified to net earnings	(118)	2,480
Items to be reclassified to net earnings	13,580	12,119
Total other comprehensive income	13,462	14,599
Total comprehensive income	73,435	91,965

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Cash Flows (Expressed in thousands of Canadian dollars)

Years ended March 31	2018	2017
Cash flows from operating activities		
Net earnings	59,973	77,366
Items not affecting cash		
Net finance expense	55,184	54,108
Depreciation and amortization	159,916	148,952
Other non-cash adjustments to property, plant and equipment	2,185	(279)
Changes in:		
Accrued employee future benefits	43	(188)
Derivative assets recognized in net earnings	(64)	(5)
Provisions	4,661	7,021
Long-term land lease	459	458
Accrued financing costs	(233)	286
Total non-cash items	222,151	210,353
Movements in operating working capital		
Trade and other receivables	(10,939)	930
Prepaid expenses	(980)	1,096
Inventories	(3,327)	(4,269)
Accounts payable and accrued liabilities	22,060	(3,033)
Deferred revenue	11,329	1,822
Change in non-cash working capital	18,143	(3,454)
Change attributable to capital asset acquisitions	(24,258)	2,357
Change in non-cash operating working capital	(6,115)	(1,097)
Cash generated from operating activities	276,009	286,622
Interest received	5,560	4,339
Interest paid	(65,615)	(64,526)
Net cash generated by operating activities	215,954	226,435

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Cash Flows (Expressed in thousands of Canadian dollars)

Years ended March 31	2018	2017
Cash flows from financing activities		
Proceeds from long-term debt	45,264	90,122
Repayment of long-term debt	(35,312)	(24,934)
Repayment of finance lease obligations	(1,583)	(1,512)
Dividends paid on preferred shares	(6,038)	(6,038)
Deferred financing costs incurred	(1,417)	(2,965)
Net cash generated by financing activities	914	54,673
Cash flows from investing activities		
Proceeds from disposal of property, plant and equipment	476	137
Purchase of property, plant and equipment and intangible assets	(220,936)	(233,768)
Changes in debt service reserve	150	(440)
Net proceeds from (purchase of) short-term investments	1,323	(54,118)
Net cash used in investing activities	(218,987)	(288,189)
Net decrease in cash and cash equivalents	(2,119)	(7,081)
Cash and cash equivalents, beginning of year	72,032	79,113
Cash and cash equivalents, end of year	69,913	72,032

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Changes in Equity (Expressed in thousands of Canadian dollars)

	SHARE CAPITAL (NOTE 18)	CONTRIBUTED SURPLUS	RETAINED EARNINGS	TOTAL EQUITY BEFORE RESERVES	RESERVES (NOTE 20(A))	TOTAL EQUITY INCLUDING RESERVES
Balance as at April 1, 2016	75,478	25,000	352,692	453,170	(24,223)	428,947
Net earnings	–	–	77,366	77,366	–	77,366
Other comprehensive income	–	–	–	–	14,599	14,599
Realized hedge losses recognized in fuel swaps	–	–	–	–	6,310	6,310
Hedge losses on interest rate forward contract reclassified to net earnings	–	–	–	–	248	248
Preferred share dividends	–	–	(6,038)	(6,038)	–	(6,038)
Balance as at March 31, 2017	75,478	25,000	424,020	524,498	(3,066)	521,432
Net earnings	–	–	59,973	59,973	–	59,973
Other comprehensive income	–	–	–	–	13,462	13,462
Realized hedge gains recognized in fuel swaps	–	–	–	–	(1,670)	(1,670)
Hedge losses on interest rate forward contract reclassified to net earnings	–	–	–	–	248	248
Preferred share dividends	–	–	(6,038)	(6,038)	–	(6,038)
Balance as at March 31, 2018	75,478	25,000	477,955	578,433	8,974	587,407

YEARS ENDED MARCH 31, 2018 AND 2017**(Tabular amounts expressed in thousands of Canadian dollars)**

British Columbia Ferry Services Inc. (the "Company") was incorporated under the *Company Act (British Columbia)* by way of conversion on April 2, 2003, and now validly exists under the *Business Corporations Act (British Columbia)*. The Company's primary business activity is the provision of coastal ferry services in British Columbia.

The Company is subject to the *Coastal Ferry Act* (the "Act") as amended, which came into force on April 1, 2003. Its common share is held by the B.C. Ferry Authority (the "Authority"), a corporation without share capital, and it is regulated by the British Columbia Ferries Commissioner (the "Commissioner") to ensure that rates are fair and reasonable and to monitor service provided.

The Company's business is seasonal in nature, with the highest activity in the summer (second quarter) and the lowest activity in the winter (fourth quarter), due to the high number of leisure travellers and their preference for travel during the summer months. The Company also takes advantage of the low activity during the winter months to perform a significant portion of the required annual maintenance on vessels and terminals.

1. ACCOUNTING POLICIES:**(a) Basis of preparation:**

British Columbia Ferry Services Inc. is a company domiciled in Canada. The address of the Company's registered office is Suite 500, 1321 Blanshard Street, Victoria, BC, Canada, V8W 0B7. These consolidated financial statements as at and for the years ended March 31, 2018 and 2017 comprise the Company and its subsidiaries (together referred to as the "Group").

These consolidated financial statements represent the annual statements of the Group prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). In accordance with IFRS, the Group has provided comparative financial information and applied the same accounting policies throughout all periods presented.

These consolidated financial statements were approved by the Board of Directors on June 19, 2018.

These consolidated financial statements have been prepared using the historical cost method, except for land, land under finance lease and certain financial assets and liabilities including derivatives.

These consolidated financial statements are presented in Canadian dollars ("CAD") which is the Group's functional currency. All tabular financial data is presented in thousands of Canadian dollars.

Transactions denominated in foreign currencies are translated by applying the exchange rate prevailing on the date of the transaction. At each reporting date, all monetary assets and liabilities denominated in foreign currencies are translated into CAD at the closing exchange rate. Any resulting translation adjustments are recorded in net earnings.

The Group operates within a single industry, within a single geographical area and under a single regulated contract. Review of operating results and decisions about resources to be allocated are done at a corporate level. Accordingly no segment reporting is presented in these consolidated financial statements.

(b) Basis of consolidation – subsidiaries:

A subsidiary is an entity controlled by the Group. Control exists when the Group has the power to manage, either directly or indirectly, the entity's financial and operational policies in order to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The financial statements of all subsidiaries are prepared to the same reporting date as the Group using consistent accounting policies.

The Group's wholly-owned subsidiaries as at March 31, 2018 are:

Pacific Marine Leasing Inc.

BCF Captive Insurance Company Ltd.

All inter-Group balances and transactions are eliminated on consolidation.

(c) Estimates and judgments:

The preparation of consolidated financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting methods and the amounts recognized in the financial statements. These estimates and the underlying assumptions are established and reviewed continuously on the basis of past experience and other factors considered reasonable in the circumstances. They therefore serve as the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from the estimates.

Significant judgments relate to the provision for contingencies, including asset retirement obligations. In forming these judgments, the Group considers the probability of future payments.

Significant estimates relate to:

(i) Property, plant and equipment and intangible assets

The calculation of depreciation and amortization involves estimates concerning the economic life and salvage value of property, plant and equipment and intangible assets. The Group applies judgment to determine expenditures eligible for capitalization and considers the future economic benefits of these expenditures in making this assessment.

(ii) Employee future benefits

Accounting for the costs of future employee benefits is based on actuarial valuations, relying on key estimates for discount rates, future salary levels, employee turnover rates and mortality tables.

(iii) Derivative assets and liabilities

Fair values for the derivative assets and liabilities are estimated using period-end market rates. These fair values approximate the amount that the Group would pay to settle the contract at the date of the statement of financial position. The calculation of the effectiveness of instruments that have been designated for hedge accounting is based on key estimates for the market price, rate of interest and volatility, and the credit risk of the instruments.

(d) Hedging relationships:

When applying hedge accounting, the Group documents all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. This process includes linking all derivatives to specific assets and liabilities on the statement of financial position or to specific firm commitments or forecast transactions. The Group also assesses, both at the hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items.

When derivatives are designated in a cash flow hedging relationship, the effective portion of changes in the fair value of derivatives is recognized in other comprehensive income ("OCI"). Any ineffective portion of a hedging relationship is recognized immediately in net earnings or loss. Accumulated gains or losses are transferred to net earnings or loss in the period when the related forecast transaction affects net earnings or loss.

When the hedged transaction results in the recognition of a non-financial asset or a non-financial liability, the gains or losses previously deferred are transferred directly from reserves and included in the measurement of the initial carrying amount of the asset or liability.

When derivatives in a hedging relationship expire or are sold and the forecast transaction is still expected to occur, any cumulative gains or losses relating to the derivative remain in reserves and are recognized in net earnings or loss when the forecast transaction occurs. If the forecast transaction is no longer expected to occur, the cumulative gains or losses are immediately reclassified to net earnings or loss.

(e) Property, plant and equipment:

Property, plant and equipment, excluding land assets, are carried at cost less accumulated depreciation and any recognized impairment loss. Cost includes direct overhead, financing costs and the initial estimate of retirement obligations.

Land is carried at fair value using the annual assessed values for property tax purposes as being representative of the fair values of these assets. Fair value increases of land assets are recognized in OCI except to the extent that such an increase represents a reversal of an amount previously recognized in net earnings or loss. Fair value decreases are recognized in net earnings or loss to the extent that the decrease exceeds the balance, if any, held in the land revaluation reserve relating to a previous revaluation.

The cost of self-constructed assets includes expenditures on materials, direct labour, financing costs and an allocated proportion of project overheads. Major parts of an item of property, plant and equipment with different estimated useful lives are accounted for as separate items (major components) of property, plant and equipment. When the cost of replacing part of an item of property, plant and equipment is capitalized, the carrying amount of the replaced part is derecognized. Any gain or loss on disposal or retirement of an item of property, plant and equipment is determined as the difference between the proceeds from disposal and the carrying amount of the asset and is recognized in net earnings or loss.

The cost of major overhauls and inspections is capitalized and depreciated over the period until the next major overhaul or inspection. Maintenance and repair expenditures that do not improve or extend productive life are expensed in the period incurred.

Where major components of an asset have different estimated useful lives, depreciation is calculated on each separate component. Depreciation commences when an asset is available for use. Estimates of remaining useful lives and residual values are reviewed annually and adjusted when appropriate.

Property, plant and equipment, including assets under finance leases, are depreciated on a straight-line basis over the estimated useful lives of the assets at the following rates:

ASSET CLASS	ESTIMATED USEFUL LIFE
Vessel hulls	45 years
Vessel propulsion and utility systems	20 to 30 years
Vessel hull, propulsion and generator overhaul	4 to 5 years
Marine structures	20 to 40 years
Buildings	20 to 40 years
Equipment and other	3 to 20 years

(f) Intangible assets:

Intangible assets consist of acquired computer software and licenses and rights of use as well as internally developed computer software and website. These assets are carried at cost plus direct overhead and financing costs, less accumulated amortization and any recognized impairment loss.

Development costs are recognized as intangible assets if it is probable that the asset created will generate future economic benefits, the costs can be reliably measured, the product is technically feasible and the Group intends to, and has sufficient resources to, complete development and use the asset. Website costs are capitalized where the expenditure is incurred on developing an income generating website. Software and website costs capitalized include materials, direct labour and financing costs. Subsequent expenditure is capitalized only if the estimated useful life is extended or functionality of the existing software is enhanced. Costs associated with maintaining computer software are expensed in the period incurred.

Intangible assets with finite useful lives are amortized on a straight-line basis over their estimated useful lives (3 to 7 years) since this most closely reflects the expected pattern of consumption of future economic benefits embodied in the asset. Rights of use intangible assets are amortized on a straight-line basis over their estimated useful lives of 10 to 30 years. Amortization commences when an asset is available for use. Estimates of remaining useful lives and residual values are reviewed annually and adjusted when appropriate.

(g) Leases:

Leases entered into are classified as either finance or operating leases. Leases that transfer substantially all the risks and rewards of ownership to the Group are accounted for as finance leases. Items of property, plant and equipment held under finance leases are initially recognized at the lower of their fair value at the inception of the lease and the present value of the minimum lease payments. Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Lease payments under an operating lease are recognized as an expense on a straight-line basis over the lease term.

(h) Financing costs:

The Group capitalizes financing costs that are directly attributable to the acquisition, construction or production of qualifying assets, as a part of the cost of those assets, until such time as the assets are substantially ready for their intended use. The Group identifies a qualifying asset as one that necessarily takes six months or more to be ready for its intended use.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the Group capitalizes the actual financing costs incurred during the period less any income generated from temporary investment of those borrowings.

To the extent that a qualifying asset is funded by general borrowings, the Group determines the financing costs eligible for capitalization by applying the weighted average cost of borrowings for the period to the expenditures on that asset.

All other financing costs are recognized in net earnings or loss in the period in which they are incurred.

(i) Inventories:

Inventories are carried at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs to make the sale.

Fuel inventories are accounted for using the first-in–first-out principle. The cost of fuel inventories includes gains or losses on the settlement of fuel swap contracts. All other inventories are accounted for using the weighted average cost method. The cost of inventories includes expenditures incurred in acquiring the inventories and other direct costs incurred in bringing them to their existing location and condition.

(j) Impairment of non-financial assets:

Non-financial assets with finite lives, including property, plant and equipment and intangible assets, are tested for impairment when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows that are largely independent of the cash flows from other assets or groups of assets (this can be at the asset or cash-generating unit level).

The impairment charged to net earnings or loss is the excess of the carrying value over the recoverable amount. The recoverable amount is the higher of an asset's fair value less cost to sell or its value in use.

