

Consolidated Financial Statements of

BRITISH COLUMBIA FERRY SERVICES INC.

Nine months ended December 31, 2011 and 2010

(unaudited)

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Balance Sheets
(expressed in thousands)

| | December 31, 2011 (unaudited) | March 31, 2011 |
|---|----------------------------------|---------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 27,642 | \$ 33,335 |
| Restricted short-term investments (note 2(c)) | 35,774 | 37,040 |
| Other short-term investments | 26,880 | 64,074 |
| Accounts receivable | 17,514 | 20,619 |
| Prepaid expenses | 7,603 | 5,648 |
| Inventories | 20,478 | 19,957 |
| Regulatory assets (note 3) | 1,194 | 3,703 |
| | <u>137,085</u> | <u>184,376</u> |
| Property, plant and equipment (note 4) | 1,582,622 | 1,581,007 |
| Intangible assets (note 5) | 38,380 | 34,929 |
| Regulatory assets (note 3) | 997 | - |
| Long-term loan receivable | 24,515 | 24,247 |
| Long-term land lease | 32,635 | 32,979 |
| | <u>\$ 1,816,234</u> | <u>\$ 1,857,538</u> |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | \$ 39,625 | \$ 51,249 |
| Short-term debt (note 2(b)) | - | 3,949 |
| Interest payable on long-term debt | 15,324 | 18,261 |
| Accrued employee costs | 50,812 | 48,194 |
| Deferred revenue | 13,348 | 15,596 |
| Derivative liabilities | - | 23 |
| Current portion of long-term debt (note 2) | 9,000 | 22,125 |
| Current portion of accrued employee future benefits | 1,200 | 1,200 |
| Current portion of obligations under capital lease | 974 | 1,040 |
| | <u>130,283</u> | <u>161,637</u> |
| Accrued employee future benefits | 11,823 | 10,907 |
| Regulatory liabilities (note 3) | - | 1,558 |
| Long-term debt (note 2) | 1,289,491 | 1,327,014 |
| Obligations under capital lease | 47,258 | 47,723 |
| | <u>1,478,855</u> | <u>1,548,839</u> |
| Shareholders' equity: | | |
| Share capital | 75,478 | 75,478 |
| Retained earnings | 261,901 | 233,221 |
| | <u>337,379</u> | <u>308,699</u> |
| Commitments (note 4) | | |
| | <u>\$ 1,816,234</u> | <u>\$ 1,857,538</u> |

See accompanying notes to consolidated financial statements.

On behalf of the Board:

"Donald P. Hayes"
Director

"Brian G. Kenning"
Director

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Earnings, Comprehensive Income and Retained Earnings

(unaudited)

(expressed in thousands)

| | Three months ended December 31 | | Nine months ended December 31 | |
|--|-----------------------------------|------------|----------------------------------|------------|
| | 2011 | 2010 | 2011 | 2010 |
| Revenue: | | | | |
| Tariffs | \$ 98,601 | \$ 99,086 | \$ 376,060 | \$ 373,007 |
| Ferry service fees | 34,420 | 33,954 | 122,287 | 118,892 |
| Federal-Provincial Subsidy Agreement | 6,872 | 6,731 | 20,615 | 20,193 |
| Retail | 16,590 | 17,208 | 63,024 | 65,351 |
| Other income | 4,804 | 5,344 | 18,032 | 21,134 |
| | 161,287 | 162,323 | 600,018 | 598,577 |
| Expenses: | | | | |
| Operations | 97,902 | 96,676 | 317,493 | 315,201 |
| Maintenance | 23,932 | 26,815 | 63,142 | 63,289 |
| Administration | 6,818 | 7,531 | 22,624 | 22,365 |
| Cost of retail goods sold | 6,473 | 6,525 | 23,903 | 24,482 |
| Amortization | 31,305 | 28,059 | 90,229 | 85,188 |
| | 166,430 | 165,606 | 517,391 | 510,525 |
| (Loss) earnings from operations | (5,143) | (3,283) | 82,627 | 88,052 |
| Gain on foreign exchange | 37 | 67 | 214 | 173 |
| Interest expense | (17,953) | (18,367) | (54,173) | (54,354) |
| (Loss) gain on disposal of capital assets | (25) | 9,146 | 12 | 8,893 |
| Net (loss) earnings | (23,084) | (12,437) | 28,680 | 42,764 |
| Other comprehensive income (note 1 (d)) | - | - | - | - |
| Net (loss) earnings and comprehensive income | (23,084) | (12,437) | 28,680 | 42,764 |
| Retained earnings, beginning of period | 284,985 | 290,679 | 233,221 | 235,478 |
| Retained earnings, end of period | \$ 261,901 | \$ 278,242 | \$ 261,901 | \$ 278,242 |

