Consolidated Financial Statements of

BRITISH COLUMBIA FERRY SERVICES INC.

Years ended March 31, 2012 and 2011

KPMG LLP
Chartered Accountants
St. Andrew's Square II
800-730 View Street
Victoria BC V8W 3Y7

Telephone (250) 480-3500
Telefax (250) 480-3539
Internet www.kpmg.ca

INDEPENDENT AUDITORS' REPORT

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 balance sheets as at March 31, 2012 and March 31, 2011 and the consolidated statements of (loss) earnings, comprehensive income and retained earnings 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 Canadian generally accepted accounting principles, 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 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 an 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 opinions.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of British Columbia Ferry Services Inc. as at March 31, 2012 and March 31, 2011, and its results of operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
June 15, 2012
Victoria, Canada

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BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Balance Sheets
(expressed in thousands)

	As at March 31, 2012	2011
Assets		
Current assets:		
Cash and cash equivalents	$ 7,700	$ 33,335
Restricted short-term investments (note 2(e))	35,705	37,040
Other short-term investments	26,880	64,074
Accounts receivable (notes 4(a) and 13)	42,341	20,619
Prepaid expenses	6,725	5,648
Inventories	22,017	19,957
Regulatory assets (note 6)	-	3,703
	141,368	184,376
Property, plant and equipment (note 7)	1,577,709	1,581,007
Intangible assets (note 8)	41,913	34,929
Long-term regulatory assets (note 6)	1,501	-
Long-term loan receivable (note 11)	24,515	24,247
Long-term land lease (note 9)	32,521	32,979
	$ 1,819,527	$ 1,857,538
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 51,985	$ 51,249
Short-term debt (note 2(d))	17,737	3,949
Interest payable on long-term debt	18,249	18,261
Accrued employee costs	49,204	48,194
Deferred revenue	13,784	15,596
Derivative liabilities (note 4(c))	12	23
Regulatory liabilities (note 6)	2,379	-
Current portion of long-term debt (note 2)	9,000	22,125
Current portion of accrued employee future benefits (note 10)	1,600	1,200
Current portion of obligations under capital lease (note 11)	974	1,040
	164,924	161,637
Accrued employee future benefits (note 10)	11,171	10,907
Long-term regulatory liabilities (note 6)	-	1,558
Long-term debt (note 2)	1,285,232	1,327,014
Obligations under capital lease (note 11)	47,013	47,723
	1,508,340	1,548,839
Shareholders' equity:		
Share capital (note 12)	75,478	75,478
Contributed surplus (note 13)	25,000	-
Retained earnings	210,709	233,221
	311,187	308,699
Commitments (notes 7 and 17)		
Contingent liabilities (notes 1(s) and 19)		
	$ 1,819,527	$ 1,857,538

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 (Loss) Earnings, Comprehensive Income and Retained Earnings
(expressed in thousands)

	Years ended March 31, 2012	2011
Revenue:		
Tariffs	$ 457,003	$ 458,049
Ferry service fees (note 14)	154,959	151,023
Federal-Provincial Subsidy Agreement (note 15)	27,487	26,924
Retail	76,522	78,920
Other income	22,206	24,354
	738,177	739,270
Expenses:		
Operations	413,259	411,116
Maintenance	86,313	85,717
Administration	30,974	31,169
Cost of retail goods sold	29,132	29,659
Amortization	122,973	114,486
	682,651	672,147
Earnings from operations	55,526	67,123
Gain on foreign exchange	233	173
Interest expense (note 16)	(71,902)	(72,173)
(Loss) gain on disposal and impairment of capital assets (note 7)	(331)	8,658
Net (loss) earnings	(16,474)	3,781
Other comprehensive income (note 1(u))	-	-
Net (loss) earnings and comprehensive income	(16,474)	3,781
Retained earnings, beginning of year	233,221	235,478
Preferred share dividend (note 12)	(6,038)	(6,038)
Retained earnings, end of year	$ 210,709	$ 233,221

See accompanying notes to consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Cash Flows
(expressed in thousands)