Impairment losses are evaluated for potential reversals when events or changes warrant such consideration. An impairment is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined had no impairment been recognized. A reversal of impairment is charged to net earnings or loss.

(k) Asset retirement obligations:

In the period when it can be reasonably determined, the Group recognizes a liability at its fair value for any legal obligations associated with the retirement of long-lived assets when those obligations result from the acquisition, construction, development or normal operation of the assets. A corresponding asset retirement cost is added to the carrying amount of the related asset and amortized to expense on a systematic and rational basis.

It is possible that the Group's estimates of its ultimate asset retirement obligations could change as a result of changes in regulations, changes in the extent of environmental remediation required, changes in the means of reclamation or changes in cost estimates. Changes in estimates are accounted for prospectively from the period the estimate is revised.

The Group's long-lived assets include certain vessels which contain undetermined amounts of asbestos. The Group handles and disposes of the asbestos and other controlled materials in a manner required by regulations. Where possible the Group will sell decommissioned vessels into the secondary markets to a responsible buyer who will keep them in active service. Under these circumstances the condition of the vessel, including the presence of any controlled material such as asbestos, will be fully disclosed and remediation and any eventual retirement obligation would become the responsibility of the new owner.

No amount has been recorded for asset retirement obligations relating to these assets as it is not possible to make a reasonable estimate of the fair value of any such liability due to the indeterminate magnitude, likelihood or financial impact, if any, of this issue. In addition, there is a reasonable expectation that retired assets may be sold to a responsible secondary market at a nominal salvage price.

(l) Financial assets and liabilities:

Financial assets include cash and cash equivalents, trade and other receivables, restricted and other short-term investments, derivatives with a positive market value and loan receivables.

Financial liabilities include trade payables, long-term debt, interest on long-term debt and derivatives with a negative market value.

Financial assets that are expected to be realized within twelve months after the reporting period are presented as "current assets". Financial assets and liabilities of a long-term nature are presented as "non-current".

(i) Recognition and measurement of non-derivative financial instruments

Financial instruments are initially recognized at fair value. If the financial instrument is not classified at fair value through profit or loss, then the initial measurement includes directly attributable transaction costs.

Subsequent to initial recognition, financial assets are measured at either amortized cost or at fair value through OCI or at fair value through net earnings or loss.

Financial liabilities are measured at either amortized cost or at fair value through net earnings or loss.

Classification depends on the nature and objective of each financial instrument and is determined when first recognized.

(ii) Loans and advances

Loans and advances are initially recognized at fair value plus directly attributable transaction costs. Subsequently, loans and advances are measured at amortized cost using the effective interest rate method, less any recognized impairment loss. They are subject to recoverable value tests, carried out at each statement of financial position date and whenever there are objective indicators that the recoverable value of these assets would be lower than the carrying value.

(iii) *Trade and other receivables*

Trade and other receivables are recorded at fair value (in most cases the same as nominal value) less provision for impairment. A provision is established when there is reasonable expectation that the Group will not be able to collect all amounts due. Any increase in the provision is recognized in net earnings or loss. When a trade receivable is uncollectible, it is written off against the provision for impairment. Subsequent recoveries of amounts previously written off are credited in net earnings or loss. As receivables are due in less than one year, they are not discounted.

(iv) *Cash and cash equivalents*

Cash includes bank deposits, cash on hand and short-term deposits with an initial maturity of three months or less. Cash equivalents are short-term investments with a term of three months or less. Due to the nature and/or short-term maturity of these financial instruments, carrying value approximates fair value. The instruments held in this category can be liquidated or sold on short notice, and do not bear any significant risk of loss in value. Cash equivalents invested in pooled funds are recorded at fair value through net earnings or loss. All other cash equivalents are carried at amortized cost.

(v) *Borrowings and other financial liabilities*

Trade and other debts are initially recorded at fair value, which is generally the same as nominal value plus or minus any premiums or discounts. Bank borrowings and other financial liabilities are subsequently measured at amortized cost calculated using the effective interest rate method. Interest accrued on short-term borrowings is included in "accounts payable and accrued liabilities" on the statement of financial position. Cash flows linked to short-term payable amounts are not discounted. Long-term cash flows are discounted whenever the impact is significant. The Group derecognizes a financial liability when its contractual obligations are discharged, cancelled or expired.

(vi) *Derivatives*

The Group may use derivative financial instruments to hedge its exposure to fluctuations in fuel prices, interest rates and foreign currency exchange rates. The Group does not utilize derivatives for trading or speculative purposes. At the inception of each hedge, the Group determines whether it will or will not apply hedge accounting. Derivatives are initially recorded at fair value and any associated transaction costs are recognized in net earnings or loss when incurred. After initial recognition, derivatives are measured at fair value based on market prices at each statement of financial position date. Changes in the fair value of these instruments are recorded in net earnings or loss except where the instrument has been designated as a hedging item in a cash flow hedge. Instruments designated as a hedging item in a cash flow hedge are recorded in accordance with note 1(d).

(vii) *Fair value hierarchy*

In estimating fair value, the Group uses quoted market prices when available. Models incorporating observable market data along with transaction specific factors are also used in estimating fair value. Financial assets and liabilities are classified in the fair value hierarchy according to the lowest level of observability of inputs that are significant to the fair value measurement. Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect placement within the following fair value hierarchy levels:

- level 1 – quoted prices in active markets for identical assets or liabilities;
- level 2 – techniques (other than quoted prices included in level 1) that are observable for the asset or liability, either directly (as prices), or indirectly (as derived from prices); and
- level 3 – techniques which use inputs that are both significant to the overall fair value measurement of the asset or liability and are not based on observable market data (unobservable inputs).

(m) Provisions:

A provision is recognized when:

- the Group has a current obligation (legal or constructive) resulting from a past event;
- it is likely that an outflow of resources will be required to settle the obligation; and
- the amount of the obligation can be measured reliably.

Provisions are measured by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as a finance expense.

(n) Employee benefits:

The Group has a number of defined benefit pension and post-retirement plans. The plans are generally funded by payments from employees and by the Group, taking into account the recommendations of independent qualified actuaries.

The Group's multi-employer defined benefit pension and long-term disability plans are accounted for using defined contribution plan accounting. These plans are administered by external parties and the Group does not have sufficient information to apply defined benefit plan accounting. The cost of these benefits is expensed as contributions are made to the plans.

The actuarial determination of the accrued benefit obligations for retirement benefits uses the projected unit credit method prorated on service (which incorporates management's best estimate of future salary levels, other cost escalation, retirement ages of employees and other actuarial factors). Under the projected unit credit method, the cost of these benefits is expensed over the service lives of employees in accordance with the advice of qualified actuaries who carry out a full valuation of the plans on a regularly scheduled basis. The pension obligation is measured at the present value of estimated future cash outflows using interest rates based on the yield of long-term high quality corporate bonds with maturities matching the pension obligation.

Assets are valued at fair value for the purpose of calculating the expected return on plan assets.

Actuarial gains (losses) arise from the difference between the actual and expected long-term rate of return on plan assets and the effects of changes in actuarial assumptions used to determine the accrued benefit obligation. Actuarial gains (losses) are recognized immediately in OCI and are not reclassified to net earnings or loss in subsequent periods.

Past service costs arising from plan amendments are recognized immediately to the extent that the benefits are already vested. Where the benefits are not vested, the costs are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment. The obligation recorded for all benefit plans includes any past service costs still to be amortized.

When a plan amendment gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to the settlement.

(o) Debt transaction costs:

Legal and financing costs incurred for arranging long-term debt are capitalized. Once the debt is issued these costs are reclassified from deferred costs and recognized as an offset to the related long-term debt. These costs are subsequently amortized to net earnings or loss using the effective interest rate method.

(p) Revenues:

Revenue from vehicle fares, including reservation fees, passenger fares and fuel surcharges (rebates), is recognized when transportation is provided. Payments for fares sold in advance of providing transportation are included in the statement of financial position as deferred revenue. These advance payments include prepaid vehicle and passenger fares, assured loading tickets and reservation fees.

Ferry service fees and federal-provincial subsidies are recognized as revenue as services specified in the related agreements with the Province of British Columbia (the "Province") are performed.

Net retail revenue consists primarily of food services and gift shop sales less the cost of goods sold.

Parking revenues are received from both owned and subcontracted parking facilities and are recognized when service is provided. Revenue is generated from various advertising contracts and recognized according to the individual agreement.

(q) Taxes:

The Group is a "Tax Exempt Corporation" as described in the *Income Tax Act* and as such is exempt from federal and provincial income taxes.

The provision of vehicle and passenger ferry services is an exempt supply under the *Excise Tax Act* for HST/GST purposes.

2. ADOPTION OF NEW AND AMENDED STANDARDS:

(a) Changes in accounting policies:

No new or amended standards or interpretations to existing standards were applied by the Group during the year ended March 31, 2018.

(b) Future changes in accounting policies:

IFRS 15 Revenue from Contracts with Customers:

IFRS 15 *Revenue from Contracts with Customers* will replace IAS 11 *Construction Contracts* and IAS 18 *Revenue*. It provides a single, principles based five-step model to be applied to all contracts with customers. IFRS 15 also requires additional disclosures. The mandatory effective date of IFRS 15 is for annual reporting periods beginning on or after January 1, 2018, and must be applied using either a full retrospective application or a retrospective with cumulative effect application. The Group assessed the impact of the standard on accounting for the Group's revenue streams and consolidated financial statements. The Group's assessment regarding the timing of recognition of revenue is as follows:

- Revenue from vehicle fares, including reservation fees, and passenger fares, recognized at the time of travel, will not be affected by IFRS 15, except for timing of revenue from the sale of third party travel vouchers which is currently recognized when the retailer takes delivery of the tickets and formally accepts them. Under IFRS 15, the Group will recognize revenue from the sale of third party travel vouchers when transportation is provided;
- Revenue from ferry service fees and federal-provincial subsidies, recognized as contract services are provided, will not be affected by IFRS 15;
- Revenue from retail services, recognized at the time of sale, will not be affected by IFRS 15;
- Revenue from fuel surcharges or rebates, recognized at the time of travel, will not be affected by IFRS 15;
- Revenue from other sources of revenue, recognized when service is provided, will not be affected by IFRS 15. Presentation of parking revenue will be changed, reflecting guidance in IAS 1, *Presentation of Financial Statements*, to present gross parking revenue and contractor's costs separately in the statements of comprehensive income. This presentation change will have no net impact on the Group's consolidated financial statements.

IFRS 15 introduces a new concept of breakage. Breakage refers to a customer's unexercised, contractual rights to receive future goods or services, but for which the customer has made a non-refundable prepayment. Under IFRS 15, revenue is recognized from the expected breakage when the likelihood of the customer exercising their remaining rights becomes remote.

The Group has concluded that one of the prepaid stored value products the Group offers to its customers will be affected by IFRS 15. To March 31, 2018, the Group has not recognized revenue from the expected breakage relating to the prepaid stored value product.

The Group will apply IFRS 15 using the modified retrospective with cumulative effect method of adoption for the annual reporting period beginning on April 1, 2018. The Group does not expect the application of this standard to have a significant impact on its consolidated financial statements, other than additional disclosure.

IFRS 9 Financial Instruments (2014):

On July 24, 2014, the IASB issued the completed version of IFRS 9. IFRS 9 (2014) introduces a new expected credit loss model for calculating impairment, and incorporates the guidance on the classification and measurement of financial assets and the final general hedge accounting requirements originally published in IFRS 9 (2013). The Group adopted IFRS 9 (2013) in the year ended March 31, 2015. The mandatory effective date of IFRS 9 (2014) is for annual reporting periods beginning on or after January 1, 2018 and should be applied retrospectively, subject to certain exceptions. Restatement of prior periods is not required and is only permitted if it is possible without the use of hindsight. The Group has determined the need to establish an expected credit loss provision for trade receivables. The Group does not expect the application of IFRS 9 to have a significant impact on its consolidated financial statements, other than additional disclosure, as the Group has an existing provision for impairment.

IFRS 16 Leases:

On January 13, 2016, the IASB issued IFRS 16 *Leases*, which will replace IAS 17 *Leases*. The standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. The standard is effective for annual reporting periods beginning on or after January 1, 2019. Early adoption is permitted if IFRS 15 *Revenue from Contracts with Customers*, has also been applied. The Group intends to early adopt IFRS 16 for the annual reporting period beginning on April 1, 2018 and apply the following practical expedients on initial application:

- use of the modified retrospective approach with no restatement of prior periods;
- application only to contracts that were previously identified as leases;
- use of a single discount rate to a portfolio of leases; and
- electing to not recognize leases for which the underlying asset is of low value.

The Group will use the modified retrospective with cumulative effect method of adoption.

The application of IFRS 16 will not have any impact on the amounts recognized in its consolidated financial statements for finance leases where an asset and a related liability for the lease arrangement have been recognized or where the Group is a lessor.

The Group's assessment of non-cancellable operating lease commitments indicates that seven arrangements will meet the definition of a lease under IFRS 16, and therefore, at April 1, 2018, the Group will recognize a right-of-use asset and a corresponding liability in respect of these leases.

Amendments to IAS 19 Employee Benefits:

On February 7, 2018, the IASB published *Amendments to IAS 19 Employee Benefits*.

Entities are required to use the updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement. The amendments also clarify how the requirements for accounting for a plan amendment, curtailment or settlement affect the asset ceiling requirements. The amendments are effective for annual reporting periods beginning on or after January 1, 2019. Early application is permitted. The Group is reviewing the amendments to determine the potential impact, if any, on its consolidated financial statements. The Group does not expect the application of these amendments to have a significant impact on its consolidated financial statements.

