Consolidated Financial Statements of

BRITISH COLUMBIA FERRY SERVICES INC.

Nine months ended December 31, 2007 and 2006

(unaudited)
BRITISH COLUMBIA FERRY SERVICES INC.
Consolidated Balance Sheets
(expressed in thousands)

<table>
<thead>
<tr>
<th></th>
<th>December 31, 2007</th>
<th>March 31, 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(unaudited)</td>
<td></td>
</tr>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current assets:</td>
<td></td>
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</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$ 27,758</td>
<td>$ 180,123</td>
</tr>
<tr>
<td>(note 2(c))</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Short-term investments</td>
<td>27,244</td>
<td>16,046</td>
</tr>
<tr>
<td>(note 2(c))</td>
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</tr>
<tr>
<td>Accounts receivable</td>
<td>15,620</td>
<td>19,050</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>6,049</td>
<td>5,879</td>
</tr>
<tr>
<td>Inventories</td>
<td>17,212</td>
<td>16,492</td>
</tr>
<tr>
<td>Regulatory assets (note 4)</td>
<td>3,581</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>97,464</td>
<td>237,590</td>
</tr>
<tr>
<td>Capital assets (note 3)</td>
<td>1,122,005</td>
<td>918,824</td>
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<tr>
<td>Deferred financing costs</td>
<td>1,270</td>
<td>9,580</td>
</tr>
<tr>
<td>(note 1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regulatory assets (note 4)</td>
<td>37,063</td>
<td>21,721</td>
</tr>
<tr>
<td>Long-term land lease</td>
<td>27,784</td>
<td>28,060</td>
</tr>
<tr>
<td></td>
<td>$ 1,265,586</td>
<td>$1,215,775</td>
</tr>
<tr>
<td><strong>Liabilities and Shareholders’ Equity</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current liabilities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounts payable and accrued</td>
<td>$ 42,965</td>
<td>$ 72,511</td>
</tr>
<tr>
<td>liabilities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Short term debt</td>
<td>39,918</td>
<td>24,888</td>
</tr>
<tr>
<td>Interest payable on long-term</td>
<td>8,453</td>
<td>12,663</td>
</tr>
<tr>
<td>debt</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accrued employee costs</td>
<td>49,769</td>
<td>47,393</td>
</tr>
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<td>Deferred revenue</td>
<td>13,168</td>
<td>12,031</td>
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<td>Derivative liabilities</td>
<td>26,340</td>
<td>-</td>
</tr>
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<td>(note 5)</td>
<td></td>
<td></td>
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<tr>
<td>Regulatory liabilities</td>
<td>1,150</td>
<td>90</td>
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<tr>
<td>(note 4)</td>
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<td></td>
</tr>
<tr>
<td>Current portion of accrued</td>
<td>800</td>
<td>800</td>
</tr>
<tr>
<td>employee future benefits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current portion of obligation</td>
<td>28</td>
<td>26</td>
</tr>
<tr>
<td>of obligation under capital</td>
<td></td>
<td></td>
</tr>
<tr>
<td>lease</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>182,591</td>
<td>170,402</td>
</tr>
<tr>
<td>Accrued employee future</td>
<td>13,265</td>
<td>13,755</td>
</tr>
<tr>
<td>benefits (note 6)</td>
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<td></td>
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<tr>
<td>Derivative liabilities</td>
<td>1,488</td>
<td>2,831</td>
</tr>
<tr>
<td>(note 5)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long-term debt (note 2)</td>
<td>740,888</td>
<td>749,628</td>
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<tr>
<td>Obligation under capital</td>
<td>91</td>
<td>112</td>
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<tr>
<td>lease</td>
<td></td>
<td></td>
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<tr>
<td>Other long-term liabilities</td>
<td>75</td>
<td>-</td>
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<tr>
<td></td>
<td>938,398</td>
<td>936,728</td>
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<td>Shareholders’ equity:</td>
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<tr>
<td>Share capital</td>
<td>75,478</td>
<td>75,478</td>
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<tr>
<td>Retained earnings</td>
<td>271,710</td>
<td>203,569</td>
</tr>
<tr>
<td></td>
<td>347,188</td>
<td>279,047</td>
</tr>
<tr>
<td>Commitments (note 3)</td>
<td></td>
<td></td>
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<tr>
<td>Subsequent event (note 10)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>$ 1,285,586</td>
<td>$ 1,215,775</td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.