See accompanying notes to consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

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

| | Three months ended December 31 | | Nine months ended December 31 | |
|---|-----------------------------------|-------------|----------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| Cash provided by (used in): | | | | |
| Operations: | | | | |
| Net (loss) earnings | \$ (23,084) | \$ (12,437) | \$ 28,680 | \$ 42,764 |
| Items not involving cash: | | | | |
| Amortization | 31,305 | 28,059 | 90,229 | 85,188 |
| Other non-cash charges | 2,379 | (8,874) | 4,227 | (7,084) |
| Long-term regulatory costs deferred | (1,855) | (1,628) | (2,555) | (6,904) |
| Change in non-cash operating working capital (note 9) | 1,431 | 7,931 | (16,867) | (414) |
| | 10,176 | 13,051 | 103,714 | 113,550 |
| Financing: | | | | |
| Repayment of long-term debt | - | - | (51,375) | (4,500) |
| Repayment of short-term loans | - | - | (3,949) | - |
| Repayment of capital lease obligations | (259) | (318) | (798) | (715) |
| | (259) | (318) | (56,122) | (5,215) |
| Investing: | | | | |
| Proceeds from disposal of property, plant and equipment | 23 | 11,040 | 107 | 11,118 |
| Purchase of property, plant and equipment and intangible assets | (35,873) | (34,420) | (91,584) | (78,196) |
| Recovery of import duties and related taxes (note 4) | - | 119,449 | - | 119,449 |
| Reduction of debt service reserves | (29) | - | 1,266 | 200 |
| Advancement of long-term loan | - | (24,247) | (268) | (24,247) |
| Proceeds from (purchase of) short-term investments | 32,230 | (51,382) | 37,194 | (51,601) |
| | (3,649) | 20,440 | (53,285) | (23,277) |
| Increase (decrease) in cash and cash equivalents | 6,268 | 33,173 | (5,693) | 85,058 |
| Cash and cash equivalents, beginning of period | 21,374 | 62,493 | 33,335 | 10,608 |
| Cash and cash equivalents, end of period | \$ 27,642 | \$ 95,666 | \$ 27,642 | \$ 95,666 |

Supplemental cash flow information (note 9)

See accompanying notes to consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)

Nine months ended December 31, 2011 and 2010

(columnar dollars expressed in thousands)

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. 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 December 31, 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 nine months ended December 31, 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.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)

Nine months ended December 31, 2011 and 2010

(columnar dollars expressed in thousands)

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 changeover date. The Company expects that all standards that will be in effect for the changeover year have already been issued by the International Accounting Standards Board ("IASB"). However, the Company is continuing to monitor the IASB and the AcSB as well as the Canadian Securities Administrators, for any developments which may affect the timing, nature or disclosure relating to our adoption of IFRS.

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 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 \$3.6 million.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)

Nine months ended December 31, 2011 and 2010

(columnar dollars expressed in thousands)

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 closed its project on rate-regulated activities. However, the IASB has commenced consulting constituents to seek input on their strategic direction and preparation in setting work plans over the next three years. It has also provided constituents with suggestions for items to add to their agenda, including rate-regulated activities. The Company has provided a response in support of reinstating a project on rate-regulated activities.

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.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
 Nine months ended December 31, 2011 and 2010
 (columnar dollars expressed in thousands)

2. Loans:

| | December 31 | March 31 |
|---|--------------|--------------|
| | 2011 | 2011 |
| Long-term debt: | | |
| 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 (a) | | |
| Tranche A (effective interest rate 5.17%) | 61,875 | 67,500 |
| Tranche B (floating interest rate of 1.65% at December 31, 2011) | 3,750 | 22,500 |
| 12 Year Loan, maturing June 2020 (a) | | |
| Tranche A (effective interest rate 5.18%) | 63,750 | 69,375 |
| Tranche B (floating interest rate of 1.65% at December 31, 2011) | 3,750 | 20,625 |
| 2.95% Loan, maturing January 2021 (effective interest rate 3.08%) | 85,500 | 90,000 |
| | 1,308,625 | 1,360,000 |
| Less: Deferred financing costs and unamortized bond discounts | (10,134) | (10,861) |
| Current portion | (9,000) | (22,125) |
| | \$ 1,289,491 | \$ 1,327,014 |

(a) 12 Year Loans:

During the quarter ended September 30, 2011, the Company entered into amendments to the two loan agreements. These amendments allowed for the continuance of Tranche B for three years provided that the outstanding balance of Tranche B was fully prepaid. The Company fully prepaid the outstanding Tranche B balances of both loans (\$22.5 million each); consequently, the Tranche A principal payments will be transferred to Tranche B for the next three years. Tranche B payments are interest only, paid in periods ranging from one to six months at the option of the Company, with the principal balance due when the loan matures. The interest rates on Tranche B are reset at floating rates of CAD LIBOR plus 30 bps, which will vary depending on the interest payment period.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
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 (columnar dollars expressed in thousands)

2. Loans (continued):

(b) Credit facility:

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

(c) 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% loan equal to not less than six months forecasted debt service, to be increased under certain conditions.