3. CASH AND CASH EQUIVALENTS:

As at March 31	2018	2017
Cash	69,443	66,093
Cash equivalents:		
Investments valued at fair value through net earnings	470	44
Investments valued at amortized cost	–	5,895
Total	69,913	72,032

4. INVENTORIES:

As at March 31	2018	2017
Consumable parts and supplies	23,665	20,598
Provision for obsolescence	(1,400)	(1,000)
Net consumable parts and supplies	22,265	19,598
Retail inventories	4,813	5,292
Fuel inventories	4,506	3,367
Total	31,584	28,257

5. LONG-TERM LAND LEASE:

On April 1, 2003, the Group's land and structures comprising its terminals were transferred by the Group to the BC Transportation Financing Authority ("BCTFA"), a British Columbia Crown Corporation and related party at the time of the transaction. In exchange, the Group received recognition of a prepayment for leases of the transferred terminal structures and land. The structures, having lives of less than the lease term, are considered a capital lease and as such have been capitalized and included with capital assets and are depreciated in accordance with the Group's depreciation policy.

The land, having an indefinite useful life, is considered an operating lease. The prepayment of the land lease has been deferred and will be amortized on a straight-line basis over eighty years, being the initial sixty year lease period plus an additional twenty year bargain renewal option. The transaction was initially recorded at the carrying values of the transferred terminal structures and land.

Since April 1, 2003, the Group has entered into various agreements with BCTFA to add lands to the existing terminal leases. During the years ended March 31, 2018 and March 31, 2017, no new land costs were added to the terminal leases.

6. PROPERTY, PLANT AND EQUIPMENT:

	VESSELS	BERTHS, BUILDINGS AND EQUIPMENT UNDER FINANCE LEASE	BERTHS, BUILDINGS AND EQUIPMENT	LAND UNDER FINANCE LEASE*	LAND*	CONSTRUCTION IN PROGRESS	TOTAL
Cost:							
Balance as at April 1, 2016	1,280,303	625,948	94,115	5,883	15,655	105,209	2,127,113
Additions	–	–	–	–	–	217,325	217,325
Revaluation	–	–	–	941	2,778	–	3,719
Disposals	(28,214)	(442)	(414)	–	–	–	(29,070)
Reclassification to:							
assets held for sale	(28,750)	–	–	–	–	–	(28,750)
Transfers from construction							
in progress	82,506	16,930	10,631	–	–	(110,067)	–
Balance as at March 31, 2017	1,305,845	642,436	104,332	6,824	18,433	212,467	2,290,337
Additions	–	–	–	–	–	236,463	236,463
Revaluation	–	–	–	353	1,503	–	1,856
Disposals	(20,982)	(2,097)	(1,113)	–	–	(628)	(24,820)
Transfers from construction							
in progress	229,935	42,488	12,329	–	–	(284,752)	–
Balance as at March 31, 2018	1,514,798	682,827	115,548	7,177	19,936	163,550	2,503,836
Accumulated depreciation:							
Balance as at April 1, 2016	422,867	122,483	41,806	–	–	–	587,156
Depreciation	101,551	27,917	9,708	–	–	–	139,176
Disposals	(28,214)	(442)	(391)	–	–	–	(29,047)
Reclassification to: assets							
held for sale	(28,750)	–	–	–	–	–	(28,750)
Balance as at March 31, 2017	467,454	149,958	51,123	–	–	–	668,535
Depreciation	106,517	29,359	10,480	–	–	–	146,356
Disposals	(20,981)	(2,065)	(1,089)	–	–	–	(24,135)
Balance as at March 31, 2018	552,990	177,252	60,514	–	–	–	790,756
Net carrying value:							
As at April 1, 2016	857,436	503,465	52,309	5,883	15,655	105,209	1,539,957
As at March 31, 2017	838,391	492,478	53,209	6,824	18,433	212,467	1,621,802
As at March 31, 2018	961,808	505,575	55,034	7,177	19,936	163,550	1,713,080

* Land under finance lease and land are measured at fair value.

Other disclosures – property, plant and equipment:

During the year ended March 31, 2018, financing costs capitalized during construction amounted to \$5.5 million (March 31, 2017: \$4.4 million) with an average capitalization rate of 5.03% (March 31, 2017: 5.02%).

Contractual commitments as at March 31, 2018, for assets to be constructed totalled \$122.0 million (March 31, 2017: \$186.7 million). These contractual commitments include \$45.5 million (March 31, 2017: \$103.7 million) of the total contract value of \$149.9 million for the mid-life upgrade and conversion to dual fuel of the two Spirit class vessels and \$54.2 million (March 31, 2017: \$nil) of the total contract value of \$60.0 million for the construction of two minor class vessels.

During the year ended March 31, 2018, the Group recorded asset impairment of \$0.6 million (March 31, 2017: \$nil). The impairment loss is reported under "Loss on disposal and revaluation of property, plant and equipment and intangible assets" in the consolidated statements of comprehensive income.

The Government of Canada, through the New Building Canada Fund, agreed to provide funding of up to \$43.4 million to help offset the costs of the newly established route connecting Port Hardy and Bella Coola and the replacement of two minor vessels. During the year ended March 31, 2018, the Group recorded \$14.9 million as a reduction of the cost of property, plant and equipment. No funding was recorded in fiscal 2017.

During the year ended March 31, 2018, the Group received \$1.1 million (March 31, 2017: \$1.1 million) of rental income earned from buildings held for leasing purposes. These buildings have a cost and accumulated depreciation of \$11.9 million and \$3.1 million, respectively, as at March 31, 2018.

During the year ended March 31, 2018, the *Queen of Nanaimo* was decommissioned and sold. The *Queen of Burnaby* (decommissioned during the year ended March 31, 2018) is classified as held for sale and has no carrying value.

7. INTANGIBLE ASSETS:

	ACQUIRED SOFTWARE, LICENSES & RIGHTS	INTERNALLY DEVELOPED SOFTWARE & WEBSITE	ASSETS UNDER DEVELOPMENT	TOTAL
Cost:				
Balance as at April 1, 2016	36,700	12,448	67,397	116,545
Additions	–	–	26,363	26,363
Disposals	(34)	–	(1,655)	(1,689)
Transfers from assets under development	66,583	876	(67,459)	–
Balance as at March 31, 2017	103,249	13,324	24,646	141,219
Additions	–	–	15,892	15,892
Disposals	(2)	(57)	(203)	(262)
Transfers from assets under development	21,472	3,151	(24,623)	–
Balance as at March 31, 2018	124,719	16,418	15,712	156,849
Accumulated amortization:				
Balance as at April 1, 2016	22,746	11,058	–	33,804
Amortization	9,183	593	–	9,776
Disposals	(34)	–	–	(34)
Balance as at March 31, 2017	31,895	11,651	–	43,546
Amortization	12,851	709	–	13,560
Disposals	(2)	(57)	–	(59)
Balance as at March 31, 2018	44,744	12,303	–	57,047
Net carrying value:				
As at April 1, 2016	13,954	1,390	67,397	82,741
As at March 31, 2017	71,354	1,673	24,646	97,673
As at March 31, 2018	79,975	4,115	15,712	99,802

Other disclosures – intangible assets:

During the year ended March 31, 2018, the Group recorded asset impairment of \$0.2 million (March 31, 2017: \$1.6 million). The impairment loss is reported under “Loss on disposal and revaluation of property, plant and equipment and intangible assets” in the consolidated statements of comprehensive income.

Capitalized financing costs during construction for intangible assets for the year ended March 31, 2018 totalled \$1.0 million (March 31, 2017: \$2.3 million).

During the year ended March 31, 2018, intangible assets totalling \$8.9 million (March 31, 2017: \$20.8 million) were acquired and \$7.0 million (March 31, 2017: \$5.6 million) were internally developed.

8. LIABILITIES ARISING FROM FINANCING ACTIVITIES:**Continuity of liabilities arising from financing activities:**

	LONG-TERM DEBT		OBLIGATIONS UNDER FINANCE LEASE		INTEREST PAYABLE ON LONG-TERM DEBT	
	2018	2017	2018	2017	2018	2017
Balance as at April 1						
Current	30,939	23,851	1,582	1,514	18,458	18,262
Non-current	1,273,860	1,218,255	40,423	42,003	–	–
	1,304,799	1,242,106	42,005	43,517	18,458	18,262
Additions	45,264	90,122	–	–	63,591	62,300
Payments	(35,312)	(24,934)	(1,584)	(1,512)	(63,512)	(62,104)
Additions to debt issue costs	(1,417)	(2,965)	–	–	–	–
Amortization of debt issue costs	1,035	470	–	–	–	–
Balance as at March 31	1,314,369	1,304,799	40,421	42,005	18,537	18,458
Current	34,594	30,939	1,652	1,582	18,537	18,458
Non-current	1,279,775	1,273,860	38,769	40,423	–	–
Balance as at March 31	1,314,369	1,304,799	40,421	42,005	18,537	18,458

9. PROVISIONS:

	WAGES PAYABLE	CLAIMS PAYABLE	TOTAL
Balance as at April 1, 2016	47,082	1,608	48,690
Provisions arising during the year	57,883	433	58,316
Provisions settled during the year	(50,845)	(450)	(51,295)
Balance as at March 31, 2017	54,120	1,591	55,711
Provisions arising during the year	60,234	1,179	61,413
Provisions settled during the year	(55,603)	(1,149)	(56,752)
Balance as at March 31, 2018	58,751	1,621	60,372

Wages payable consists of contractual liabilities to employees for deferred or accrued compensation. Liabilities for deferred compensation amounts are generally settled either through payment or provision of paid time off.

Claims payable represents reserves for settlement amounts payable to third parties for injuries or damage to persons or property.

10. LOANS:

Long-term debt: As at March 31	2018	2017
6.25% Senior Secured Bonds, Series 04-4, due October 2034 (effective interest rate of 6.41%)	250,000	250,000
5.02% Senior Secured Bonds, Series 07-1, due March 2037 (effective interest rate of 5.06%)	250,000	250,000
5.58% Senior Secured Bonds, Series 08-1, due January 2038 (effective interest rate of 5.62%)	200,000	200,000
4.70% Senior Secured Bonds, Series 13-1, due October 2043 (effective interest rate of 4.75%)	200,000	200,000
4.29% Senior Secured Bonds, Series 14-1, due April 2044 (effective interest rate of 4.45%)	200,000	200,000
12 Year Loan, maturing March 2020 Tranche A (effective interest rate of 5.17%)	15,000	22,500
Tranche B (floating interest rate of 2.00% at March 31, 2018)	22,500	22,500
12 Year Loan, maturing June 2020 Tranche A (effective interest rate of 5.18%)	16,875	24,375
Tranche B (floating interest rate of 2.02% at March 31, 2018)	22,500	22,500
2.95% Loan, maturing January 2021 (effective interest rate of 3.08%)	27,000	36,000
2.09% Loan, maturing October 2028 (effective interest rate of 2.70%)	40,175	43,923
2.09% Loan, maturing January 2029 (effective interest rate of 2.68%)	41,482	45,264
2.09% Loan, maturing January 2029 (effective interest rate of 2.70%)	41,482	–
	1,327,014	1,317,062
Less: Unamortized deferred financing costs and bond discounts	(12,645)	(12,263)
Total	1,314,369	1,304,799
Current portion	34,594	30,939
Non-current portion	1,279,775	1,273,860
Total	1,314,369	1,304,799

In May 2004, the Group entered into a master trust indenture which established common security and a set of common covenants for the benefit of all lenders under the Group's financing plan. The financing plan encompasses an ongoing program capable of accommodating a variety of corporate debt instruments and borrowings, ranking *pari passu*.

The Group has five outstanding series of obligation bonds and a credit facility agreement secured by pledged bonds. In addition, the Group has two 12-year loan agreements, a 2.95% loan agreement and three 2.09% loans outstanding with KfW IPEX-Bank GmbH ("KfW").

(a) Bonds:

Bonds are issued under supplemental indentures either as obligation bonds or as pledged bonds. The bonds are secured by a registered first mortgage and charge over vessels, an unregistered first mortgage and charge over ferry terminal leases, and by a general security agreement on property and contracts. The bonds are redeemable in whole or in part at the option of the Group. The following table shows the semi-annual interest payment dates for the obligation bonds each year through to maturity.

BONDS	INTEREST PAYMENT DATES	
Series 04-4	April 13	October 13
Series 07-1	March 20	September 20
Series 08-1	January 11	July 11
Series 13-1	April 23	October 23
Series 14-1	April 28	October 28

(b) 12 Year Loans, maturing March and June 2020:

Proceeds of \$90.0 million were received in each of February and May 2008 to coincide with conditional acceptance of the *Coastal Inspiration* and the *Coastal Celebration* and applied toward the purchase of the vessels. Quarterly payments are due in March, June, September and December each year of the term of the loans.

The principal payments on these loans were deferred for three years to a second tranche (Tranche B) until June 2014 in accordance with amendments made to the two loan agreements in September 2011. The Tranche B principal is due on maturity, with floating-rate interest paid in periods ranging from one to six months at the option of the Group. The interest rates on Tranche B can be reset at the beginning of each interest period at rates based on the prevailing CDOR rate plus 30 bps. As of June 2014, the Tranche B balance for each loan reached a maximum of \$22.5 million and regular principal payments resumed on Tranche A.

(c) 2.95% Loan, maturing January 2021:

Proceeds of \$108.0 million from the loan were received in January 2009 to coincide with conditional acceptance of the *Northern Expedition* and applied toward the purchase of the vessel. Equal semi-annual principal payments plus interest are due in January and July each year of the 12 year term of the loan.

(d) 2.09% Loans, maturing October 2028 and January 2029:

The Group has a loan agreement with KfW, a German export credit bank. This loan agreement is secured under the Master Trust Indenture ("MTI") and allows for three loans of up to \$45.3 million each.