On behalf of the Board:

[Signature]

Director

[Signature]

Director
BRITISH COLUMBIA FERRY SERVICES INC.
Consolidated Statements of Earnings, Comprehensive Income and Retained Earnings (unaudited)
(expressed in thousands)

<table>
<thead>
<tr>
<th></th>
<th>Three months ended December 31</th>
<th></th>
<th>Nine months ended December 31</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tariffs</td>
<td>$ 79,711</td>
<td>$ 75,233</td>
<td>$ 312,808</td>
<td>$ 295,860</td>
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<tr>
<td>Ferry service fees</td>
<td>26,855</td>
<td>25,703</td>
<td>94,892</td>
<td>84,276</td>
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<tr>
<td>Federal-Provincial Subsidy Agreement</td>
<td>6,464</td>
<td>6,327</td>
<td>19,392</td>
<td>18,982</td>
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<tr>
<td>Retail</td>
<td>17,067</td>
<td>15,916</td>
<td>64,673</td>
<td>58,893</td>
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<tr>
<td>Other income</td>
<td>6,463</td>
<td>5,360</td>
<td>24,720</td>
<td>19,815</td>
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<tr>
<td></td>
<td>136,560</td>
<td>128,539</td>
<td>516,485</td>
<td>477,826</td>
</tr>
<tr>
<td>Expenses:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operations</td>
<td>77,826</td>
<td>72,558</td>
<td>250,709</td>
<td>231,530</td>
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<tr>
<td>Maintenance</td>
<td>23,482</td>
<td>21,863</td>
<td>65,641</td>
<td>53,104</td>
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<td>Administration</td>
<td>12,524</td>
<td>11,459</td>
<td>36,098</td>
<td>33,889</td>
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<td>Cost of retail goods sold</td>
<td>6,551</td>
<td>6,349</td>
<td>23,998</td>
<td>22,865</td>
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<td>Amortization</td>
<td>16,538</td>
<td>13,748</td>
<td>48,930</td>
<td>40,371</td>
</tr>
<tr>
<td></td>
<td>136,921</td>
<td>125,967</td>
<td>425,376</td>
<td>381,759</td>
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<tr>
<td>(Loss) earnings from operations</td>
<td>(361)</td>
<td>2,572</td>
<td>91,109</td>
<td>96,067</td>
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<tr>
<td>Gain on foreign exchange</td>
<td>2</td>
<td>29</td>
<td>152</td>
<td>266</td>
</tr>
<tr>
<td>Interest expense (note 7)</td>
<td>(7,336)</td>
<td>(4,454)</td>
<td>(23,410)</td>
<td>(14,331)</td>
</tr>
<tr>
<td>(Loss) gain on disposal of capital assets</td>
<td>(68)</td>
<td>13</td>
<td>(188)</td>
<td>(7)</td>
</tr>
<tr>
<td>Net (loss) earnings before extraordinary gain</td>
<td>(7,763)</td>
<td>(1,840)</td>
<td>67,663</td>
<td>81,995</td>
</tr>
<tr>
<td>Extraordinary gain (note 8)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>61,272</td>
</tr>
<tr>
<td>Net (loss) earnings</td>
<td>(7,763)</td>
<td>(1,840)</td>
<td>67,663</td>
<td>143,267</td>
</tr>
<tr>
<td>Other comprehensive income (note 1(c))</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Net (loss) earnings and comprehensive income</td>
<td>(7,763)</td>
<td>(1,840)</td>
<td>67,663</td>
<td>143,267</td>
</tr>
<tr>
<td>Retained earnings, beginning of period</td>
<td>279,473</td>
<td>244,657</td>
<td>203,569</td>
<td>99,550</td>
</tr>
<tr>
<td>Adjustment to retained earnings (note 1(c))</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>478</td>
</tr>
<tr>
<td>Restated balance, beginning of period</td>
<td>279,473</td>
<td>244,657</td>
<td>204,047</td>
<td>99,550</td>
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<tr>
<td>Retained earnings, end of period</td>
<td>$ 271,710</td>
<td>$ 242,817</td>
<td>$ 271,710</td>
<td>$ 242,817</td>
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See accompanying notes to consolidated financial statements.
BRITISH COLUMBIA FERRY SERVICES INC.
Consolidated Statements of Cash Flows (unaudited)
(expressed in thousands)