	Years ended March 31, 2012	2011
Cash provided by (used in):		
Operations:		
Net (loss) earnings	$ (16,474)	$ 3,781
Items not involving cash:		
Amortization	122,973	114,486
Other non-cash items	(2,665)	(6,659)
Long-term regulatory costs deferred	(3,059)	(7,543)
Change in non-cash operating working capital (note 20)	(318)	1,459
	100,457	105,524
Financing:		
Dividends paid on preferred shares	(6,038)	(6,038)
Repayment of long-term debt	(55,875)	(9,000)
Proceeds from (repayment of) short-term loans	13,788	3,949
Repayment of capital lease obligations	(1,042)	(1,021)
	(49,167)	(12,110)
Investing:		
Proceeds from disposal of property, plant and equipment	118	11,181
Purchase of property, plant and equipment and intangible assets	(115,304)	(120,874)
Recovery of import duties and related taxes (note 7)	-	119,449
Reduction of restricted short-term investments	1,335	200
Advancement of long-term loan	(268)	(24,247)
Proceeds from (purchase of) short-term investments	37,194	(56,396)
	(76,925)	(70,687)
(Decrease) increase in cash and cash equivalents	(25,635)	22,727
Cash and cash equivalents, beginning of year	33,335	10,608
Cash and cash equivalents, end of year	$ 7,700	$ 33,335

Supplemental cash flow information (note 20)

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 Company is subject to the *Coastal Ferry Act* (the "Act"), 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 levels.

On June 24, 2010, the Province enacted the *Miscellaneous Statutes Amendment Act (No.3), 2010*, (Bill 20), amending several statutes, including the Act. The amendments include changes to the governance and regulatory framework within which the Company operates.

Among other things, the Bill 20 amendments to the Act changed the mandate of the Authority to include: responsibility for the compensation plans of the Company's directors and certain executive officers; a requirement that effective September 30, 2010, a director of the Authority cannot also be a director of the Company; and subjected the records of the Company and the Authority to the *Freedom of Information and Protection of Privacy Act*. The amendments to the regulatory framework expanded the responsibilities of the Commissioner to include: consideration of the interests of ferry users, regulation of reservation fees, and regulation of ferry transportation services where the Commissioner determines the Company has an unfair competitive advantage.

1. Significant accounting policies:

(a) Basis of presentation:

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and include the accounts of the Company and its wholly owned subsidiaries. All inter-company balances and transactions have been eliminated on consolidation.

(b) Future accounting changes:

International Financial Reporting Standards ("IFRS"):

The Company's changeover date for the conversion to IFRS was originally April 1, 2011. In October, 2010, the Canadian Accounting Standards Board ("AcSB") amended Part 1 of the CICA Handbook – Accounting ("Handbook") to permit qualifying entities with rate-regulated activities to defer the adoption of IFRSs by one year to no later than annual periods beginning on or after January 1, 2012. The Company elected this option which deferred the changeover date for conversion to IFRS to April 1, 2012. In March 2012, the AcSB announced its intention to extend the option for deferral of the mandatory IFRS changeover date for entities with qualifying rate regulated activities by one more year to annual periods beginning on or after January 1, 2013. The Handbook was amended in May 2012 to permit this further deferral of IFRS adoption. The Company has chosen not to defer the adoption of IFRS for this additional one year period. Accordingly, the Company's changeover date for conversion to IFRS will remain April 1, 2012.

1. Significant accounting policies (continued):

(b) Future accounting changes (continued):

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

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.

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.

1. Significant accounting policies (continued):

(b) Future accounting changes (continued):

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

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. The details of regulatory assets and liabilities will be disclosed in the notes to the IFRS financial statements commencing with the interim period ending June 30, 2012. 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.

(c) Regulation:

The Company is regulated by the Commissioner to ensure that tariffs are fair and reasonable and to monitor service levels. In order to recognize the economic effects of regulation, the timing of recognition of certain revenues and expenses may differ from that otherwise expected under generally accepted accounting principles. These timing differences give rise to regulatory assets and regulatory liabilities in the financial statements.