Proceeds of \$44.9 million from the first loan and \$45.3 million from the second loan were received during the year ended March 31, 2017, to coincide with the contract payment schedule for the *Salish Orca* and *Salish Eagle*, respectively, and applied toward the purchase of the vessels.

Proceeds of \$45.3 million from the third and final loan were received during the year ended March 31, 2018, to coincide with the contract payment schedule for the *Salish Raven*, and applied toward the purchase of the vessel.

Each of these loans are payable over a 12-year term at an interest rate of 2.09% per annum. Quarterly principal payments plus interest are due in January, April, July and October each year of the term of the loans.

(e) Credit facility:

The Group has a credit facility with a syndicate of Canadian banks, secured by pledged bonds. This revolving facility, in the amount of \$155.0 million, was renewed on March 19, 2018 to extend the maturity date to April 20, 2023. There were no draws on this credit facility as at March 31, 2018 and as at March 31, 2017. There was no interest expensed during the years ended March 31, 2018 and March 31, 2017. Letters of credit outstanding against this facility as at March 31, 2018 totalled \$0.1 million (March 31, 2017: \$0.1 million).

(f) Debt service reserves:

Long-term debt agreements require the Group to maintain debt service reserves equal to a minimum of six months of interest payments, to be increased under certain conditions. As at March 31, 2018, debt service reserves of \$32.3 million (March 31, 2017: \$32.4 million) were held in short-term investments and have been classified as restricted short-term investments on the statements of financial position.

(g) Debt service coverage:

Debt service coverage (earnings before interest, taxes, depreciation, amortization and rent) is required to be at least 1.25 times the debt service cost under the credit facility agreement. As at March 31, 2018, the debt service coverage ratio was 2.79.

In addition, there are other covenants contained in the MTI (May 2004) available at www.SEDAR.com. The Group was in compliance with all of its covenants at March 31, 2018 and at March 31, 2017.

11. ACCRUED EMPLOYEE FUTURE BENEFITS:**(a) Description of benefit plans:**

	FUNDING STATUS	ADMINISTRATOR	PLAN TYPE	BASIS OF ACCOUNTING
Public Service Pension	funded	Third Party	Multi-employer defined benefit	Defined contribution
Long-term disability	funded	Third Party	Multi-employer defined benefit	Defined contribution
Retirement benefit	unfunded	Group	Defined benefit	Defined benefit
Death benefit	unfunded	Group	Defined benefit	Defined benefit
Sick Bank obligation	unfunded	Group	Defined benefit	Defined benefit
Supplemental executive retirement plan	unfunded	Group	Defined benefit	Defined benefit
WCB obligation	unfunded	Third Party	Defined benefit	Defined benefit

The Group and its employees contribute to the Public Service Pension Plan (the "Plan"). The Pension Corporation of the Province of British Columbia administers the Plan, including the payment of retirement and post-employment benefits on behalf of employers. The Plan is a multi-employer defined benefit pension plan. Under joint trusteeship, which became effective January 1, 2001, the risk and reward associated with the Plan's unfunded liability or surplus is shared between the employers and the plan members and will be reflected in their future contributions.

A funded long-term disability multi-employer plan provides disability income benefits after employment, but before retirement. Sufficient information is not available for either multi-employer defined benefit plan to be accounted for as a defined benefit plan.

In addition, eligible employees are entitled to other retirement and future benefits as provided for under the collective agreement and terms of employment. These are unfunded defined benefit plans administered by the Group. Retirement benefits and death benefits are based on years of service and final average salary. The accumulated sick leave bank ("Sick Bank obligation") consists of unused sick time credits earned prior to the discontinuation of the sick leave accumulation benefit in 1979. Accumulated sick leave may be drawn down at 100% or paid out at 50%. Benefits are paid out at current salary rates. No new credits are accumulated to this bank.

The Group also administers an unfunded supplemental executive retirement plan which encourages continued retention and provides additional pension compensation.

The Group's employees may also receive compensation benefits arising from claims prior to March 31, 2003, administered by the Workers' Compensation Board ("WCB obligation"). Prior to March 31, 2003, the Group participated in the Workers' Compensation Board deposit class coverage system. Subsequent to March 31, 2003, the Group has been covered under the Workers' Compensation Board rate system. The change to the rate system resulted in a residual liability from the deposit class system that has been valued by actuarial assumptions as appropriate for a closed plan. This obligation is unfunded.

(b) Total cash payments:

Total cash payments for employee future benefits for the year ended March 31, 2018, consisting of cash contributed by the Group to its multi-employer defined benefit plans, cash payments directly to beneficiaries for its unfunded other benefit plans, and cash contributed to a third party administrator of an unfunded plan, was \$32.6 million (March 31, 2017: \$29.6 million).

(c) Multi-employer plans:

The total cost recognized for the Group's multi-employer plans is as follows:

	2018	2017
Public Service Pension Plan contributions (i)	25,814	24,222
Long-term disability plan contributions (ii)	4,269	3,043
Total	30,083	27,265

- (i) The March 31, 2017 actuarial valuation report for the Public Service Pension Plan was received by the Public Service Pension Board of Trustees ("the Board") on December 4, 2017. This report indicated that the pension fund has an actuarial surplus of \$1,896 million. Under the terms of the plan's joint trust agreement, plan members and employers share in any increase or decrease in contribution rates.

On March 16, 2018, the Board announced plan changes which will take effect April 1, 2018 for pensionable service earned on or after that date. The changes include contribution at a flat 8.35% of salary for members and 9.85% of salary for employer from member and employer contribution rates that were dependent on how much the salary was below and above the year's maximum pensionable earnings. The Board has also decided to use a portion of the surplus funds to improve the pension benefits for pensionable service accrued between April 1, 2006 and March 31, 2018. The next valuation, expected to be received during the fiscal year ending March 31, 2021, will be as at March 31, 2020.

- (ii) Contribution rates for the long-term disability plan are actuarially determined every year as a percentage of covered payroll. The funding policy for this plan calls for amortization of individual participating employer deficits and surpluses over 5 years and a 110% funding target for each participant in 5 years. As a result the employer contribution rate was reduced from 2.12% to 1.91% of covered payroll effective April 1, 2018. The most recent valuation, as at September 30, 2017, determined an overall fund surplus. The next scheduled valuation, expected to be received during the fiscal year ended March 31, 2019, will be as at March 31, 2018.

(d) Other defined benefit plans:

All of the Group's defined benefit plans, except its multi-employer plans, are currently unfunded. The most recent actuarial valuation of the retirement and death benefit plans is as at March 31, 2017. A plan amendment at December 31, 2007 restricts exempt employees from joining the retirement and death benefit plans. As part of an implementation plan to assist with the transition of certain shipboard management to excluded positions, a further plan amendment was made during the year ended March 31, 2011. This amendment allows bargaining unit employees transferring to excluded positions to continue to be eligible for the retirement benefit, provided the transfer happened on or before December 31, 2013. The most recent actuarial valuation of the WCB obligation was at March 31, 2016.

During the year ended March 31, 2018, a net loss of \$1.9 million was recognized in OCI to reflect the actuarial valuation of the liability as at March 31, 2017, for the retirement and death benefit plans.

	OTHER BENEFIT PLANS	
	2018	2017
Accrued benefit obligations		
Balance, beginning of year	22,313	21,261
Current service cost	1,473	1,209
Interest cost	1,044	984
Benefits paid	(2,474)	(2,381)
Actuarial loss (note 20(a))	1,943	1,240
Balance, end of year	24,299	22,313

	OTHER BENEFIT PLANS	
	2018	2017
Reconciliation of funded status of the benefit plans to the amounts recorded in the financial statements		
Fair value of plan assets	–	–
Accrued benefit obligation	24,299	22,313
Funded status of plans – deficit	(24,299)	(22,313)
Accrued benefit liability	(24,299)	(22,313)
Current portion of accrued employee future benefits	3,000	1,400
Accrued non-current employee future benefits	(21,299)	(20,913)

	OTHER BENEFIT PLANS	
	2018	2017
Elements of defined benefit costs recognized in the year		
Current service cost	1,473	1,209
Interest cost	1,044	984
Defined benefit costs recognized	2,517	2,193

Significant assumptions:

The significant assumptions used are as follows (weighted average):

	2018	2017
Accrued benefit obligation as at March 31 and benefit cost for the years ended March 31:		
Discount rate	5.0%	5.0%
Rate of compensation increase	1.8%	0.9%
Annual employee retention rate	93.7%	96.0%
Employees with eligible dependents at pre-retirement death	43.0%	43.0%
Average remaining service period of active employees (years)	9.65	9.61

12. OBLIGATIONS UNDER FINANCE LEASE:

During the year ended March 31, 2011, agreements which constitute a finance lease for space in a downtown Victoria, BC office building took effect following the completion of construction of the building. The initial term of the building lease is for fifteen years, with four renewal options of five years each. The lease agreement includes payment of building operating costs and property taxes based on the Group's proportion of total rentable area.

Loan and purchase option:

The Group has advanced funds to, and has a loan receivable from, the developer of the office property in the amount at \$24.5 million. The term of the loan is fifteen years, secured by a second mortgage on the property. The loan agreement provides for interest equal to one-half of the net cash flow from the property, subject to minimum and maximum percentage rates of interest. Over the term of the loan, interest is expected to approximate the market rate when the loan was made. Incidental to the loan, the Group was granted an option to purchase up to 50% of the owner's equity interest in the building. The purchase option expires at the end of the loan term.

Future minimum lease payments and obligations under the head office and other finance leases are as follows:

	MINIMUM LEASE PAYMENTS	EXECUTORY COSTS	IMPUTED INTEREST (4.45%)	OBLIGATION
Less than one year	5,243	1,861	1,730	1,652
Between one and five years	22,054	7,823	6,111	8,120
Later than five years	14,916	5,759	3,023	6,134
Purchase option	24,515	–	–	24,515
Total	66,728	15,443	10,864	40,421
Current portion				(1,652)
Non-current portion				38,769

13. OTHER LIABILITIES:

FortisBC Energy Inc. has committed to provide the Group with funding as part of the Natural Gas for Transportation ("NGT") incentive funding.

During the year ended March 31, 2018, the Group received \$1.8 million of the total contribution of \$10.0 million to be applied towards the mid-life upgrade, including conversion to natural gas ("NG"), of the two Spirit class vessels.

During the year ended March 31, 2018, the Group recorded the remaining \$0.7 million of the total contribution of \$6.0 million as trade receivables to be applied towards the purchase of the three new Salish class vessels. The Group expects to receive this amount during the year ending March 31, 2019.

The contributions are dependent upon the purchase of NG and will be used to offset the incremental capital costs of the vessels.

NGT incentive funding as at March 31, 2018:

	SALISH CLASS	SPIRIT CLASS	TOTAL
Balance as at March 31, 2017	5,250	–	5,250
Additions	750	1,750	2,500
Balance as at March 31, 2018	6,000	1,750	7,750

14. FINANCIAL INSTRUMENTS:

The carrying values of the Group's financial instruments approximate fair value as at March 31, 2018 and March 31, 2017 for all financial instruments except for long-term debt:

As at March 31	2018		2017	
	CARRYING VALUE	APPROX FAIR VALUE	CARRYING VALUE	APPROX FAIR VALUE
Long-term debt, including current portion ¹	1,314,369	1,614,108	1,304,799	1,597,761

1. Classified in Level 2 as the significant measurement inputs used in the valuation models are indirectly observable in active markets (derived from prices).

Carrying value is measured at amortized cost using the effective interest rate method. Fair value is calculated by discounting the future cash flows of each debt issue at the estimated yield to maturity for the same or similar issues at the date of the statements of financial position, or by using available quoted market prices.

The following items shown in the consolidated statements of financial position as at March 31, 2018 and March 31, 2017 are carried at fair value on a recurring basis using Level 1 or 2 inputs. There were no financial assets and liabilities at March 31, 2018 or at March 31, 2017, valued using Level 3 inputs.

As at March 31	2018		2017	
	LEVEL 1	LEVEL 2	LEVEL 1	LEVEL 2
Asset (liability):				
Cash ¹	69,443	–	66,093	–
Cash equivalents ¹	470	–	44	–
Derivatives ²	–	12,530	–	556
	69,913	12,530	66,137	556

1 Classified in Level 1 as the measurement inputs are derived from observable, unadjusted quoted prices in active markets for identical assets.

2 Classified in Level 2 as the significant measurement inputs used in the valuation models are indirectly observable in active markets (derived from prices).

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates cannot be determined with precision as they are subjective in nature and involve uncertainties and matters of judgment. Where market prices are not available, fair values are estimated using discounted cash flow analysis. No amounts have been reclassified into or out of fair value classifications in the year ended March 31, 2018.

During the year ended March 31, 2018, gains or losses related to Level 2 derivatives have been recorded in OCI. There were no Level 3 instruments outstanding during the period.

The Group may use derivative instruments to hedge its exposure to fluctuations in fuel prices, interest rates and foreign currency exchange rates. The fair value of commodity derivatives reflects only the value of the commodity derivatives and not the offsetting change in value of the underlying future purchase of fuel. These fair values reflect the estimated amounts that the Group would receive or pay should the derivative contracts be terminated at the period end dates.

15. FINANCIAL RISK MANAGEMENT:

Exposure to credit risk, liquidity risk and market risk arises in the normal course of the Group's business.

The source of risk exposure and how each is managed is outlined below.

(a) Credit risk:

Credit risk is the risk that a third party to a financial instrument might fail to meet its obligations under the terms of the financial instrument. For cash and cash equivalents, short-term investments, derivative assets and trade and other receivables, the Group's credit risk is limited to the carrying value on the statement of financial position. Management does not believe that the Group is subject to any significant concentration of credit risk.