<table>
<thead>
<tr>
<th></th>
<th>Three months ended</th>
<th></th>
<th>Nine months ended</th>
<th></th>
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<tr>
<td></td>
<td>December 31</td>
<td>2007</td>
<td>December 31</td>
<td>2006</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2006</td>
<td></td>
<td></td>
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<td>Cash provided by (used in):</td>
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<td>Operations:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net (loss) earnings before</td>
<td>$ (7,763)</td>
<td>$ (1,840)</td>
<td>$ 67,663</td>
<td>$ 81,995</td>
</tr>
<tr>
<td>extraordinary gain</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Extraordinary gain (note 8)</td>
<td>-</td>
<td>-</td>
<td></td>
<td>61,272</td>
</tr>
<tr>
<td>Net (loss) earnings</td>
<td>(7,763)</td>
<td>(1,840)</td>
<td>67,663</td>
<td>143,267</td>
</tr>
<tr>
<td>Items not involving cash:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Amortization</td>
<td>16,538</td>
<td>13,748</td>
<td>48,930</td>
<td>40,371</td>
</tr>
<tr>
<td>Other non-cash charges</td>
<td>476</td>
<td>(395)</td>
<td>761</td>
<td>114</td>
</tr>
<tr>
<td>Regulatory costs deferred</td>
<td>4,390</td>
<td>(616)</td>
<td>9,657</td>
<td>(3,048)</td>
</tr>
<tr>
<td>Change in operating working</td>
<td>5,496</td>
<td>15,670</td>
<td>(8,069)</td>
<td>(25,382)</td>
</tr>
<tr>
<td>capital</td>
<td></td>
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<td></td>
</tr>
<tr>
<td></td>
<td>19,137</td>
<td>26,567</td>
<td>118,942</td>
<td>155,322</td>
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<td>Financing:</td>
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<tr>
<td>Deferred financing costs incurred</td>
<td>(95)</td>
<td>(79)</td>
<td>(255)</td>
<td>(239)</td>
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<td>Amounts drawn from credit</td>
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<td>41,515</td>
<td>15,128</td>
<td>41,515</td>
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<td>facility (note 2)</td>
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<tr>
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<td>39,741</td>
<td>41,436</td>
<td>14,873</td>
<td>41,276</td>
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<td>Investing:</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>(Costs of) proceeds from</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>disposal of capital assets</td>
<td>(39)</td>
<td>12</td>
<td>(14)</td>
<td>28</td>
</tr>
<tr>
<td>Purchase of capital assets</td>
<td>(167,135)</td>
<td>(102,498)</td>
<td>(274,968)</td>
<td>(176,849)</td>
</tr>
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<td>Purchase of short-term</td>
<td>(32)</td>
<td>-</td>
<td>(11,198)</td>
<td>-</td>
</tr>
<tr>
<td>investments</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in lands under long-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(60)</td>
</tr>
<tr>
<td>term lease</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(167,206)</td>
<td>(102,498)</td>
<td>(286,180)</td>
<td>(176,881)</td>
</tr>
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<td>(Decrease) increase in cash</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>and cash equivalents</td>
<td>(108,328)</td>
<td>(34,483)</td>
<td>(152,365)</td>
<td>19,717</td>
</tr>
<tr>
<td>Cash and cash equivalents,</td>
<td>136,086</td>
<td>56,491</td>
<td>180,123</td>
<td>2,291</td>
</tr>
<tr>
<td>beginning of period</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents, end</td>
<td>$ 27,758</td>
<td>$ 22,008</td>
<td>$ 27,758</td>
<td>$ 22,008</td>
</tr>
<tr>
<td>of period</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supplemental cash flow</td>
<td></td>
<td></td>
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<tr>
<td>information:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash paid during the period for</td>
<td>$ 15,135</td>
<td>$ 15,167</td>
<td>$ 36,581</td>
<td>$ 30,429</td>
</tr>
<tr>
<td>interest</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

See accompanying notes to consolidated financial statements.
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 interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the fiscal year ended March 31, 2007 except as disclosed below. The disclosures provided below are incremental to those included with the annual consolidated financial statements. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto for the year ended March 31, 2007.

