Consolidated Financial Statements of

BRITISH COLUMBIA FERRY SERVICES INC.

Three months ended June 30, 2011 and 2010

(unaudited)

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Balance Sheets
(expressed in thousands)

	June 30, 2011 (unaudited)	March 31, 2011
Assets		
Current assets:		
Cash and cash equivalents	$ 9,897	$ 33,335
Restricted short-term investments (note 2(b))	37,040	37,040
Other short-term investments	59,074	64,074
Accounts receivable	23,253	20,619
Prepaid expenses	15,893	5,648
Inventories	20,853	19,957
Regulatory assets (note 3)	3,581	3,703
	169,591	184,376
Property, plant and equipment (note 4)	1,577,309	1,581,007
Intangible assets (note 5)	35,796	34,929
Long-term loan receivable	24,515	24,247
Long-term land lease	32,865	32,979
	$ 1,840,076	$ 1,857,538
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 43,493	$ 51,249
Short-term debt (note 2(a))	-	3,949
Interest payable on long-term debt	15,115	18,261
Accrued employee costs	49,164	48,194
Deferred revenue	19,095	15,596
Derivative liabilities	11	23
Current portion of long-term debt (note 2)	24,000	22,125
Current portion of accrued employee future benefits	1,200	1,200
Current portion of obligations under capital lease	1,014	1,040
	153,092	161,637
Accrued employee future benefits	11,534	10,907
Regulatory liabilities (note 3)	1,017	1,558
Long-term debt (note 2)	1,323,504	1,327,014
Obligations under capital lease	47,739	47,723
	1,536,886	1,548,839
Shareholders' equity:		
Share capital	75,478	75,478
Retained earnings	227,712	233,221
	303,190	308,699
Commitments (note 4)		
	$ 1,840,076	$ 1,857,538

See accompanying notes to consolidated financial statements.

On behalf of the Board:

"Elizabeth J. Harrison"	*"Brian G. Kenning"*
Director	Director

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of (Loss) Earnings, Comprehensive (Loss) Income and Retained Earnings
(unaudited)
(expressed in thousands)

	For the three months ended June 30, 2011	June 30, 2010
Revenue:		
Tariffs	$ 115,473	$ 118,212
Ferry service fees	39,411	38,531
Federal-Provincial Subsidy Agreement	6,872	6,731
Retail	19,399	20,090
Other income	5,530	6,675
	186,685	190,239
Expenses:		
Operations	105,038	103,617
Maintenance	25,026	23,851
Administration	7,357	7,517
Cost of retail goods sold	7,463	7,680
Amortization	29,394	28,688
	174,278	171,353
Earnings from operations	12,407	18,886
Gain on foreign exchange	21	75
Interest expense	(17,966)	(18,028)
Gain (loss) on disposal of capital assets	29	(14)
Net (loss) earnings	(5,509)	919
Other comprehensive income (note 1(d))	-	-
Net (loss) earnings and comprehensive (loss) income	(5,509)	919
Retained earnings, beginning of period	233,221	235,478
Retained earnings, end of period	$ 227,712	$ 236,397

See accompanying notes to consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Cash Flows (unaudited)
(expressed in thousands)

	For the three months ended	
	June 30, 2011	June 30, 2010
Cash provided by (used in):		
Operations:		
Net (loss) earnings	$ (5,509)	$ 919
Items not involving cash:		
Amortization	29,394	28,688
Other non-cash charges	984	389
Long-term regulatory costs deferred	(541)	(2,349)
Change in non-cash operating working capital (note 9)	(18,584)	(11,302)
	5,744	16,345
Financing:		
Repayment of long-term debt	(1.875)	-
Repayment of short-term loans	(3,949)	-
Repayment of capital lease obligations	(276)	(111)
	(6,100)	(111)
Investing:		
Proceeds from disposal of property, plant and equipment	29	26
Purchase of property, plant and equipment and intangible assets	(27,843)	(20,639)
Advancement of long-term loan	(268)	-
Proceeds from (purchase of) short-term investments	5,000	(162)
	(23,082)	(20,775)
Decrease in cash and cash equivalents	(23,438)	(4,541)
Cash and cash equivalents, beginning of period	33,335	10,608
Cash and cash equivalents, end of period	$ 9,897	$ 6,067

Supplemental cash flow information (note 9)

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, 2011 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, 2011.

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 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:

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Pacific Marine Leasing Inc. ("PML"), BCF Captive Insurance Company Ltd. ("BCF Captive"), Pacific Marine Ventures Inc. ("PMV"), and BCF Global Services Inc. ("Global"). All inter-company balances and transactions have been eliminated on consolidation.