The Group limits its exposure to credit risk on cash and cash equivalents and investments by investing in liquid securities with high credit quality counterparties, placing limits on tenor of investment instruments and instituting maximum investment values per counter party. The Group undertakes to invest in instruments that are issued, insured or guaranteed by the Government of Canada or a provincial government or a deposit insurance corporation established by or on behalf of the Government of Canada or the Province; pooled funds comprised of investments issued, insured or guaranteed by any level of government in Canada; or issued by corporate short term issues of debt with a rating of no less than R-1 (Mid) by DBRS or equivalent, or in pooled funds of such investments.

Accounts receivable by source are as follows:

As at March 31	2018		2017	
	\$	%	\$	%
Trade customers and miscellaneous	16,926	64.5%	11,958	78.1%
Federal and Provincial governments	9,332	35.5%	3,361	21.9%
Total	26,258	100.0%	15,319	100.0%

Accounts receivable from trade customers are primarily due from commercial customers and transportation operators. Credit risk is reduced by a large and diversified customer base and is managed through the review of third party credit reports on customers both before extending credit and during the business relationship.

The Group manages its exposure to credit risk associated with all customers through the monitoring of aging of receivables, by collecting deposits from and adjusting credit terms for higher risk customers and customers who are not on a pre-authorized payment plan. Amounts due from tickets sold to passengers through the use of major credit cards are settled shortly after sale and are classified as cash and cash equivalents on the statements of financial position.

Accounts receivable from trade customers are generally due in 30 days. As at March 31, 2018, 96% of trade receivables are current. As at March 31, 2018, the provision for impairment was \$0.1 million (March 31, 2017: \$0.1 million) and reflects management's estimate of uncollectible receivables from trade customers based on past experience and analysis of customer accounts.

Amounts due from the Government of Canada and the Province are considered low credit risk.

The Group is exposed to credit risk in the event that a counterparty to an investment contract or a derivative contract defaults on its obligation. The Group manages credit risk by entering into contracts with high credit quality counterparties, in accordance with established investment parameters, and by an ongoing review of its exposure to counterparties. Counterparty credit rating and exposures are monitored by management on an ongoing basis, and are subject to approved credit limits. The counterparties with which the Group has significant derivative transactions must be rated A or higher. The Group does not expect any counterparties to default on their obligations.

(b) Liquidity risk:

Liquidity risk is the risk that an entity will not be able to meet its obligations associated with its financial liabilities. The Group's financial position could be adversely affected if it fails to arrange sufficient and cost effective financing to fund, among other things, capital expenditures and the repayment of maturing debt. The ability to arrange sufficient and cost effective financing is subject to numerous factors, including the results of operations and financial position of the Group, conditions in the capital and bank credit markets, ratings assigned by rating agencies and general economic conditions.

The Group manages liquidity risk through daily monitoring of cash balances, the use of long-term forecasting models, maintaining access to a credit facility and the maintenance of debt service reserves (note 10). The Group targets a strong investment grade credit rating to maintain capital market access at reasonable interest rates.

As at March 31, 2018 the Group's credit ratings were as follows:

	DBRS	STANDARD & POOR'S
British Columbia Ferry Services Inc.:	A (high)(stable)	AA- (positive)
Senior secured long-term debt	(March 31, 2017: A (positive))	(March 31, 2017: AA- (stable))

The following is an analysis of the contractual maturities of the Group's financial liabilities as at March 31, 2018:

FINANCIAL LIABILITIES	< 1 YEAR	2-3 YEARS	4-5 YEARS	> 5 YEARS	TOTAL
Accounts payable and accrued liabilities	77,233	–	–	–	77,233
Interest payable on long-term debt	18,537	–	–	–	18,537
Provisions (note 9)	60,372	–	–	–	60,372
Obligations under finance lease, including current portion	1,652	3,671	4,449	30,649	40,421
Long-term debt, including current portion (excluding deferred costs) ¹	35,282	102,439	22,564	1,166,729	1,327,014
Other liabilities	900	2,450	1,200	3,200	7,750
Total financial liabilities – principal only	193,976	108,560	28,213	1,200,578	1,531,327
Interest payable – long-term debt ²	61,855	120,149	117,967	906,769	1,206,740
Interest payable – obligations under finance lease	1,730	3,234	2,877	3,023	10,864
Total financial liabilities, including interest payable	257,561	231,943	149,057	2,110,370	2,748,931

¹ Carrying value at March 31, 2018, excludes unamortized deferred financing costs of \$12.6 million. The majority of the Group's long-term debt relates to funds used for acquisition of property, plant and equipment.

² Interest payable on long-term debt excludes the variable rate interest payable on Tranche B of the 12 Year loans (note 10(b)).

(c) Market risk:

Market risk is the risk that the fair value of future cash flows of financial instruments will fluctuate due to changes in market interest rates, foreign currency prices or fuel prices.

The Group manages market risk arising from the exposure to volatility in foreign currency, interest rates and fuel prices in part through the use of derivative financial instruments including forward contracts and swaps. The Group does not utilize derivative financial instruments for trading or speculative purposes. At the inception of each hedge the Group determines whether it will or will not apply hedge accounting.

Interest rate risk:

The Group is exposed to interest rate risk associated with short-term borrowings, floating rate debt and the pricing of future issues of long-term debt. As at March 31, 2018, the Group's cash equivalents and short-term investments include fixed rate instruments with maturities of 182 days or less. Accordingly, the Group has exposure to interest rate movement that occurs beyond the term of the maturity of the fixed rate investments. The Group's credit facility and the second tranche of each of the two 12 year loans are at variable rates and are subject to interest rate risk.

To manage this risk, the Group maintains between 70% and 100% of its debt portfolio in fixed rate debt, in aggregate. As at March 31, 2018, the Group had approximately 3.3% of total debt in variable rate instruments. A 50 basis point change in interest rates would have had an effect of less than \$0.2 million on net earnings for the year ended March 31, 2018.

Foreign currency price risk:

The Group is exposed to risk from foreign currency prices on financial instruments, such as accounts payable and future purchase commitments denominated in currencies other than the Canadian dollar. To manage exposure on future purchase commitments, the Group reviews foreign currency denominated commitments and enters into derivative instruments as necessary. As at March 31, 2018, the notional amount of the Group's foreign currency forward contracts was \$1.7 million (March 31, 2017: \$0.9 million). A 10% change in foreign exchange rates would have had an effect of approximately \$0.2 million on net earnings for the year ended March 31, 2018.

Fuel price risk:

The Group is exposed to risks associated with changes in the market price of marine diesel fuel and natural gas fuel. In order to reduce price volatility and add a fixed component to the inherent floating nature of fuel prices, the Group may manage its exposure by entering into hedging instruments with certain financial intermediaries. Fuel price hedging instruments are used to reduce fuel price risk and to minimize fuel surcharges, not for generating trading profits. Gains and losses resulting from fuel forward contracts are recognized as a component of fuel costs. The Group's Financial Risk Management Policy limits hedging, to a maximum of 95% of anticipated monthly fuel consumption for the immediately following 12 month period; 90% of anticipated monthly fuel consumption for the 12 month period thereafter to the end of the fourth performance term.

The Group is also allowed by regulatory order to use deferred fuel cost accounts to mitigate the impact of changes in fuel price on its earnings (note 27).

During the year ended March 31, 2018, the Group entered into ultra-low sulfur diesel ("ULSD") fuel swap contracts with a notional value of \$29.2 million CAD (March 31, 2017: \$33.7 million). To reduce its exposure to changes in the ULSD and foreign exchange risk components associated with forecast diesel fuel purchases, the Group hedges using CAD denominated ULSD swaps. The notional value of all fuel swap contracts outstanding as at March 31, 2018 was \$54.6 million CAD (March 31, 2017: \$66.7 million CAD). Hedge accounting was applied to these contracts. No NG swap contracts were entered into during the year ended March 31, 2018.

An economic relationship exists between the hedged item and the hedging instrument as the fair values of both the hedged item and hedging instrument move in opposite directions in response to the same risk. The inclusion of credit risk in the fair value of the hedging instrument which is not replicated in the hedged item is a potential source of ineffectiveness, however, the Group does not consider this risk to be material.

During the year ended March 31, 2018, the total change in the value of fuel swap contracts was \$11.9 million (March 31, 2017: \$18.4 million). The realized fair value change of \$13.6 million was recognized in OCI. The net realized hedging gain of \$1.7 million was reclassified from reserves and included in the Group's fuel expense during the year ended March 31, 2018. There was no hedge ineffectiveness for the year ended March 31, 2018.

	FISCAL 2019	FISCAL 2020	TOTAL
Cash flow hedges:			
Fuel price risk:			
Fuel contracts (litres in thousands)	68,800	30,180	98,980
Contract price range (\$/litre)	\$0.5247 - \$0.5680	\$0.5308 - \$0.5599	

- (i) As at March 31, 2018, the Group's derivative assets of \$12.5 million, of which \$9.0 million will mature within twelve months, included foreign exchange forward contracts and fuel swap contracts.

Fuel swap contracts as at March 31, 2018:

	NOTIONAL VALUE OF THE HEDGING INSTRUMENT	CARRYING VALUE OF THE HEDGING INSTRUMENT	ITEM LOCATION	FAIR VALUE CHANGES USED FOR CALCULATING HEDGE INEFFECTIVENESS		
				CASH FLOW HEDGE RESERVE	HEDGING INSTRUMENTS	HEDGED ITEMS
Cash flow hedges:						
Fuel price risk	54,569	12,472	Derivative assets	12,472	12,472	12,517

- (ii) Cash flow hedge reserve:

As at March 31	2018	2017
Hedging gains recognized in cash flow hedge reserve:		
Fuel swap contracts (note 20(a))	13,580	12,119
Hedging (gains) losses reclassified from cash flow hedge reserve:		
Interest rate forward contracts – amortization of hedge loss	248	248
Fuel swap contracts – (gain) loss recognized in net earnings (note 20(a))	(1,670)	6,310
Net change in cash flow hedge reserve	12,158	18,677

16. OTHER COMMITMENTS:

The Group has entered into operating leases for certain building spaces, land and equipment. Lease payments charged to expense during the year ended March 31, 2018 were \$1.1 million (March 31, 2017: \$0.9 million).

Future minimum lease payments are as follows:

Less than one year	994
Between one and five years	1,032
More than five years	258
Total	2,284

17. CONTINGENT LIABILITIES:

The Group, in conducting its usual business activities, is involved in various legal proceedings and litigation, the outcome of which is uncertain. It is the Group's policy to carry adequate insurance to minimize the financial risk associated with such matters. Management is of the opinion that the aggregate net liability, if any, of these proceedings and litigation would not be significant to the Group. Any additional future costs or recoveries which differ from the accrued amounts will be recognized in net earnings or loss as determined.

18. SHARE CAPITAL:**(a) Authorized:**

1,000,000	Class A voting common shares, without par value
1	Class B voting common share, without par value
80,000	Class C non-voting, 8% cumulative preferred shares, with a par value of \$1,000 per share, convertible to Class A shares upon the sale of the outstanding Class B share by the initial shareholder. Special rights attached to the Class C shares restrict the Group's ability to issue shares and to declare dividends.

(b) Issued and outstanding:

As at March 31	2018		2017	
	NUMBER OF SHARES	AMOUNT \$	NUMBER OF SHARES	AMOUNT \$
Class B, common	1	1	1	1
Class C, preferred	75,477	75,477	75,477	75,477
		75,478		75,478

(c) Dividends:

Dividends on the Class C cumulative preferred shares, if declared, are payable annually on March 31 of each year. All dividend entitlements to date have been paid.

19. CAPITAL MANAGEMENT:

The Group's principal business of ferry transportation requires ongoing access to capital in order to fund operations, satisfy outstanding long-term debt obligations and fulfill future capital asset acquisition obligations. In order to ensure capital market access is maintained, the Group targets maintaining strong investment grade credit ratings (note 15(b)).

The capital structure of the Group is presented in the following table:

As at March 31	2018		2017	
	\$	%	\$	%
Aggregate borrowings ¹	1,522,435	72.47	1,559,737	74.83
Total equity before reserves	578,433	27.53	524,498	25.17
Total	2,100,868	100.00	2,084,235	100.00

¹ Includes long-term debt, including current portion, credit facility (drawn and undrawn) and short-term borrowings.

The Group has covenants restricting the issuance of additional debt, distributions to shareholders, and guarantees and restricted investments. Incurrence of additional debt and distributions are restricted when aggregate borrowings exceed 85% of the Group's total capital while certain guarantees and certain investments may be restricted when aggregate borrowings exceed 75%.

Under the credit facility and the KfW loans, debt service coverage (earnings before interest, taxes, depreciation, amortization and rent) must be at least 1.25 times the debt service cost. Under the MTI, the Group is required to maintain debt service reserves (notes 10 and 15). Incurrence of additional debt is restricted if the debt service coverage ratio is less than 1.5 times the debt service cost and distributions are restricted if the debt service coverage ratio is less than 1.3 times. In addition to these restrictions and requirements, there are other covenants contained in these loan documents. The Group was in compliance with all of its covenants during the years ended March 31, 2018 and March 31, 2017.