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 travelers and their preference to 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. Significant accounting policies:

   (a) Basis of presentation:


   (b) Comparative figures:

       Certain comparative figures have been reclassified to conform to the presentation adopted for the current period.

   (c) Changes in accounting policies:

       Effective April 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Sections 1530 "Comprehensive Income", 3251 "Equity", 3855 "Financial Instruments – Recognition and Measurement", 3861 "Financial Instruments – Disclosure and Presentation", and 3865 "Hedges". These new Handbook Sections provide comprehensive requirements for the recognition and measurement of financial instruments, as well as standards on when and how hedge accounting may be applied. Handbook Section 1530 also establishes standards for reporting and displaying comprehensive income. Comprehensive income is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income but that are excluded from net income calculated in accordance with generally accepted accounting principles.
1. Significant accounting policies (continued):
   (c) Changes in accounting policies (continued):

   Under these new standards, all financial instruments are classified into one of the following five categories: held for trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities.

   All financial instruments, including derivatives, are included on the consolidated balance sheet and are initially measured at fair value. Subsequent measurement and recognition of changes in fair value of financial instruments depends on their initial classification. Held for trading financial instruments are measured at fair value and all gains and losses are included in net income in the period in which they arise. Available-for-sale financial instruments are measured at fair value with revaluation gains and losses included in other comprehensive income until the asset is removed from the balance sheet. Loans and receivables, investments held-to-maturity and other financial liabilities are measured at amortized cost.

   The standards require derivative instruments to be recorded as either assets or liabilities measured at their fair value unless exempted from derivative treatment as a normal purchase and sale. Certain derivatives embedded in other contracts must also be measured at fair value. All changes in the fair value of derivatives are recognized in earnings unless specific hedge criteria are met, which requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting.

   The adoption of these standards has the following effect on the consolidated financial statements for the nine months ended December 31, 2007:

   (1) Recognition of foreign currency forward contracts as derivative assets and liabilities in the consolidated financial statements (note 5);

   (2) Restatement of opening retained earnings at April 1, 2007 to recognize the prior years' earnings effect of accounting for long-term debt using the effective interest method; and

   (3) Reclassification of deferred financing costs to long-term debt (note 2).

   The Company also de-designated all previously designated hedges on June 30, 2007 under Section 3855 – "Hedges". All of these hedges, which were entered into to provide greater certainty of the cost of new vessel acquisitions denominated in foreign currencies, were effective at the time of de-designation. All hedges are recorded at fair value with unrealized gains and losses recorded to the regulatory asset or liability accounts on the balance sheet.

   The Company has no embedded derivatives that meet the requirements of Section 3855 which would require that they be separated from host contracts and valued separately at fair value.

   The Company has not recognized any adjustments through other comprehensive income for the three and nine months ended December 31, 2007.
BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
For the nine months ended December 31, 2007 and 2006

(columnar dollars expressed in thousands)

1. Significant accounting policies (continued):

   (c) Changes in accounting policies (continued):

   The adoption of these sections is done prospectively without restatement of the consolidated financial statements of prior periods. As at April 1, 2007, the impact on the consolidated financial statements of recording foreign currency forward contracts as derivative assets and liabilities, measuring the long-term debt using the effective interest rate method and reclassifying the deferred financing costs directly attributable to the issuance of the long-term debt is summarized in the table below:

<table>
<thead>
<tr>
<th></th>
<th>April 1, 2007</th>
<th>March 31, 2007</th>
<th>Net Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Derivative assets</td>
<td>$ 8,625</td>
<td>$ -</td>
<td>$ 8,625</td>
</tr>
<tr>
<td>Other assets - deferred financing costs</td>
<td>1,017</td>
<td>9,580</td>
<td>(9,563)</td>
</tr>
<tr>
<td>Derivative liabilities</td>
<td>18,677</td>
<td>2,831</td>
<td>15,846</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>740,587</td>
<td>749,628</td>
<td>(9,041)</td>
</tr>
<tr>
<td>Retained earnings</td>
<td>204,047</td>
<td>203,569</td>
<td>478</td>
</tr>
</tbody>
</table>

   In the table above, the remaining balance of deferred financing costs at April 1, 2007 represent costs incurred for long-term debt arranged for but not yet issued.