The Company follows Accounting Guideline 19 "*Disclosures by Entities Subject to Rate Regulation*" (AcG-19) of the CICA Handbook which establishes guidelines on certain aspects of the disclosure and presentation of information in the financial statements of entities subject to rate regulation. AcG-19 requires the disclosure of general information regarding the nature and economic effects of rate regulation, as well as additional information on how rate regulation has affected the financial statements (note 6). The guideline does not address recognition and measurement issues associated with the accounting for rate-regulated operations.

(d) Cash and cash equivalents:

Cash and cash equivalents are comprised of cash and investments that are highly liquid in nature and have original maturity dates of three months or less.

(e) Short-term investments:

Short-term investments consist of financial instruments with original maturity dates greater than three months and less than a year.

(f) 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.

1. Significant accounting policies (continued):

(g) Financial instruments:

The Company establishes the classification of financial instruments at their initial recognition. Financial assets are classified as held-for-trading, available for sale, held-to-maturity, or loans and receivables. Financial liabilities are classified as held-for-trading or other 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 earnings 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 at which time the cumulative gain or loss previously reported in other comprehensive income is recognized in net earnings except for permanent impairment losses which are recognized in net earnings as incurred. Loans and receivables, investments held-to-maturity and other financial liabilities are initially measured at fair value and are subsequently measured at amortized cost. Derivative instruments are recorded as either assets or liabilities measured at their fair values unless exempted from derivative treatment as a normal purchase and sale.

In estimating fair value, the Company 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 which have a significant effect on recorded fair values for the asset or liability that are not based on observable market data (unobservable inputs).

(h) Embedded derivatives:

As at March 31, 2012, 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.

(columnar dollars expressed in thousands)

1. Significant accounting policies (continued):

(i) Hedging relationships:

Derivative financial instruments are utilized by the Company to manage market risk against the volatility in foreign currency, interest rate, and fuel price exposures. The Company does not utilize derivative financial instruments for trading or speculative purposes. At the inception of each hedge the Company determines whether it will or will not apply hedge accounting.

When applying hedge accounting, the Company documents all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company 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. 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 the period in which they have been terminated or cease to be effective.

(j) Property, plant and equipment:

The costs of major replacements, additions, extensions and improvements, including direct overhead and financing costs during construction, are capitalized. The costs of maintenance, repairs, refit and minor renewals or replacements are expensed as incurred.

Capital assets, including assets under capital leases, are amortized on a straight-line basis over their estimated useful lives as follows:

Asset class	Estimated useful life
Ship hulls	40 years
Ship propulsion and utility systems	20 to 30 years
Marine structures	20 to 40 years
Buildings	20 to 40 years
Equipment and other	3 to 20 years

(k) Intangible assets:

The costs of acquired computer software, licenses and rights of use as well as internally developed computer software and websites are capitalized. These intangible assets are valued at their acquisition cost plus direct overhead and financing costs, less amortization. Computer software, licenses, and websites are amortized on a straight-line basis over their estimated useful lives of 3 to 7 years. Rights of use intangible assets are amortized on a straight-line basis over their estimated useful lives of 20 to 30 years.

1. Significant accounting policies (continued):

(l) Impairment of long-lived assets:

The Company reviews capital assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by comparison of their carrying amount to the future undiscounted cash flows the assets are expected to generate. If such capital assets are considered to be impaired, the impairment to be recognized equals the amount by which the carrying amount of the assets exceeds their fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(m) Revenue recognition:

Tariff revenue is recognized when transportation is provided. The value of pre-sold fare media is included in the balance sheets as deferred revenue. Ferry service fees are recorded when service is provided.

(n) Pension and other employee future benefit plans:

Defined contribution plan accounting is applied to the Company's multi-employer defined benefit pension and long-term disability plans. These multi-employer plans are administered by external parties and the Company does not have sufficient information to apply defined benefit plan accounting. The actuarial determination of the accrued benefit obligations for retirement benefits other than pension uses the projected benefit 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).

For the purpose of calculating the expected return on plan assets, those assets are valued at fair value.