20. OTHER COMPREHENSIVE INCOME (LOSS):

(a) Continuity of reserves:

	LAND REVALUATION RESERVES ¹	EMPLOYEE FUTURE BENEFIT REVALUATION RESERVES	FUEL SWAPS RESERVES	INTEREST RATE FORWARD CONTRACTS RESERVES	TOTAL
Balance as at April 1, 2016	3,389	(2,786)	(17,868)	(6,958)	(24,223)
Land revaluation	3,720	–	–	–	3,720
Actuarial loss on defined benefit plans (note 11(d))	–	(1,240)	–	–	(1,240)
Derivatives designated as cash flow hedges (note 15(c))					
Net change in fair value	–	–	12,119	–	12,119
Realized losses (note 15(c))	–	–	6,310	–	6,310
Amortization of losses (note 15(c))	–	–	–	248	248
Balance as at March 31, 2017	7,109	(4,026)	561	(6,710)	(3,066)
Land revaluation	1,825	–	–	–	1,825
Actuarial loss on defined benefit plans (note 11(d))	–	(1,943)	–	–	(1,943)
Derivatives designated as cash flow hedges (note 15(c))					
Net change in fair value	–	–	13,580	–	13,580
Realized (gains) (note 15(c))	–	–	(1,670)	–	(1,670)
Amortization of losses (note 15(c))	–	–	–	248	248
Balance as at March 31, 2018	8,934	(5,969)	12,471	(6,462)	8,974

¹ Land revaluation reserves represent the valuation surplus resulting from changes in fair value of land assets. The reserve increases during the years ended March 31, 2018 and March 31, 2017, are shown above. During the year ended March 31, 2018, the Group recognized less than \$0.1 million (March 31, 2017: less than \$0.1 million) in net earnings.

(b) Other comprehensive income:

Years ended March 31	2018	2017
Items to be reclassified to net earnings:		
Hedge gains on fuel swaps (note 15(c))	13,580	12,119
Items not to be reclassified to net earnings:		
Land revaluations	1,825	3,720
Actuarial losses on defined benefit plans (note 11(d))	(1,943)	(1,240)
Total other comprehensive income	13,462	14,599

21. NET RETAIL:

Years ended March 31	2018	2017
Retail revenue	98,339	91,098
Cost of goods sold	(38,268)	(35,959)
Net retail	60,071	55,139

22. OPERATING EXPENSES:

Years ended March 31	2018	2017
Salaries, wages & benefits	371,988	347,862
Fuel	102,485	100,616
Materials, supplies and contracted services	84,725	70,241
Other operating expenses	63,569	58,550
Depreciation and amortization	159,916	148,952
Total operating expenses	782,683	726,221

23. NET FINANCE EXPENSE:

Years ended March 31	2018	2017
Finance expenses:		
Long-term debt	63,612	62,504
Short-term debt	451	373
Finance leases	1,799	1,870
Amortization of deferred financing costs and bond discounts	1,283	718
Interest capitalized in the cost of qualifying assets	(6,466)	(6,706)
Total finance expenses	60,679	58,759
Finance income	(5,495)	(4,651)
Net finance expense	55,184	54,108

24. RELATED PARTY TRANSACTIONS:**(a) Management compensation:**

The compensation of the Group's directors and executive officers during the year is as follows:

Years ended March 31	2018	2017
Short-term benefits	2,120	1,696
Post-employment benefits	260	357
Termination benefits	593	–
Total	2,973	2,053

(b) B.C. Ferry Authority:

In accordance with the Act, the Group is responsible for paying any expenses that are incurred by the Authority, without charge. During the year ended March 31, 2018, the Group paid \$0.2 million (March 31, 2017: \$0.1 million) of such expenses.

The Province owns the Group's 75,477 non-voting preferred shares, but has no voting interest in either the Group or the Authority.

25. FERRY SERVICE FEES:

On April 1, 2003, the Group entered into an agreement with the Province to provide ferry services on specified routes that would not be commercially viable and to administer certain social policy initiatives on behalf of the Province. In exchange for these services and to compensate for these non-profitable routes, the Group receives ferry service fees. The agreement is for a period of sixty years, the details of which are renegotiated after a first term of five years and each four year term thereafter. The agreement has been amended from time to time to, among other things, establish the ferry service levels and the fees for the provision of such service for the fourth performance term ending March 31, 2020.

26. FEDERAL-PROVINCIAL SUBSIDY AGREEMENT:

The Group receives revenue provided to the Province from the Government of Canada pursuant to a contract between the federal and provincial governments. The federal government gives financial assistance to fulfill the obligation of providing ferry services to coastal British Columbia. The annual payment increases with the Vancouver Consumer Price Index.

27. ECONOMIC EFFECT OF RATE REGULATION:

The Group is regulated by the Commissioner to ensure, among other things, that tariffs are fair and reasonable. Under the terms of the Act, the tariffs the Group charges its customers are subject to price caps. The Commissioner may, in extraordinary situations, allow increases in price caps over the set levels.

In January 2014, the IASB issued IFRS 14 *Regulatory Deferral Accounts*. IFRS 14 is an interim standard that addresses the accounting for regulatory deferral accounts; however, it does not allow the recognition of regulatory assets and regulatory liabilities that result from the regulated price cap setting process for entities that had already transitioned to IFRS. The Group transitioned to IFRS effective April 1, 2011. As a result, the Group is not permitted to recognize its regulatory assets and regulatory liabilities in its consolidated statements of financial position.

Regulatory assets generally represent incurred costs that have been deferred for purposes of rate regulation because they are probable of future recovery in tariffs or fuel surcharges. Regulatory liabilities represent obligations to customers which will be settled through future tariff reductions or fuel rebates. Management continually assesses whether the Group's regulatory assets are probable of future recovery by considering such factors as applicable regulatory changes. Management believes that the obligations represented by the regulatory liabilities at March 31, 2018, will be settled through future tariff reductions or fuel rebates.

If the Group was permitted under IFRS to recognize the effects of rate regulation, the following regulatory assets and regulatory liabilities would be shown on the consolidated statements of financial position:

As at March 31	2018	2017
Regulatory (liabilities) assets		
Deferred fuel costs (a):		
Balance – beginning of year	4,450	(6,132)
Fuel costs under set price	(8,630)	(7,625)
Rebates	19,386	18,068
Fuel price risk recoveries payable to the Province	291	139
Corporate contribution	(15,736)	–
Balance – end of year	(239)	4,450
Total long term regulatory (liabilities) assets	(239)	4,450

(a) Deferred fuel costs:

As prescribed by regulatory order, the Group defers differences between actual fuel costs and approved fuel costs which were used to develop the regulated price caps.

The regulatory deferred fuel cost accounts operate as follows:

- i) for those routes operating on the mid-coast and to and from Prince Rupert;
 - a. the first 5 cents per litre of difference is recorded in deferral accounts for recovery or settlement through future tariffs to customers;
 - b. any difference beyond 5 cents per litre is recorded in accounts receivable or payable for subsequent recovery from or payment to the Province, and
- ii) for all other routes;
 - a. recorded in deferral accounts for recovery or settlement through future tariffs to customers.

Also prescribed by regulatory order, the Group collects fuel surcharges or provides fuel rebates from time to time which are applied against deferred fuel cost account balances.

During the year ended March 31, 2018, the amounts payable to the Province in relation to fuel cost differences totalled \$0.3 million (March 31, 2017: \$0.1 million). At March 31, 2018, the Group contributed \$15.7 million to cover the balance in the non-northern routes' deferred fuel cost account and eliminate the need to recoup these costs from customers in the future.

(b) Tariffs in excess of price cap:

The Act contains provisions which ensure that if tariffs charged by the Group exceed established price caps, the excess amounts collected will be returned to customers through future tariffs. At March 31, 2018 and March 31, 2017, tariffs charged to customers were below established price caps.

If the Group was permitted under IFRS to recognize the effects of rate regulation and to record regulatory assets and regulatory liabilities, net earnings for the year ended March 31, 2018 would have been \$4.7 million lower (March 31, 2017: \$10.6 million higher) as detailed below:

Effect of rate regulation on net earnings

Years ended March 31	2018	2017
Regulatory accounts:		
Deferred fuel costs	(4,689)	10,582
Total (decrease) increase in net earnings	(4,689)	10,582

Board of Directors

(fiscal year ended March 31, 2018)

Donald P. Hayes

Chair

Jane M. Bird

(ceased to be a director February 23, 2018)

Bruce A. Chan

Jan K. Grude

(effective June 29, 2017)

John A. Horning

Brian G. Kenning

Gordon M. Kukec

Sarah A. Morgan-Silvester

P. Geoffrey Plant, QC

Senior Officers of the Company

(fiscal year ended March 31, 2018)

Mark F. Collins

President & Chief Executive Officer

Glen N. Schwartz

Executive Vice President, Human Resources
& Corporate Development

Corrine E. Storey

Vice President & Chief Operating Officer

M. Alana Gallagher

Vice President, Finance & Chief Financial Officer

Officers of the Company

(fiscal year ended March 31, 2018)

Joanne E. Carpendale

Treasurer

Janet E. Carson

Vice President, Marketing & Customer Experience

Cynthia M. Lukaitis

Vice President & Corporate Secretary

Captain D.W. James Marshall

Vice President, Business Development & Innovation

Erwin Martinez

Vice President & Chief Information Officer

Mark C. Wilson

Vice President, Strategy & Community Engagement

A family consisting of a woman, a man, and a young child are sitting on a blue metal bench on the deck of a ferry. They are looking out at the vast blue ocean. The deck has a white metal railing. The water is choppy with white foam from the ferry's wake. The scene is bright and sunny, with shadows cast on the deck.

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On behalf of the board of directors of the B.C. Ferry Authority (the "Authority"), I am pleased to present the annual report of the Authority for the fiscal year ended March 31, 2018. This report provides information on the actions taken by the Authority to meet its statutory responsibilities during the fiscal year, and is an important part of the Authority's framework for accountability to stakeholders and the public generally.

The Authority is the sole voting shareholder of British Columbia Ferry Services Inc. ("BC Ferries" or the "Company"), the service provider under contract to the Province of British Columbia, responsible for the delivery of safe, efficient and dependable ferry service along coastal British Columbia. The Authority has responsibility under the *Coastal Ferry Act* for appointing the board of directors of BC Ferries and for approving compensation plans for the directors and certain executive officers of the Company.

This past year, the Authority continued to focus on ensuring that BC Ferries has a strong and effective board of directors to oversee the key operational and strategic objectives of the Company. During the year, the Authority appointed one new director to the board of BC Ferries, and extended the appointments of two incumbent directors for subsequent terms. The Authority is confident that the depth of skills and experience represented on the BC Ferries board will ensure that the oversight and stewardship of the Company continues to be effective.

No changes were made to the BC Ferries director and executive compensation plans previously established by the Authority. These plans are available for public view on the Authority's website at www.bcferryauthority.com.

The close of this past year brought with it a change in the membership of the board of the Authority. On behalf of the board, I extend special thanks to outgoing director Randy Morriss for his years of dedicated and valuable service to the Authority. I also take pleasure in welcoming Shelley Chrest to the Authority board and recognize the experience and expertise she will bring.

A handwritten signature in black ink that reads "Yuri Fulmer". The signature is written in a cursive style.

YURI FULMER
CHAIR OF THE BOARD OF DIRECTORS
B.C. FERRY AUTHORITY

The B.C. Ferry Authority (the "Authority" or "BCFA") is established and governed by the *Coastal Ferry Act*. The Authority is a corporation without share capital which owns the single issued voting share of British Columbia Ferry Services Inc. ("BC Ferries" or the "Company"), the service provider under contract to the Province of British Columbia (the "Province") responsible for the delivery of ferry service along coastal British Columbia. The Province is the holder of all of the preferred shares of BC Ferries and has no voting interest in either the Authority or BC Ferries.

The Authority's principal responsibilities are set out in the *Coastal Ferry Act* and are to appoint the directors of BC Ferries and to establish compensation plans for the directors and certain executive officers of the Company.

The Authority and BC Ferries have entered into a protocol agreement which clarifies and confirms their respective roles and responsibilities in relation to the authority of BCFA as shareholder of BC Ferries and the matters respecting the appointment and remuneration of BC Ferries' directors, and the remuneration of certain executive officers of the Company.

The Authority has adopted high standards of public and stakeholder accountability that require the Authority's financial and operating performance, the plans it has established in respect of BC Ferries' director and executive compensation, and its processes for appointing directors of the Authority and BC Ferries to be open to public view.

APPOINTMENT OF DIRECTORS OF BC FERRIES

In accordance with the *Coastal Ferry Act*, the Authority makes its determinations on the composition of the BC Ferries board of directors (the "board") in consideration of the skills and experience that each director holds. The Authority selects individuals for appointment or renewal of term in such a way as to ensure that, as a group, the directors of the Company are qualified candidates who hold all of the skills and all of the experience needed to oversee the operation of BC Ferries in an efficient and cost-effective manner. The Authority has established a profile setting out the key skills and experience that BC Ferries' directors individually and collectively should possess to meet this legislative requirement. The skills and experience profile is reviewed regularly by BCFA to ensure alignment of the skills and experience represented on the BC Ferries board with the key operational and strategic objectives of the Company for which the directors collectively have oversight responsibility.

The Authority holds the view that a diverse board makes prudent business sense and makes for good corporate governance. Within the over-riding objective of ensuring that the board of BC Ferries possesses the appropriate skills and experience, the Authority also seeks to maintain a composition of talented and dedicated directors with a diverse mix of backgrounds that is reflective of the nature of the business environment in which the Company operates, and the people and the communities it serves.

In the year ended March 31, 2018 ("fiscal 2018"), the Authority increased the size of the BC Ferries board from eight to nine, and appointed one new director, Jan K. Grude, for a term ending 2021, and re-appointed incumbent director Brian G. Kenning for a subsequent term ending 2019. These changes were effective June 29, 2017. Also in fiscal 2018, the Authority extended the term of incumbent director and chair of the board, Donald P. Hayes, by one year to 2019.

The directors of BC Ferries in fiscal 2018 are listed in Table 1.