   (d) Future accounting changes:

   The following Handbook Sections have not yet been adopted by the Company:

   Section 3031 "Inventory" replaces Section 3030 and becomes effective for the Company beginning April 1, 2008. This section provides guidance on the determination of inventory cost, subsequent recognition as expense, and write-downs to net realizable value. The Company does not expect application of this section to have a significant impact on the consolidated financial statements.

   Section 1535 "Capital Disclosures" becomes effective for the Company beginning April 1, 2008. This section establishes standards for disclosing information about the Company's capital and how it is managed. The standard requires disclosures of the Company's objectives, policies and processes for managing capital, the quantitative data about what the Company regards as capital, whether the Company has complied with any capital requirements and if it has not complied, the consequences of such non-compliance. The Company does not expect application of this section to have a significant impact on the consolidated financial statements.

   Section 3862 "Financial Instruments – Disclosure" becomes effective for the Company beginning April 1, 2008. This section requires disclosures, by class of financial instrument, which will enable users to evaluate the significance of financial instruments for the Company's financial position and performance, including disclosures about fair value.
1. Significant accounting policies (continued):

   d) Future accounting changes (continued):

   In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk, and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of financial market risk to which an entity is exposed, showing how net earnings and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. The Company does not expect application of this section to have a significant impact on the consolidated financial statements.

   Section 3863 "Financial Instruments – Presentation" becomes effective for the Company beginning April 1, 2008. Under this new section, the existing requirements on presentation of financial instruments are carried forward unchanged, and accordingly, the Company does not expect application of this section to have any impact on the consolidated financial statements.

   Amendments to Sections 1100 "Generally Accepted Accounting Principles", 3465 "Income Taxes" and Accounting Guideline AcG-19 "Disclosures by Entities Subject to Rate Regulation" become effective for the Company April 1, 2009 and are to be applied prospectively. With release of these amendments, a temporary exemption that permitted assets and liabilities arising from rate regulation to be recognized and measured on a basis other than in accordance with the primary sources of generally accepted accounting principles will be removed. In addition, accounting recommendations have been amended to require the recognition of future income tax liabilities and assets as well as offsetting regulatory assets and liabilities at entities subject to rate regulation. The Company does not expect application of these amendments to have any impact on the consolidated financial statements. The Company is continuing to monitor any additional implications on its financial reporting related to accounting for rate regulated operations.

2. Loans:

   (a) Bonds:

   The CICA recommendations regarding the measurement of financial liabilities require that they be measured at initial recognition using the effective interest method. Accordingly, deferred financing costs and unamortized bond discounts have been recalculated using the effective interest method. Commencing April 1, 2007, in accordance with CICA recommendations regarding the presentation of financial liabilities, long term debt has been reduced by the cumulative unamortized balance of deferred financing costs and unamortized bond discounts.
2. Loans (continued):

(a) Bonds (continued):

<table>
<thead>
<tr>
<th>Long-term debt</th>
<th>December 31 2007</th>
<th>March 31 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.74% Senior Secured Bonds, Series 04-1, due May 2014 (effective interest rate 5.921%)</td>
<td>$250,000</td>
<td>$250,000</td>
</tr>
<tr>
<td>6.25% Senior Secured Bonds, Series 04-4, due October 2034 (effective interest rate 6.411%)</td>
<td>250,000</td>
<td>250,000</td>
</tr>
<tr>
<td>5.021% Senior Secured Bonds, Series 07-1, due March 2037 (effective interest rate 5.062%)</td>
<td>250,000</td>
<td>250,000</td>
</tr>
<tr>
<td>Less: Deferred financing costs and unamortized bond discounts</td>
<td>(9,112)</td>
<td>(372)</td>
</tr>
<tr>
<td></td>
<td>$740,888</td>
<td>$749,628</td>
</tr>
</tbody>
</table>

(b) Credit facility:

During the quarter ended June 30, 2007, the Company negotiated an amendment agreement to the credit facility with a syndicate of Canadian banks, secured by pledged bonds. The facility makes available to the Company a five year revolving facility maturing May 12, 2012 in the amount of $155 million. The amendment includes a provision giving the Company, on an annual basis, an option to request a one year extension. Draws on this facility totaled $40.0 million as at December 31, 2007 (March 31, 2007: $25.0 million), and are shown as short-term debt at their discounted value of $39.9 million (March 31, 2007: $24.9 million). The effective interest rate on these borrowings was 5.02%. Interest expensed during the quarter ended December 31, 2007 was $0.1 million (December 31, 2006 – nil). Interest expensed during the nine months ended December 31, 2007 was $0.1 million (December 31, 2006 – nil).