(b) Inventories:

Inventories, which consist of materials and supplies, catering stores and fuel, are valued at the lower of weighted-average cost and net realizable value.

(c) Embedded derivatives:

As at June 30, 2011, 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.

(d) Comprehensive income:

The Company has not recognized any adjustments through other comprehensive income for the three months ended June 30, 2011.

(e) Financial instruments - loans and receivables:

The long-term loan receivable has been classified under loans and receivables which are initially measured at fair value and are subsequently measured at amortized cost.

1. Significant accounting policies (continued):

(f) Future accounting changes:

International Financial Reporting Standards ("IFRS"):

The Company's changeover date for the conversion to IFRS was originally April 1, 2011. The Canadian Accounting Standards Board ("AcSB") has amended Part 1 of the CICA Handbook – Accounting to require:

- Qualifying entities with rate-regulated activities to adopt IFRSs for the first time no later than annual periods beginning on or after January 1, 2012; and
- Entities electing to defer the first-time adoption of IFRSs to disclose the fact.

The Canadian Securities Administrators' regulations have also been amended to incorporate the AcSB's one-year deferral option. The Company has elected this option which defers the changeover date for conversion to IFRS to April 1, 2012.

Transition to IFRS will require the restatement for comparative purposes of amounts reported by the Company for the year prior to the changeover date. While the Company is continuing to assess the adoption of IFRS, the financial reporting impact of the transition cannot be reasonably estimated at this time.

The areas that have the highest potential to significantly impact the Company are rate-regulated operations; property plant and equipment; intangible assets and asset impairment; and initial adoption of IFRS under the provisions of IFRS 1 "*First-Time Adoption of IFRS"*. The Company is monitoring any International Accounting Standards Board ("IASB") initiatives with the potential to impact rate-regulated accounting under IFRS.

The IASB published an amendment to IFRS 1 on May 6, 2010 which provides an exemption for property, plant and equipment and intangible assets used in operations subject to rate regulation. A first-time adopter may elect to use, on an item by item basis, the previous GAAP carrying amount of such items as deemed cost at the date of transition to IFRS. The Company has assessed the impact of the options available as a result of this IFRS 1 amendment and has decided to adopt the exemption for all its intangible assets and the majority of its items of property, plant and equipment. The Company has chosen the revaluation method for its land assets, which will result in a $12.2 million increase in the value of these assets at its transition date of April 1, 2011.

IFRS 1 First-Time Adoption of IFRS allows a choice to either recognize all cumulative actuarial gains and losses of defined benefit plans through opening retained earnings or recalculate the actuarial gains and losses under IFRS from the inception of the defined benefit plans. The Company has elected to recognize all cumulative actuarial gains and losses through opening retained earnings at April 1, 2011. The actuarial loss to be recognized in opening retained earnings is $3.3 million.

1. Significant accounting policies (continued):

(f) Future accounting changes (continued):

International Financial Reporting Standards ("IFRS") (continued):

In September 2010, the IASB staff released Agenda Paper 12 on rate-regulated activities. In the staff's opinion, while the impact of regulators may have an economic impact on entities subject to rate-regulation:

- Regulatory assets do not meet the definition of a financial asset nor the definition of an intangible asset as specified in IAS 38; and
- Regulatory liabilities do not meet the definition of a financial liability nor the definition of a provision as specified in IAS 37.

The IASB has closed the current project on rate-regulated activities and plans to consult constituents in 2011 on whether issues relating to rate-regulated activities should be considered in a new project in its post-2011 agenda.

The Company expects that issues regarding rate-regulated activities will remain unresolved for some time and that regulatory assets or liabilities will not be reported on the IFRS Statement of Financial Position. Accordingly, current regulatory assets of $3.7 million and long-term regulatory liabilities of $1.6 million will be derecognized on the Company's transition date of April 1, 2011 with a net reduction in retained earnings of $2.1 million. As future balances of its regulatory accounts are unknown, the Company cannot reasonably estimate and conclude the impact on future financial position and results of operations with respect to accounting for rate-regulated activities.

(columnar dollars expressed in thousands)