Table 1 – BC Ferries Board of Directors

Year ended March 31, 2018

DIRECTOR	TERM ENDING
Donald P. Hayes, Chair	2019
Jane M. Bird ¹	2021
Bruce A. Chan	2019
Jan K. Grude ²	2021
John A. Horning	2020
Brian G. Kenning	2019
Gordon M. Kukec	2018
Sarah A. Morgan-Silvester	2020
P. Geoffrey Plant	2019

1. Jane M. Bird resigned from the board effective February 23, 2018.

2. Jan K. Grude was appointed to the board effective June 29, 2017.

In fiscal 2018, the Authority also confirmed its intent to re-appoint incumbent director Gordon M. Kukec for a subsequent term ending 2022. This change was effective June 28, 2018.

BC FERRIES COMPENSATION PLANS

As required by the *Coastal Ferry Act*, the Authority has established director and executive compensation plans for BC Ferries. The current plans are available for public view on the Authority's website: www.bcferryauthority.com.

Directors' Compensation Plan

The compensation plan for the directors of BC Ferries was established in the year ended March 31, 2011. The remuneration limits set out in the plan were established with the assistance of an independent third-party compensation expert and with reference to the *Coastal Ferry Act*, which requires that the remuneration under a directors' compensation plan be consistent with the remuneration that organizations in Canada that are of a similar size and scope to BC Ferries provide to their directors, and not be greater than the remuneration that provincial public sector organizations in British Columbia provide to their directors. The remuneration for the directors of the Company was set by BCFA in accordance with the plan effective October 1, 2010. The directors' compensation plan and the remuneration framework for the Company's directors have remained unchanged since their establishment by the Authority.

Executive Compensation Plan

An executive compensation plan applies to the executives of the Company, as that term is defined in the *Coastal Ferry Act*, and includes the individuals holding the positions of, or acting in a similar capacity or performing similar functions to, the Chief Executive Officer ("CEO") or an Executive Vice President. Pursuant to *Miscellaneous Statutes Amendment Act No. 3 - 2010* ("Bill 20"), an individual who held such a position on the date Bill 20 received first reading in 2010 is excluded from the provisions of an executive compensation plan for so long as that individual remains in that executive position with BC Ferries.

An executive compensation plan describes the philosophy for executive compensation and the maximum remuneration that the individuals whose compensation is governed by such a plan can receive in any year. The remuneration limits set out in an executive compensation plan are established with the assistance of an independent third-party compensation expert and with reference to the *Coastal Ferry Act*, which requires that the remuneration under an executive compensation plan be consistent with the remuneration provided to individuals who, in organizations in Canada that are of a similar size and scope to BC Ferries, perform similar services or hold similar positions, and not be greater than the remuneration that provincial public sector employers in British Columbia provide to individuals who, in those organizations, perform similar services or hold similar positions.

In the year-ended March 31, 2017, the Authority approved an executive compensation plan with an effective date of September 1, 2016 (the "2017 plan"). At the commencement of fiscal 2018, in accordance with the *Coastal Ferry Act* and Bill 20, this plan solely governed the remuneration of the Company's President and CEO.

The remuneration limits set out in an executive compensation plan are periodically reviewed in conjunction with market data from the appropriate comparator organizations. Occasioned by the Company's decision to appoint a new Chief Financial Officer and a Chief Operating Officer, the Authority undertook a review in fiscal 2018 of the remuneration limits in the 2017 plan for these two positions. The remuneration limits were reviewed against recent remuneration provided for similar positions in comparator organizations in the public and private sectors. Based on this review, the Authority determined that the maximum level of remuneration for the positions, as set out in the 2017 plan, continued to meet the requirements of the *Coastal Ferry Act*, and no amendment of the plan was required. BC Ferries' appointments to the positions of Chief Financial Officer and Chief Operating Officer were effective July 1, 2017 and October 16, 2017, respectively, and remuneration for the positions was set by the Company in accordance with the 2017 plan.

Appointment of BCFA Directors

The composition of the board of the Authority is set out in the *Coastal Ferry Act* and includes regional and stakeholder representation. Four directors are to be appointed by the board from nominees of four appointment areas composed of coastal regional districts, and one director is to be appointed from the nominees of the BC Ferry & Marine Workers' Union, the trade union representing the employees of BC Ferries. The board is also to include two directors appointed by the Province and two additional directors appointed by the board from members of the community-at-large.

At the conclusion of fiscal 2018, Randolph K. Morriss, appointed from nominees of the Central Vancouver and Northern Georgia Strait appointment area, retired from the board. Effective April 1, 2018, the board appointed Shelley L. Chrest, a qualified candidate nominated by the Central Vancouver Island and Northern Georgia Strait appointment area as a director, and re-appointed incumbent directors Yuri L. Fulmer, a qualified candidate from the community-at-large, and Michael W. Pucci, a qualified candidate nominated by the Northern Coastal and North Island appointment area, each for a subsequent term as a director. All three appointments are for three-year terms ending March 31, 2021.

The directors of BCFA in fiscal 2018 are listed in Table 2. In selecting individuals to serve as directors of the Authority, two primary objectives continued to guide the board in its deliberations. The first objective was to ensure that the composition of the board continues to meet the requirements of the *Coastal Ferry Act*, and the second was to ensure that, collectively, the board includes qualified individuals with the skills and experience necessary to ensure the sound performance of the Authority and the effective interaction and operation of the board. The skills and experience profile for the BCFA board guided the board in its appointment process during the year. The profile is reviewed by the board on an annual basis to ensure it encompasses the appropriate set of skills and experience. A copy of the current profile is attached as Schedule "A" to the general bylaws of the Authority.

The Authority believes that a diverse board serves to strengthen decision making and enhances overall board governance. Within the overarching objective of ensuring that the board is composed of members that collectively possess the appropriate skills and experience to enable the Authority to perform its stewardship role effectively, the board, in selecting candidates for appointment, also seeks to maintain and/or enhance the diversity of background among its members.

Table 2 – BCFA Board of Directors

Year Ended March 31, 2018

DIRECTOR		TERM ENDING MARCH 31
Yuri L. Fulmer, Chair ¹	Community-at-Large	2018
Fiona L. Macdonald	Community-at-Large	2019
Shirley J. Mathieson	Organized Labour	2019
Susan G. Mehinagic	Southern Vancouver Island Appointment Area	2020
Randolph K. Morriss ²	Central Vancouver Island and Northern Georgia Strait Appointment Area	2018
G. Wynne Powell	Province of British Columbia	2020
Michael W. Pucci ³	Northern Coastal and North Island Appointment Area	2018
Sandra A. Stoddart-Hansen	Southern Mainland Appointment Area	2020
Paul L. Williams	Province of British Columbia	2019

1. Yuri L. Fulmer was re-appointed to the board from the community-at-large effective April 1, 2018 for a subsequent term ending 2021.

2. Randolph K. Morriss retired from the board on March 31, 2018, and Shelley L. Chrest, a nominee of the Central Vancouver Island and Northern Georgia Strait appointment area, was appointed to the board effective April 1, 2018 for a term ending 2021.

3. Michael W. Pucci, a nominee of the Northern Coastal and North Island appointment area, was re-appointed to the board effective April 1, 2018 for a subsequent term ending 2021.

BCFA GENERAL BYLAWS

The general bylaws of the Authority are available for public view on the Authority's website. There were no amendments made to the general bylaws in fiscal 2018.

BCFA BOARD MEETINGS

The board meets regularly to conduct its business. In fiscal 2018, the board met on five occasions. This included the annual general meeting of the Authority held in accordance with the *Coastal Ferry Act*. A summary of the outcomes of the meetings of the board is provided in Table 3.

Table 3 – Summary of Meeting Outcomes

Year Ended March 31, 2018

DATE	TYPE	OUTCOMES ¹
June 29, 2017	Board of Directors	<ul style="list-style-type: none"> • Fiscal 2017 audited financial statements of the Authority approved. • Fiscal 2017 annual report of the Authority approved. • Fiscal 2017 report on the Authority's compliance with the <i>Coastal Ferry Act</i> approved for submission to the British Columbia Ferries Commissioner. • Amendments to the board's governance manual approved. • Corporate Secretary authorized to execute the shareholder's unanimous consent resolutions pertaining to matters respecting the business required to be transacted at the 2017 annual general meeting of BC Ferries. • Yuri L. Fulmer re-appointed a director of the Authority from the community-at-large effective April 1, 2018 for a subsequent term ending March 31, 2021. • Term of appointment of Donald P. Hayes as a director of BC Ferries extended one year to 2019.
August 18, 2017	Board of Directors	<i>No resolutions passed.</i>
August 18, 2017	Annual General Meeting	<i>Annual General Meeting open to the public held in Vancouver, British Columbia.</i>
September 8, 2017	Board of Directors	<ul style="list-style-type: none"> • Remuneration caps in the BC Ferries executive compensation plan for the Chief Operating Officer and Chief Financial Officer positions confirmed.
March 22, 2018	Board of Directors	<ul style="list-style-type: none"> • Michael W. Pucci re-appointed a director of the Authority from nominees of the Northern Coastal and North Island appointment area effective April 1, 2018 for a subsequent term ending March 31, 2021. • Shelley L. Chrest appointed a director of the Authority from nominees of the Central Vancouver Island and Northern Georgia Strait appointment area effective April 1, 2018 for a term ending March 31, 2021. • Appointment of Yuri L. Fulmer as chair of the board continued. • External auditor of the Authority re-appointed for a period of up to three years commencing fiscal 2019. • Fiscal 2018 terms of engagement of the external auditor approved. • Fiscal 2019 operating budget of the Authority approved. • Time and location of the 2018 annual general meeting of the Authority confirmed. • Intent to re-appoint Gordon M. Kukec as a director of BC Ferries for a term ending 2022 confirmed.

1. Meeting outcomes are resolutions passed by the board.

Meeting attendance for board members is an important issue and one that the Authority monitors on a regular basis. In fiscal 2018, meeting attendance by board members was 100 percent.

REMUNERATION OF BCFA DIRECTORS

An outline of the current remuneration framework for directors of the Authority is provided in Table 4. The framework was set by the board effective October 1, 2010 and has remained unchanged since that date. The amount each director received for remuneration and expenses in fiscal 2018 is set out in Table 5.

Table 4 – BCFA Director Remuneration Framework**Year Ended March 31, 2018****ANNUAL RETAINERS**

Board Chair Retainer	\$25,000
Board Member Retainers:	
Base Retainer (all directors excluding board Chair)	\$ 6,250
Committee Chair Retainer ¹	\$ 2,000
Committee Member Retainer ¹	\$ 750

PER DIEM FEES²

Board Member Fees (all directors excluding board Chair)	Up to \$1,200 per day
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FERRY TRAVEL PASS

Ferry pass for directors and eligible members of their respective immediate families, for complimentary vehicle and personal travel on BC Ferries' vessels.

1. There currently are no committees of the board.

2. Directors are also eligible for reimbursement of reasonable expenses incurred on board-related business.

Table 5 – BCFA Director Remuneration and Expenses**Year Ended March 31, 2018**

DIRECTOR	REMUNERATION ¹ \$	EXPENSES REIMBURSED \$
Yuri L. Fulmer ²	28,837	115
Fiona L. Macdonald	11,491	Nil
Shirley J. Mathieson	12,556	Nil
Susan G. Mehinagic	14,998	228
Randolph K. Morriss	13,638	958
G. Wynne Powell	13,538	Nil
Michael W. Pucci	17,154	823
Sandra A. Stoddart-Hansen	15,231	1,783
Paul L. Williams	11,050	Nil

1. Remuneration includes retainers, per diem fees and taxable income from the ferry travel pass program.

2. Yuri L. Fulmer served as Chair of the board in fiscal 2018.

TO THE BOARD OF DIRECTORS, B.C. FERRY AUTHORITY

We have audited the accompanying financial statements of B.C. Ferry Authority, which comprise the statements of financial position as at March 31, 2018, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audit is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the financial statements present fairly, in all material respects, the financial position of B.C. Ferry Authority as at March 31, 2018, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.



Chartered Professional Accountants

Victoria, Canada

June 28, 2018

B.C. FERRY AUTHORITY

Statements of Financial Position (Expressed in thousands of Canadian dollars)

As at March 31	2018	2017
ASSETS		
Investment in British Columbia Ferry Services Inc.	511,930	445,955
Total assets	511,930	445,955
EQUITY		
Invested in common share of British Columbia Ferry Services Inc.	1	1
Contributed surplus of British Columbia Ferry Services Inc.	25,000	25,000
Accumulated undistributed earnings of British Columbia Ferry Services Inc.	486,929	420,954
Total equity	511,930	445,955

Statements of Comprehensive Income (Expressed in thousands of Canadian dollars)

Years ended March 31	2018	2017
REVENUE		
Distributable earnings of British Columbia Ferry Services Inc. (note 3)	65,975	92,485
Total revenue	65,975	92,485
EXPENSES		
Administration	164	119
Recovery from British Columbia Ferry Services Inc. (note 4)	(164)	(119)
Total expenses	–	–
Total comprehensive income	65,975	92,485

Statements of Cash Flows (Expressed in thousands of Canadian dollars)

Years ended March 31	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings	65,975	92,485
Items not affecting cash		
Distributable earnings of British Columbia Ferry Services Inc. (note 3)	(65,975)	(92,485)
Net increase in cash	–	–

Statements of Changes in Equity (Expressed in thousands of Canadian dollars)

	INVESTED IN BCFS	CONTRIBUTED SURPLUS OF BCFS	ACCUMULATED UNDISTRIBUTED EARNINGS OF BCFS	TOTAL EQUITY
Balance as at April 1, 2016	1	25,000	328,469	353,470
Total comprehensive income for the year ended March 31, 2017	–	–	92,485	92,485
Balance as at March 31, 2017	1	25,000	420,954	445,955
Total comprehensive income for the year ended March 31, 2018	–	–	65,975	65,975
Balance as at March 31, 2018	1	25,000	486,929	511,930

YEARS ENDED MARCH 31, 2018 AND 2017**(Tabular amounts expressed in thousands of Canadian dollars)**

B.C. Ferry Authority (the "Authority") was established by the *Coastal Ferry Act* (British Columbia) (the "Act") on April 1, 2003, as a corporation without share capital. The Act specifies that the Authority is governed by a board of nine directors. The terms of three director positions expire each fiscal year. The board of directors appoints replacements for outgoing directors for seven of the positions as follows:

- four appointed from nominees of qualified individuals, as defined in the Act, provided to the board by each of the four appointment areas consisting of those coastal regional districts that the Lieutenant Governor in Council of British Columbia may prescribe, with one director appointed from each area;
- one appointed from nominees of qualified individuals provided by the trade union representing the employees of British Columbia Ferry Services Inc. ("BCFS");
- two appointed from qualified individuals selected by the board of directors.