(c) Debt service reserve:

The Company is required to maintain a debt service reserve for the Series 04-1, 04-4 and 07-1 bonds equal to not less than six months forecasted debt service, to be increased under certain conditions. As at December 31, 2007, debt service reserves of $21.3 million were invested in short-term investments. As at March 31, 2007, $14.1 million was invested in short-term investments and $7.2 million in cash equivalents.
3. Capital assets:

<table>
<thead>
<tr>
<th>December 31, 2007</th>
<th>Cost</th>
<th>Accumulated amortization</th>
<th>Net book value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vessels</td>
<td>$1,045,288</td>
<td>$552,991</td>
<td>$492,297</td>
</tr>
<tr>
<td>Berths, buildings and equipment</td>
<td>100,317</td>
<td>74,599</td>
<td>25,718</td>
</tr>
<tr>
<td>Berths, buildings and equipment</td>
<td>531,994</td>
<td>236,661</td>
<td>293,333</td>
</tr>
<tr>
<td>Land</td>
<td>1,406</td>
<td>-</td>
<td>1,406</td>
</tr>
<tr>
<td>Construction-in-progress</td>
<td>309,251</td>
<td>-</td>
<td>309,251</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$1,988,256</td>
<td>$866,251</td>
<td>$1,122,005</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>March 31, 2007</th>
<th>Cost</th>
<th>Accumulated amortization</th>
<th>Net book value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vessels</td>
<td>$1,006,968</td>
<td>$522,112</td>
<td>$484,856</td>
</tr>
<tr>
<td>Berths, buildings and equipment</td>
<td>102,894</td>
<td>70,273</td>
<td>32,621</td>
</tr>
<tr>
<td>Berths, buildings and equipment</td>
<td>488,098</td>
<td>225,414</td>
<td>262,684</td>
</tr>
<tr>
<td>Land</td>
<td>1,406</td>
<td>-</td>
<td>1,406</td>
</tr>
<tr>
<td>Construction-in-progress</td>
<td>137,257</td>
<td>-</td>
<td>137,257</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>$1,736,623</td>
<td>$817,799</td>
<td>$918,824</td>
</tr>
</tbody>
</table>

For the nine months ended December 31, 2007 capitalized financing costs during construction amounted to $6.5 million (December 31, 2006: $4.1 million).

In addition to the construction-in-progress referenced above, contractual commitments at December 31, 2007 for capital assets to be constructed totaled $382.7 million (March 31, 2007: $489.8 million). Included in the contractual commitments as at December 31, 2007 is $173.9 million (March 31, 2007: $293.5 million) committed for design and construction of three “Super C” Class vessels, $119.9 million (March 31, 2007: $126.5 million) for design and construction of a new vessel for use on the north coast, and $30.2 million (March 31, 2007: $36.3 million) committed to procure an intermediate class vessel. Delivery of the first of the “Super C” vessels occurred in December 2007 while delivery of the remaining two is scheduled to occur in mid 2008. Delivery of the intermediate class vessel and the new north coast vessel is scheduled to occur in mid 2008 and mid 2009 respectively.

4. Financial statement effect of rate regulation:

The Company is regulated by the Commissioner to ensure that tariffs are fair and reasonable and to monitor service levels. Under the terms of the Coastal Ferry Act, the tariffs the Company charges its customers are subject to price caps. Annual increases in price caps have been set for the first five year term through March 31, 2008. The Commissioner may, under certain circumstances, allow increases in price caps over the set levels. The Commissioner has set price
4. Financial statement effect of rate regulation (continued):

caps for the second four year term through March 31, 2012 and will establish the price caps to apply for each subsequent term.