Actuarial gains (losses) arise from the difference between actual long-term rate of return on plan assets for a period and the expected long-term rate of return on plan assets for that period or from changes in actuarial assumptions used to determine the accrued benefit obligation. For the Company's retirement bonus and death benefit plans, the excess of the net accumulated actuarial gain (loss) over 10 percent of the greater of the benefit obligation and the fair value of plan assets is amortized over the average remaining service period of active employees.

Past service costs arising from plan amendments are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment.

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

1. Significant accounting policies (continued):

(o) Use of estimates:

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates relate to the valuation of assets held for sale, the economic life of capital assets and the corresponding periods of amortization, the recoverability of capital assets, the valuation of employee future benefits, and provisions for contingencies. Actual results could differ from these estimates.

(p) Taxes:

The Company 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 GST/HST purposes.

(q) Foreign currency transactions:

The Company’s normal operating currency is the Canadian dollar. Monetary assets and liabilities denominated in foreign currency are translated to Canadian dollars at the rate of exchange prevailing at the balance sheet date. Revenues and expenses are translated at rates in effect at the time of the transaction. Foreign exchange gains and losses are recognized in the statement of earnings during the period in which they arise.

(r) 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 to long-term debt which is measured using the effective interest rate method.

(s) Asset retirement obligations:

In the period when it can be reasonably determined, the Company 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 Company’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 Company’s long-lived assets include certain vessels which contain undetermined amounts of asbestos. Under certain circumstances the Company may be required to handle and dispose of the asbestos in a manner required by regulations. It is the Company’s intention to sell decommissioned vessels into world markets for continued use in providing commercial ferry service. Under these circumstances asbestos remediation would become the responsibility of the new owner.

1. Significant accounting policies (continued):

(s) Asset retirement obligations (continued):

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.

(t) Interest rate support:

The Company receives interest rate support from the Government of Canada for eligible new Canadian built vessels or major refurbishment of vessels. Amounts receivable in regard to capitalized interest are recognized as a reduction of capitalized interest upon completion of the project. Amounts receivable in regard to post-completion debt service costs are recognized as a reduction to interest expense.

(u) Comprehensive income:

The Company has not recognized any adjustments through other comprehensive income for the years ended March 31, 2012 and 2011.

(v) Comparative figures:

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

(columnar dollars expressed in thousands)

2. Loans:

Long-term debt:	As at March 31, 2012	2011
5.74% Senior Secured Bonds, Series 04-1, due May 2014 (effective interest rate 5.92%) (a)	$ 250,000	$ 250,000
6.25% Senior Secured Bonds, Series 04-4, due October 2034 (effective interest rate 6.41%) (a)	250,000	250,000
5.02% Senior Secured Bonds, Series 07-1, due March 2037 (effective interest rate 5.06%) (a)	250,000	250,000
5.58% Senior Secured Bonds, Series 08-1, due January 2038 (effective interest rate 5.62%) (a)	200,000	200,000
6.21% Senior Secured Bonds, Series 08-2, due December 2013 (effective interest rate 6.33%) (a)	140,000	140,000
12 Year Loan, maturing March 2020 (b)		
Tranche A (effective interest rate 5.17%)	60,000	67,500
Tranche B (floating interest rate of 1.48% at March 31, 2012)	5,625	22,500
12 Year Loan, maturing June 2020 (b)		
Tranche A (effective interest rate 5.18%)	61,875	69,375
Tranche B (floating interest rate of 1.47% at March 31, 2011)	5,625	20,625
2.95% Loan, maturing January 2021 (effective interest rate 3.08%) (c)	81,000	90,000
	1,304,125	1,360,000
Less: Deferred financing costs and unamortized bond discounts	(9,893)	(10,861)
Current portion	(9,000)	(22,125)
	$ 1,285,232	$ 1,327,014

Principal repayments due in the next five fiscal years are:

Year ended	
2013	$ 9,000
2014	149,000
2015	270,250
2016	24,000
2017	24,000
Thereafter	827,875
	$ 1,304,125

(columnar dollars expressed in thousands)

2. Loans (continued):

In May 2004, the Company entered into a master trust indenture which established common security and a set of common covenants for the benefit of all lenders under the Company'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 Company has issued five bond series of obligation bonds under the master trust indenture and entered into a credit facility agreement. In addition, the Company has entered into loan agreements which provided $288 million to partially finance the Company's purchase of two Super 'C' class vessels and one northern vessel. These funds were released to coincide with the conditional acceptance of the vessels in February 2008, May 2008 and January 2009.