As at December 31, 2011, debt service reserves of \$35.8 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:

| | December 31 | March 31 |
|---|---------------|-------------------|
| | 2011 | 2011 |
| Regulatory accounts | | |
| 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 | (17,907) | (14,326) |
| Total of first performance term accounts | 1,194 | 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) | 14,349 | 849 |
| (Surcharges) rebates granted | (8,884) | 8,593 |
| Fuel price risk recoveries from the Province | (1,443) | (196) |
| Other payments from the Province | (1,503) | (1,556) |
| Interest payable | (58) | (295) |
| Balance – end of period | 671 | (1,790) |
| Tariffs in excess of price cap (b) | - | (1,072) |
| Performance term submission costs | 326 | 232 |
| Total of second performance term accounts | 997 | (2,630) |
| Total regulatory assets | 2,191 | 2,145 |
| Current regulatory assets | 1,194 | 3,703 |
| Total long-term regulatory assets (liabilities) | \$ 997 | \$ (1,558) |

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
 Nine months ended December 31, 2011 and 2010
 (columnar dollars expressed in thousands)

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

(a) Amortization expense:

During the quarter ended December 31, 2011 the Company recognized \$1.2 million in amortization expense for first performance term accounts (December 31, 2010: \$1.2 million). Amortization expense for first performance term accounts for the nine months ended December 31, 2011 totalled \$3.6 million (December 31, 2010: \$3.6 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 December 31, 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 nine months ended December 31, 2011, would have been unchanged (December 31, 2010: \$2.1 million higher) as detailed below:

| Impact of regulatory accounts on net earnings | Three months ended | | Nine months ended | |
|--|--------------------|-----------------|-------------------|-------------------|
| | December 31, | | December 31, | |
| | 2011 | 2010 | 2011 | 2010 |
| First performance term accounts: | | | | |
| Deferred fuel costs | \$ (1,156) | \$ (1,156) | \$ (3,469) | \$ (3,469) |
| Performance term submission costs | (37) | (37) | (112) | (112) |
| Second performance term accounts: | | | | |
| Deferred fuel costs | 1,855 | 1,568 | 2,461 | 6,806 |
| Performance term submission costs | - | 59 | 94 | 97 |
| Tariffs in excess of price cap | - | 1,202 | 1,072 | (5,472) |
| Total increase (decrease) in net earnings resulting from regulatory accounts | 662 | 1,636 | 46 | (2,150) |
| Unamortized training costs (note 5) | (49) | 24 | (59) | 94 |
| Total increase (decrease) in net earnings | \$ 613 | \$ 1,636 | \$ (13) | \$ (2,056) |

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
 Nine months ended December 31, 2011 and 2010
 (columnar dollars expressed in thousands)

4. Property, plant and equipment:

| December 31, 2011 | Cost | Accumulated amortization | Net book value |
|---|---------------------|-----------------------------|---------------------|
| Vessels | \$ 1,713,850 | \$ 674,850 | \$ 1,039,000 |
| Berths, buildings and equipment | 94,367 | 54,598 | 39,769 |
| Berths, buildings and equipment under capital lease | 722,250 | 272,020 | 450,230 |
| Land | 1,385 | - | 1,385 |
| Land under capital lease | 5,177 | - | 5,177 |
| Construction-in-progress | 47,061 | - | 47,061 |
| | \$ 2,584,090 | \$ 1,001,468 | \$ 1,582,622 |

| 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 |

At the end of September 2010, the Company received confirmation that a request for \$119.4 million of duty remission, including related GST, for the purchase of four vessels built in Germany was granted by the Government of Canada. This amount was recorded as a reduction of the cost of these assets during the quarter ended September 30, 2010. The funds were received during the quarter ended December 31, 2010.

During the quarter ended December 31, 2010, the Company disposed of its former head office building located at 1112 Fort Street, Victoria for \$11.0 million, resulting in a gain on sale of \$9.3 million.

Capitalized financing costs during construction for property, plant and equipment for the nine months ended December 31, 2011 totalled \$1.2 million (December 31, 2010: \$1.7 million).