2. Loans:

Long-term debt:		June 30 2011		March 31 2011
5.74% Senior Secured Bonds, Series 04-1, due May 2014 (effective interest rate 5.92%)	$	250,000	$	250,000
6.25% Senior Secured Bonds, Series 04-4, due October 2034 (effective interest rate 6.41%)		250,000		250,000
5.02% Senior Secured Bonds, Series 07-1, due March 2037 (effective interest rate 5.06%)		250,000		250,000
5.58% Senior Secured Bonds, Series 08-1, due January 2038 (effective interest rate 5.62%)		200,000		200,000
6.21% Senior Secured Bonds, Series 08-2, due December 2013 (effective interest rate 6.33%)		140,000		140,000
12 Year Loan, maturing March 2020				
Tranche A (effective interest rate 5.17%)		65,625		67,500
Tranche B (floating interest rate of 1.40% at June 30, 2011)		22,500		22,500
12 Year Loan, maturing June 2020				
Tranche A (effective interest rate 5.18%)		67,500		69,375
Tranche B (floating interest rate of 1.38% at June 30, 2011)		22,500		20,625
2.95% Loan, maturing January 2021 (effective interest rate 3.08%)		90,000		90,000
		1,358,125		1,360,000
Less: Deferred financing costs and unamortized bond discounts		(10,621)		(10,861)
Current portion		(24,000)		(22,125)
	$	1,323,504	$	1,327,014

(a) Credit facility:

There were no draws on the $155 million credit facility as at June 30, 2011 and draws on this facility totalled $3.9 million as at March 31, 2011. Interest expensed during the three months ended June 30, 2011 was $0.1 million (June 30, 2010: $0.1 million). Letters of credit outstanding against this facility at June 30, 2011 totalled $0.1 million (March 31, 2011: $0.2 million).

(columnar dollars expressed in thousands)

2. Loans (continued):

(b) Debt service reserves:

The Company is required to maintain debt service reserves for the Series 04-1, 04-4, 07-1, 08-1 and 08-2 bonds equal to not less than six months forecasted debt service, to be increased under certain conditions. Further debt service reserves are required to be maintained for the 12 year loans and the 2.95% loans equal to not less than six months forecasted debt service, to be increased under certain conditions.

As at June 30, 2011, debt service reserves of $37.0 million (March 31, 2011: $37.0 million) were held in short-term investments and have been classified as restricted short-term investments on the balance sheet.

3. Financial statement effect of rate regulation:

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

Regulatory accounts	June 30 2011	March 31 2011
First performance term accounts:		
Balance at March 31, 2008:		
Deferred fuel costs	$ 18,501	$ 18,501
Performance term submission costs	600	600
	19,101	19,101
Accumulated amortization	(15,520)	(14,326)
Total of first performance term accounts	**3,581**	**4,775**
Second performance term accounts:		
Deferred fuel costs		
Balance – beginning of period	(1,790)	(9,185)
Fuel costs deferred (including realized hedge gains and losses)	3,603	849
(Surcharges) rebates granted	(1,155)	8,593
Fuel price risk recoveries from the Province	-	(196)
Other payments from the Province	(1,938)	(1,556)
Interest payable	(32)	(295)
Balance – end of period	(1,312)	(1,790)
Tariffs in excess of price cap (b)	-	(1,072)
Performance term submission costs	295	232
Total of second performance term accounts	**(1,017)**	**(2,630)**
Total regulatory assets	**2,564**	**2,145**
Current regulatory assets	**3,581**	**3,703**
Total long-term regulatory (liabilities)	**$ (1,017)**	**$ (1,558)**

(columnar dollars expressed in thousands)

3. Financial statement effect of rate regulation (continued):

(a) Amortization expense:

During the three months ended June 30, 2011 the Company recognized $1.2 million in amortization expense for first performance term accounts (June 30, 2010: $1.2 million).

(b) Tariffs in excess of price cap:

The *Coastal Ferry Act* (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. At June 30, 2011 tariffs charged to customers on all route groups were below established price caps and at March 31, 2011, tariffs charged to customers on the Major Route Group exceeded the price cap by $1.1 million.

If the Company was not a rate-regulated entity and did not record regulatory assets and liabilities, net earnings for the three months ended June 30, 2011, would have been $0.4 million lower (2010: $1.1 million lower) as detailed below:

Impact of regulatory accounts on net earnings	As at June 30, 2011	2010
First performance term accounts:		
Deferred fuel costs	$ (1,156)	$ (1,156)
Performance term submission costs	(38)	(38)
Second performance term accounts:		
Deferred fuel costs	478	2,356
Performance term submission costs	63	(7)
Tariffs in excess of price cap	1,072	-
Total increase in net earnings resulting from regulatory accounts	$ 419	$ 1,155
Unamortized training costs (note 5)	(46)	(38)
Total increase in net earnings	373	1,117

(columnar dollars expressed in thousands)

4. Property, plant and equipment:

June 30, 2011	Cost	Accumulated amortization	Net book value
Vessels	$ 1,710,105	$ 640,042	$ 1,070,063
Berths, buildings and equipment	90,027	51,561	38,466
Berths, buildings and equipment under capital lease	694,732	264,859	429,873
Land	914	-	914
Land under capital lease	5,177	-	5,177
Construction-in-progress	32,816	-	32,816
	$ 2,533,771	$ 956,462	$ 1,577,309

March 31, 2011	Cost	Accumulated amortization	Net book value
Vessels	$ 1,698,151	$ 620,758	$ 1,077,393
Berths, buildings and equipment	91,932	49,260	42,672
Berths, buildings and equipment under capital lease	686,128	259,789	426,339
Land	914	-	914
Land under capital lease	5,177	-	5,177
Construction-in-progress	28,512	-	28,512
	$ 2,510,814	$ 929,807	$ 1,581,007

Capitalized financing costs during construction for property, plant and equipment for the three months ended June 30, 2011 totalled $0.4 million (June 30, 2010: $0.5 million).