(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 Company. The following table shows the semi-annual interest payment dates for the obligation bonds each year through to maturity.

Bonds	Interest payment dates	
Series 04-1	May 27	November 27
Series 04-4	April 13	October 13
Series 07-1	March 20	September 20
Series 08-1	January 11	July 11
Series 08-2	December 19	June 19

(b) 12 Year Loans:

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

These loan agreements deferred the principal payments for the first three years to a second tranche (Tranche B) on which interest only is 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. 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 financed by draws under Tranche B for the next three years.

2. Loans (continued):

(c) 2.95% Loan:

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

(d) Credit facility:

The Company 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 amended on April 20, 2012 to extend the maturity date from May 2013 to April 2017. Draws on this facility totalled $17.7 million as at March 31, 2012 (2011: $3.9 million), and are shown as short-term debt. The average interest rate on these borrowings was 1.9% at March 31, 2012. Interest expensed during the year ended March 31, 2012, was less than $0.1 million (2011: less than $0.1 million). In addition, letters of credit outstanding against this facility at March 31, 2012 were $0.1 million (2011: $0.2 million).

(e) 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 permitted under the terms of the 12 year loans and the 2.95% loan, during the year ended March 31, 2012, the Company withdrew $1.3 million from the debt service reserves representing six months interest on the principal paid to date on these loans (2011: $0.2 million).

As at March 31, 2012, debt service reserves of $35.7 million were held in short-term investments and have been classified as restricted short-term investments on the balance sheet (2011: $37.0 million).

(columnar dollars expressed in thousands)

3. Financial instruments:

The carrying and fair values of the Company's financial instruments are as follows:

	As at March 31, 2012		As at March 31, 2011	
	Carrying Value	Approx Fair Value	Carrying Value	Approx Fair Value
Available for sale [1]				
Cash	$ 4,034	$ 4,034	$ 1,648	$ 1,648
Held-for-trading [2]				
Other cash equivalents	1,457	1,457	137	137
Restricted short-term investments	-	-	37,040	37,040
Derivative liabilities	12	12	23	23
Held-to-maturity [3]				
Investments with maturities < 3 months	2,209	2,209	31,550	31,550
Restricted short-term investments	35,705	35,705	-	-
Other short-term investments	26,880	26,880	64,074	64,074
Loans and receivables [3]				
Accounts receivable	42,341	42,341	20,619	20,619
Loan receivable [4]	24,515	24,515	24,247	24,247
Other financial liabilities [3]				
Accounts payable and accrued liabilities	51,985	51,985	51,249	51,249
Short-term debt	17,737	17,737	3,949	3,949
Interest payable on long-term debt	18,249	18,249	18,261	18,261
Accrued employee costs	49,204	49,204	48,194	48,194
Long-term debt, including current portion [5, 6]	1,294,232	1,491,008	1,349,139	1,463,954

[1] Measured at fair value with revaluation gains and losses included in other comprehensive income until the asset is removed from the balance sheet. Due to the nature of this financial instrument, carrying value approximates fair value.
[2] Measured at fair value with all gains and losses included in net earnings in the period in which they arise. Fair values for the derivative liabilities have been estimated using period-end market rates. These fair values approximate the amount that the Company would pay to settle the contract at March 31.
[3] Measured at amortized cost. Due to the nature of these financial instruments and/or short-term maturity of these financial instruments, carrying value approximates fair value except as noted.
[4] Measured at amortized cost. Carrying value approximates fair value as the rate of return is variable and is expected to return a market rate of interest.
[5] Carrying value is measured at amortized cost using the effective interest rate method.
[6] 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 March 31, 2012, or by using available quoted market prices.