Amortization expense for assets under capital lease for the quarter ended December 31, 2011 totalled \$5.8 million (December 31, 2010: \$5.1 million) and the nine months ended December 31, 2011 totalled \$16.9 million (December 31, 2010: \$14.5 million).

In addition to the construction-in-progress referenced above, the contractual commitments at December 31, 2011 for capital assets to be constructed, totalled \$17.0 million (March 31, 2011: \$48.7 million).

Rental income earned from buildings held for leasing purposes for the quarter ended December 31, 2011, totalled \$0.2 million (December 31, 2010: \$0.2 million) and nine months ended December 31, 2011, totalled \$0.6 million (December 31, 2010: \$0.6 million). These buildings have a cost and accumulated amortization of \$13.6 million and \$2.0 million respectively, as at December 31, 2011.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
Nine months ended December 31, 2011 and 2010
(columnar dollars expressed in thousands)

5. Intangible assets:

| December 31, 2011 | Cost | Accumulated amortization | Net book value |
|--|-----------|-----------------------------|-------------------|
| Acquired software, licenses and rights | \$ 29,176 | \$ 14,064 | \$ 15,112 |
| Internally developed software and websites | 23,684 | 14,702 | 8,982 |
| Work-in-progress | 14,286 | - | 14,286 |
| | \$ 67,146 | \$ 28,766 | \$ 38,380 |

| 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 nine months ended December 31, 2011 or the year ended March 31, 2011.

Capitalized financing costs during construction for intangible assets for the nine months ended December 31, 2011 totalled \$0.4 million (December 31, 2010: \$0.3 million).

Included in the cost of intangible assets as at December 31, 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 nine months ended December 31, 2011 intangible assets totaling \$7.7 million (December 31, 2010: \$9.1 million) were acquired and \$0.4 million (December 31, 2010: \$1.3 million) were internally developed. Amortization expense for the nine months ended December 31, 2011 totalled \$4.6 million (December 31, 2010: \$3.8 million).

6. Accrued employee future benefits:

During the quarter ended December 31, 2011 the Company recognized total defined benefit costs of \$0.6 million (December 31, 2010: \$0.3 million) and during the nine months ended December 31, 2011 the Company recognized total defined benefit costs of \$2.3 million (December 31, 2010: \$1.0 million). The amount recognized in the three months ended June 30, 2011 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.

BRITISH COLUMBIA FERRY SERVICES INC.

Notes to Consolidated Financial Statements (unaudited)
 Nine months ended December 31, 2011 and 2010
 (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 December 31, 2011 interest rate support received and recorded as a reduction of interest expense totalled \$0.4 million (December 31, 2010: \$0.1 million) and \$nil (December 31, 2010: \$0.1 million) was recorded as a reduction of capitalized interest. During the nine months ended December 31, 2011 interest rate support received and recorded as a reduction of interest expense totalled \$1.2 million (December 31, 2010: \$0.3 million) and a further \$0.2 million (December 31, 2010: \$0.1 million) was recorded 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 nine months ended December 31, 2011, the Company paid \$113,815 (December 31, 2010: \$17,161) 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 December 31 | | Nine months ended December 31 | |
|--|-----------------------------------|------------|----------------------------------|-----------|
| | 2011 | 2010 | 2011 | 2010 |
| (a) Changes in non-cash operating working capital: | | | | |
| Change in working capital | | | | |
| Accounts receivable | \$ 3,319 | \$ 125,987 | \$ 3,105 | \$ 2,729 |
| Prepaid expenses | 601 | 1,833 | (1,955) | 763 |
| Inventories | 468 | 954 | (521) | 210 |
| Regulatory assets | - | - | (1,072) | 4,775 |
| Accounts payable and accrued liabilities | 1,066 | 4,482 | (11,624) | 8,832 |
| Interest payable on long-term debt | (2,963) | (2,892) | (2,937) | (2,838) |
| Accrued employee costs | 1,320 | 2,057 | 2,618 | (911) |
| Deferred revenue | (1,060) | (461) | (2,248) | (3,418) |
| Regulatory liabilities | - | (1,202) | - | 697 |
| Change in non-cash working capital | 2,751 | 130,758 | (14,634) | 10,839 |
| Change attributable to capital asset acquisitions | (1,320) | (122,827) | (2,233) | (11,253) |
| Change in non-cash operating working capital | \$ 1,431 | \$ 7,931 | \$ (16,867) | \$ (414) |
| (b) Cash paid during the period for interest | \$ 21,604 | \$ 21,944 | \$ 59,135 | \$ 58,561 |
| (c) Non-cash transactions: | | | | |
| Capital assets acquired under capital lease | \$ - | \$ - | \$ - | \$ 49,247 |