The accounting for regulated operations of the Company may differ from non-regulated businesses following Canadian generally accepted accounting principles (GAAP). As a result, the Company records assets and liabilities that result from the regulated price cap setting process that would not be recorded under GAAP for non-regulated entities. Regulatory assets generally represent incurred costs that have been deferred because they are probable of future recovery in tariffs. Regulatory liabilities represent obligations to customers which will be settled through future tariffs. Management continually assesses whether the regulatory assets are probable of future recovery by considering factors such as applicable regulatory changes and believes the existing regulatory assets are probable of recovery. This determination reflects the current regulatory climate, and is subject to change in the future. If future recovery of costs ceases to be probable, asset write-offs would be required to be recognized in the current period earnings at that time.

Accounting for the impacts of rate regulation has resulted in recording the following regulatory assets and liabilities in the consolidated balance sheets:

<table>
<thead>
<tr>
<th>Regulatory assets – Current</th>
<th>December 31 2007</th>
<th>March 31 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred fuel costs (a)</td>
<td>$ 3,469</td>
<td>$ -</td>
</tr>
<tr>
<td>Performance term submission costs (b)</td>
<td>112</td>
<td>-</td>
</tr>
<tr>
<td>Total current regulatory assets</td>
<td>$ 3,581</td>
<td>$ -</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Regulatory assets – Long Term</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred fuel costs (a)</td>
<td>$ 9,209</td>
<td>$ 18,819</td>
</tr>
<tr>
<td>Performance term submission costs (b)</td>
<td>486</td>
<td>532</td>
</tr>
<tr>
<td>Hedge losses – vessel construction contracts (c)</td>
<td>27,368</td>
<td>2,370</td>
</tr>
<tr>
<td>Total long-term regulatory assets</td>
<td>$ 37,063</td>
<td>$ 21,721</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Regulatory liabilities</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Tariffs in excess of price cap (d) - current</td>
<td>$ 1,150</td>
<td>$ 90</td>
</tr>
</tbody>
</table>

(a) Deferred fuel costs:

As prescribed by regulatory order, the Company defers fuel costs in excess of approved fuel costs which were used to develop the regulated price caps. The difference between the approved fuel costs and the actual fuel costs (including fuel hedge gains and losses) is deferred for recovery from future tariffs.
4. Financial statement effect of rate regulation (continued):

(a) Deferred fuel costs (continued):

The order also allows interest to be calculated on outstanding deferred fuel cost balances and included in the amount to be recovered. Also prescribed by regulatory order, the Company collects fuel surcharges which are applied against deferred fuel costs. The Commissioner has considered deferred fuel costs in the determination of the price caps set for the four years beginning April 1, 2008 and it is expected that recovery will occur over this four year period. If the Company was not a regulated entity, earnings for the quarter ended December 31, 2007 would have been $0.8 million higher (December 31, 2006: $0.5 million lower), and earnings for the nine months ended December 31, 2007 would have been $6.1 million higher (December 31, 2006: $3.3 million lower), except for this deferral.

(b) Performance term submission costs:

The Commissioner has authorized the Company to defer costs of representation associated with the second performance term. The Commissioner has considered these costs in the determination of the price caps set for the four years beginning April 1, 2008. The Commissioner has not included an allowance for a return on investment for this item. It is expected that the recovery period will be the four year period of the second performance term, commencing April 1, 2008.

If the Company was not a regulated entity, earnings for the quarter ended December 31, 2007 would have been unchanged (December 31, 2006 – $0.1 million lower); and earnings for the nine months ended December 31, 2007 would have been $0.1 million lower (December 31, 2006 – $0.2 million lower), except for this deferral.

(c) Hedge gains or losses – vessel construction contracts:

The Company defers gains or losses on financial derivative instruments which have been entered into to manage market risk against fluctuations in the Canadian dollar equivalent of vessel construction contracts denominated in foreign currencies. The intent and effect of these transactions is to provide greater certainty of the cost of the related new vessel acquisitions. The total cost of these assets, including hedge gains or losses, has been determined by the Commissioner to be reasonable and will be taken into account in the determination of price caps set for the periods following the entry of these assets into service. It is expected that the settlement or recovery period of hedge gains or losses is five to forty years. If the Company was not a regulated entity, earnings for the quarter ended December 31, 2007 would have been $25.7 million higher (December 31, 2006: $0.9 million higher), and earnings for the nine months ended December 31, 2007 would have been $25.0 million lower (December 31, 2006: $2.4 million lower), except for this deferral.