The Lieutenant Governor in Council of British Columbia appoints the other two directors from qualified individuals as terms expire.

The Authority's primary purposes are set out in the Act and are to hold the single-issued common voting share of BCFS, a company incorporated under the *Company Act* (British Columbia) by way of conversion on April 2, 2003, and which now validly exists under the *Business Corporations Act* (British Columbia), to appoint the directors of BCFS, and to establish compensation plans for the directors and certain executive officers of BCFS. BCFS's primary business is the provision of coastal ferry services in British Columbia. The Province of British Columbia (the "Province") contributed the initial capital to the Authority to fund the purchase of the BCFS common share. The Act provides that upon a sale of the common share of BCFS held by the Authority, the Province is to be repaid its initial contribution and the Authority is dissolved. The Act also provides that upon dissolution of the Authority, all remaining assets of the Authority, if any, vest in the Province. As part of his annual report to the Lieutenant Governor in Council, the British Columbia Ferries Commissioner is required by the Act to issue an opinion on the performance of the Authority in carrying out its legislated responsibilities.

1. ACCOUNTING POLICIES:**(a) Basis of preparation:**

B.C. Ferry Authority is a corporation domiciled in Canada. The address of the Authority's head office is Suite 500, 1321 Blanshard Street, Victoria, BC Canada, V8W 0B7. These financial statements of the Authority as at and for the years ended March 31, 2018 and 2017 comprise the Authority and its wholly-owned subsidiary, BCFS (along with its subsidiaries), together referred to as (the "Group"). The Group's investment in its wholly-owned subsidiary, BCFS, is accounted for using the equity method. Under the equity method the original cost of the investment is adjusted for the Authority's share of post-acquisition earnings or losses, dividends and any other post-acquisition changes in the equity of BCFS.

These financial statements represent the annual statements of the Group prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). In accordance with IFRS, the Group has provided comparative financial information and applied the same accounting policies throughout all periods presented.

These financial statements were approved by the Board of Directors on June 28, 2018.

These financial statements have been prepared using the historical cost method, except for land, land under finance lease, and certain financial assets and liabilities, including derivatives, which are measured at fair value.

These financial statements are presented in Canadian dollars which is the Group's functional currency. All financial data is presented in thousands of Canadian dollars.

(b) Use of estimates and judgements:

The preparation of financial statements in accordance with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting methods and the amounts recognized in the financial statements. These estimates and the underlying assumptions are established and reviewed continuously on the basis of past experience and other factors considered reasonable in the circumstances. They therefore serve as the basis for making judgements about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from the estimates.

(c) Taxes:

The Group is a "Tax Exempt Corporation" as described in the *Income Tax Act* and as such is exempt from federal and provincial income taxes.

2. ADOPTION OF NEW AND AMENDED STANDARDS:**(a) Changes in accounting policies:**

No new or amended standards or interpretations to existing standards were applied by the Group during the year ended March 31, 2018.

(b) Future changes in accounting policies:**IFRS 15 Revenue from Contracts with Customers:**

IFRS 15 *Revenue from Contracts with Customers* will replace IAS 11 *Construction Contracts* and IAS 18 *Revenue*. It provides a single, principles based five-step model to be applied to all contracts with customers. IFRS 15 also requires additional disclosures. The mandatory effective date of IFRS 15 is for annual reporting periods beginning on or after January 1, 2018, and must be applied using either a full retrospective application or a retrospective with cumulative effect application. There is no impact on the Group's financial statements other than the impact on the earnings or losses and other changes in equity of BCFS.

IFRS 9 Financial Instruments (2014):

On July 24, 2014, the IASB issued the completed version of IFRS 9. IFRS 9 (2014) introduces a new expected credit loss model for calculating impairment, and incorporates the guidance on the classification and measurement of financial assets and the final general hedge accounting requirements originally published in IFRS 9 (2013). The Group adopted IFRS 9 (2013) in the year ended March 31, 2015. The mandatory effective date of IFRS 9 (2014) is for annual reporting periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions. There is no impact on the Group's financial statements other than the impact on earnings or losses and other changes in equity of BCFS.

IFRS 16 Leases:

On January 13, 2016, the IASB issued IFRS 16 *Leases*, which will replace IAS 17 *Leases*. The standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. The standard is effective for annual reporting periods beginning on or after January 1, 2019. Early adoption is permitted if IFRS 15 *Revenue from Contracts with Customers* has also been applied. The Group intends to early adopt IFRS 16 for the annual reporting period beginning on April 1, 2018. There is no impact on the Group's financial statements other than the impact on earnings or losses and other changes in equity of BCFS.

3. DISTRIBUTABLE EARNINGS OF BRITISH COLUMBIA FERRY SERVICES INC.:

The distributable earnings of BCFS consist of the current period total comprehensive income, less amounts reclassified from equity and any dividends paid in the current period and less a reserve for undeclared preferred share dividends, if any.

Years ended March 31	2018	2017
Net earnings of BCFS	59,973	77,366
Other comprehensive (loss) gain		
Items not to be reclassified to net earnings	(118)	2,480
Items to be reclassified to net earnings	13,580	12,119
Total comprehensive income	73,435	91,965
Realized hedge (gain) losses recognized on fuel swaps	(1,670)	6,310
Hedge losses on interest rate forward contract reclassified to net earnings	248	248
Dividends paid on 8% cumulative preferred shares	(6,038)	(6,038)
Distributable earnings	65,975	92,485

4. RECOVERY FROM BRITISH COLUMBIA FERRY SERVICES INC.:

In accordance with the Act, BCFS is responsible for paying any expenses that are incurred by the Authority.

5. SUBSIDIARY SUPPLEMENTAL INFORMATION:

The consolidated financial position and operating results for BCFS and its wholly-owned subsidiaries are summarized below:

As at March 31	2018	2017
Assets:		
Current assets	295,254	272,674
Non-current assets	1,867,168	1,774,220
	2,162,422	2,046,894
Liabilities:		
Current liabilities	227,422	185,016
Non-current accrued employee future benefits	21,299	20,913
Long-term debt and other long-term liabilities	1,326,294	1,319,533
	1,575,015	1,525,462
Equity:		
Common share held by the Authority	1	1
Preferred shares (a)	75,477	75,477
Contributed surplus	25,000	25,000
Retained earnings	477,955	424,020
Equity before reserves	578,433	524,498
Reserves	8,974	(3,066)
Total equity including reserves	587,407	521,432
	2,162,422	2,046,894

Years ended March 31	2018	2017
Revenue	899,018	859,283
Expenses	839,045	781,917
Net earnings	59,973	77,366
Other comprehensive income	13,462	14,599
Total comprehensive income	73,435	91,965
Cash flows from operating	215,954	226,435
Cash flows from financing	914	54,673
Cash flows from investing	(218,987)	(288,189)

- (a) The outstanding non-voting, 8% cumulative preferred shares are held by the Province and are convertible to common shares upon a sale of the outstanding common share. Special rights attached to the preferred shares restrict BCFS' ability to issue share capital and to declare dividends.

(b) Other comprehensive income (loss):

(i) Continuity of reserves:

	LAND REVALUATION RESERVES	EMPLOYEE FUTURE BENEFIT REVALUATION RESERVES	FUEL SWAP RESERVES	INTEREST RATE FORWARD CONTRACTS RESERVES	TOTAL
Balance at April 1, 2016	3,389	(2,786)	(17,868)	(6,958)	(24,223)
Land revaluation	3,720	–	–	–	3,720
Actuarial loss on defined benefit plans	–	(1,240)	–	–	(1,240)
Derivatives designated as cash flow hedges:					
Net change in fair value	–	–	12,119	–	12,119
Realized losses	–	–	6,310	–	6,310
Amortization of losses	–	–	–	248	248
Balance at March 31, 2017	7,109	(4,026)	561	(6,710)	(3,066)
Land revaluation	1,825	–	–	–	1,825
Actuarial loss on defined benefit plans	–	(1,943)	–	–	(1,943)
Derivatives designated as cash flow hedges:					
Net change in fair value	–	–	13,580	–	13,580
Realized (gains)	–	–	(1,670)	–	(1,670)
Amortization of losses	–	–	–	248	248
Balance at March 31, 2018	8,934	(5,969)	12,471	(6,462)	8,974

(ii) Other comprehensive income:

Years ended March 31	2018	2017
Items to be reclassified to net earnings:		
Hedge gain on fuel swaps	13,580	12,119
Items not to be reclassified to net earnings:		
Land revaluations	1,825	3,720
Actuarial losses on defined benefit plans	(1,943)	(1,240)
Total other comprehensive income	13,462	14,599

Other comprehensive income of BCFS includes:

- In cash flow hedging relationships, the effective portion of the change in the fair values of the derivatives.
- Fair value increases of land and land under finance lease assets, except to the extent that such an increase represents a reversal of an amount previously recognized in net earnings or loss. Fair value decreases are recognized in net earnings or loss to the extent the decrease exceeds the balance, if any, held in the land revaluation reserve relating to a previous revaluation.
- Actuarial gains and losses on employee future benefits which are not reclassified to net earnings or loss in subsequent periods.

6. RELATED PARTY TRANSACTIONS:**Management compensation:**

The compensation of the Group's directors and executive officers during the year is as follows:

Years ended March 31	2018	2017
Short-term benefits	2,258	1,838
Post-employment benefits	260	357
Termination benefits	593	–
Total	3,111	2,195

7. SHARE CAPITAL:

The share capital of BCFS is described below:

(a) Authorized:

1,000,000 Class A voting common shares, without par value

1 Class B voting common share, without par value

80,000 Class C non-voting, 8% cumulative preferred shares, with a par value of \$1,000 per share, convertible to Class A shares upon the sale of the outstanding Class B share by the initial shareholder. Special rights attached to the Class C shares restrict the Group's ability to issue shares and to declare dividends.

(b) Issued and outstanding:

As at March 31	2018		2017	
	NUMBER OF SHARES	AMOUNT \$	NUMBER OF SHARES	AMOUNT \$
Class B, common	1	1	1	1
Class C, preferred	75,477	75,477	75,477	75,477
		75,478		75,478

(c) Dividends:

Dividends on the Class C cumulative preferred shares, if declared, are payable annually on March 31 of each year. All dividend entitlements to date have been paid.

Board of Directors

(Year ended March 31, 2018)

Yuri L. Fulmer

Chair

Fiona L. Macdonald

Shirley J. Mathieson

Susan G. Mehinagic

Randolph K. Morriss

G. Wynne Powell

Michael W. Pucci

Sandra A. Stoddart-Hansen

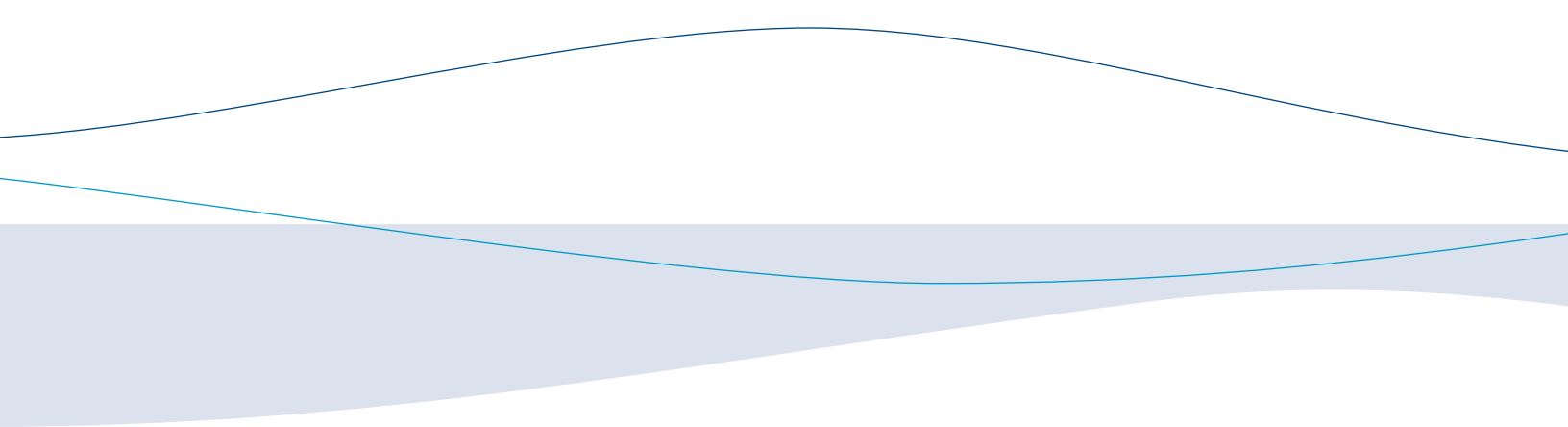
Paul L. Williams

Officers of the Company

(Year ended March 31, 2018)

Cynthia M. Lukaitis

Vice President & Corporate Secretary



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