Amortization expense for assets under capital lease for the three months ended June 30, 2011 totalled $5.5 million (June 30, 2010: $4.7 million).

In addition to the construction-in-progress referenced above, the contractual commitments at June 30, 2011 for capital assets to be constructed, totalled $38.0 million (March 31, 2011: $48.7 million).

During the three months ended June 30, 2011, the Company received $0.3 million (June 30, 2010: $0.3 million) of rental income earned from buildings held for leasing purposes. These buildings have a cost and accumulated amortization of $13.5 million and $1.8 million respectively, as at June 30, 2011.

(columnar dollars expressed in thousands)

5. Intangible assets:

June 30, 2011		Cost		Accumulated amortization		Net book value
Acquired software, licenses and rights	$	37,352	$	20,732	$	16,620
Internally developed software and websites		26,297		16,178		10,119
Work-in-progress		9,057		-		9,057
	$	72,706	$	36,910	$	35,796

March 31, 2011		Cost		Accumulated amortization		Net book value
Acquired software, licenses and rights	$	36,476	$	19,767	$	16,709
Internally developed software and websites		23,920		15,652		8,268
Work-in-progress		9,952		-		9,952
	$	70,348	$	35,419	$	34,929

There was no impairment of intangible assets during the three months ended June 30, 2011 or the year ended March 31, 2011.

Capitalized financing costs during construction for intangible assets for the three months ended June 30, 2011 totalled $0.1 million (June 30, 2010: $0.1 million).

Included in the cost of intangible assets as at June 30, 2011 is $0.7 million of unamortized training costs (March 31, 2011: $0.8 million). If the Company was not a regulated entity, these training costs would be expensed in the period incurred.

During the three months ended June 30, 2011 intangible assets totaling $2.1 million (June 30, 2010: $5.2 million) were acquired and $0.3 million (June 30, 2010: $1.1 million) were internally developed. Amortization expense for the three months ended June 30, 2011 totalled $1.5 million (June 30, 2010: $1.1 million).

6. Accrued employee future benefits:

During the three months ended June 30, 2011 the Company recognized total defined benefit costs of $1.3 million (June 30, 2010: $0.3 million). This amount includes a cost of $1.0 million to reflect the actuarial valuation of the residual liability at March 31, 2011 for workers' compensation claims arising from the Workers' Compensation Board deposit class coverage system in which our predecessor entity participated prior to April 1, 2003. This actuarial valuation report was received June 15, 2011.

(columnar dollars expressed in thousands)

7. Interest rate support:

During the quarter ended June 30, 2011 the Government of Canada agreed to provide $1.3 million in the form of interest rate support to the Company for the major refurbishment of one vessel (during the year ended March 31, 2011: $1.0 million for the major refurbishment of one vessel). During the quarter ended June 30, 2011, interest rate support received and recorded as a reduction of interest expense totalled $0.5 million (June 30, 2010: $0.1 million) and $0.2 million (June 30, 2010: $nil) as a reduction of capitalized interest.

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. Related party transactions:

In accordance with the Act, the Company is responsible for paying any expenses that are incurred by its parent, B.C. Ferry Authority ("the Authority") without charge. During the three months ended June 30, 2011, the Company paid $32,807 (June 30, 2010: $nil) of such expenses.

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

9. Supplemental cash flow information:

	Three months ended June 30,	
(a) Changes in non-cash operating working capital:	2011	2010
Change in working capital		
Accounts receivable	$ (2,634)	$ 16
Prepaid expenses	(10,245)	(5,983)
Inventories	(896)	(145)
Regulatory assets	(1,072)	-
Accounts payable and accrued liabilities	(7,756)	2,200
Interest payable on long-term debt	(3,146)	(3,076)
Accrued employee costs	970	(1,093)
Deferred revenue	3,499	2,096
Change in non-cash working capital	(21,280)	(5,985)
Change attributable to capital asset acquisitions	2,696	(5,317)
Change in non-cash operating working capital	$ (18,584)	$ (11,302)
(b) Cash paid during the period for interest	$ 21,861	$ 21,367