(d) Tariffs in excess of price cap:

The Act contains provisions which ensure that if tariffs charged by the Company exceed established price caps, the excess amounts collected will be returned to customers through future tariffs.

Tariffs charged to customers on the Bear Cove – Mid Coast route group exceeded the price cap by $0.2 million at December 31, 2007 (March 31, 2007: $0.1 million) and is expected to
BRITISH COLUMBIA FERRY SERVICES INC.
Notes to Consolidated Financial Statements (unaudited)
For the nine months ended December 31, 2007 and 2006
(columnar dollars expressed in thousands)

4. Financial statement effect of rate regulation (continued):
   (d) Tariffs in excess of price cap (continued):

   be settled April 1, 2008 with the commencement of performance term two and the
   amalgamation of this route group into the new northern route group.

   Tariffs charged to customers in excess of established price caps for the third quarter ended
   December 31, 2007 totaled $0.1 million on the minor route group and $0.9 million on the
   major route group. The excess amounts from the minor route group are expected to be
   returned to customers through tariffs during the quarter ending March 31, 2008. The excess
   amounts on the major route group are expected to be returned to customers through tariffs
   during the quarter ending June 30, 2008.

   In the absence of rate regulated accounting, GAAP would require these revenues to be
   recognized as income in the period collected, and earnings for the quarter ended December
   31, 2007 would have been $1.0 million higher (December 31, 2006: $0.2 million lower), and
   earnings for the nine months ended December 31, 2007 would have been $1.1 million higher
   (December 31, 2006: $0.9 million lower), except for this deferral.

5. Derivative liabilities:

   The fair value as at December 31, 2007 of financial derivative liabilities for foreign currency
   hedges is $27.8 million (March 31, 2007: $2.8 million).

6. Accrued employee future benefits:

   During the quarter ended December 31, 2007 the Company recognized total defined benefit
   costs of $0.3 million (December 31, 2006 - $0.3 million).

   During the nine months ended December 31, 2007 the Company recognized total defined benefit
   costs of $0.9 million (December 31, 2006 - $0.9 million).

7. Interest rate support:

   The Government of Canada has agreed to provide $9.9 million in the form of interest rate support
   to the Company for major refinements on three vessels (March 31, 2007: $9.9 million). Of this
   amount, $7.6 million has been previously recorded in periods prior to March 31, 2007 as either a
   reduction of capitalized interest or as a reduction of interest expense. During the quarter ended
   December 31, 2007, $0.5 million has been recorded as a reduction of interest expense
   (December 31, 2006 - $1.2 million as a reduction of interest expense and $0.5 million as a
   reduction of capitalized interest). For the nine months ended December 31, 2007, $2.1 million
   has been recorded as a reduction of interest expense (December 31, 2006 - $3.8 million as a
   reduction of interest expense and $0.5 million as a reduction of capitalized interest). At December
   31, 2007 all interest rate support pursuant to these agreements has been recognized. The
   Company has no requirement to repay these funds, other than as a result of an event of default
   under the agreement with the Government of Canada.
8. Extraordinary gain:

On March 22, 2006 the vessel Queen of the North ran aground and subsequently sank. During the period ended June 30, 2006, the Company settled with its hull and machinery insurance providers. The Company has received insurance proceeds, net of deductible, of $67.9 million in settlement of the claim under the hull and machinery policy. At March 31, 2006, $6.6 million of the proceeds from this claim had been recognized to offset insurable losses (including $4.3 million net book value of capital assets) incurred as a result of this event.

9. Related party transactions:

In accordance with the Coastal Ferry Act, the Company is responsible for paying all expenses that are incurred by its parent, B.C. Ferry Authority (BCFA). During the nine months ended December 31, 2007 the Company paid $32,358 (December 31, 2006: $14,437) of such expenses.

The Province of British Columbia owns the Company's 75,477 non-voting preferred shares, but has no voting interest in either the Company or its parent, BCFA.

10. Subsequent Event:

On January 11, 2008 the Company issued $200 million of 5.581% Senior Secured Bonds, Series 08-1, due January 2038. The Company has established a debt service reserve for these bonds equal to six months of forecasted debt service (total of $5.6 million) and invested it in cash equivalents.