3. Financial instruments (continued):

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 the market prices are not available, fair values are estimated using discounted cash flow analysis based on the Company's current borrowing rate for similar borrowing arrangements.

As at March 31, 2012, all available for sale and held-for-trading financial instruments are classified as level 1 in the fair value hierarchy with quoted prices in active markets.

During the year ended March 31, 2012, no profits resulting from the use of valuation techniques used to measure level 2 or 3 instruments in the fair value hierarchy (i.e. those with no active market price) have been recognized.

The Company may use derivative instruments to hedge its exposure to fluctuations in fuel prices 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 Company would receive or pay should the derivative contracts be terminated at the stated dates. Any gains or losses related to fuel commodity swaps are charged to the Company's deferred fuel cost accounts.

4. Financial risk management:

Exposure to credit risk, liquidity risk, and market risk arises in the normal course of the Company's business. The Company manages 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. The Company does not utilize derivative financial instruments for trading or speculative purposes. At the inception of each hedge the Company determines whether it will or will not apply hedge accounting. No hedges have been designated under Section 3865 – "*Hedges*" as at March 31, 2012 and 2011.

(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, and accounts receivable the Company's credit risk is limited to the carrying value on the balance sheet. Management does not believe that the Company is subject to any significant concentration of credit risk.

The Company limits its exposure to credit risk on cash and cash equivalents and short-term investments by investing in liquid securities with high credit quality counter parties, placing limits on tenor of investment instruments and instituting maximum investment values per counter party.

(columnar dollars expressed in thousands)

4. Financial risk management (continued):

(a) Credit risk (continued):

Accounts receivable by source are as follows:

	March 31, 2012		
Trade customers and miscellaneous	18.2%	$	7,692
Federal and Provincial governments	81.8%		34,649
Total	100.0%	$	42,341

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 Company 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 balance sheet.

Accounts receivable from trade customers are generally due in 30 days. As at March 31, 2012, 99% of trade receivables are current. As at March 31, 2012, the provision for credit losses was $0.1 million (2011: $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 of British Columbia (the “Province”) are considered low credit risk.

The Company is exposed to credit risk in the event that a counter party in a derivative contract defaults on its obligation, including fuel commodity swaps and foreign exchange forward contracts. The Company manages the credit exposure related to financial instruments by dealing with high credit quality institutions, in accordance with established investment parameters, and by an ongoing review of its exposure to counter parties. Counter party credit rating and exposures are monitored by management on an ongoing basis, and are subject to approved credit limits. The counter parties with which the Company has significant derivative transactions must be rated single A or higher. The Company does not expect any counter parties to default on their obligations.

(columnar dollars expressed in thousands)

4. Financial risk management (continued):

(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 Company'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 Company, conditions in the capital and bank credit markets, ratings assigned by rating agencies and general economic conditions.

The Company manages liquidity risk through daily monitoring of cash balances, the use of long-term forecasting models and the maintenance of debt service reserves (note 2). The Company targets a strong investment grade credit rating to maintain capital market access at reasonable interest rates. As at March 31, 2012 and March 31, 2011, the Company's credit ratings were as follows:

	DBRS	Standard & Poor's
British Columbia Ferry Services Inc.:		
Senior secured long-term debt	A	A+

The following is an analysis of the contractual maturities of the Company's financial liabilities as at March 31, 2012:

Financial liabilities	< 1 year	2-3 years	4-5 years	> 5 years	Total
Accounts payable and accrued liabilities	$ 51,985	$ -	$ -	$ -	$ 51,985
Short-term debt	17,737				17,737
Interest payable on long-term debt	18,249	-	-	-	18,249
Accrued employee costs	49,204	-	-	-	49,204
Obligations under capital lease, including current portion	974	2,071	2,746	42,196	47,987
Long-term debt, including current portion (excluding deferred costs) [1]	9,000	419,250	48,000	827,875	1,304,125
	$ 147,149	$ 421,321	$ 50,746	$ 870,071	$ 1,489,287

[1] Carrying value at March 31, 2012, excludes unamortized deferred financing costs of $9.9 million.

4. Financial risk management (continued):

(c) Market risk:

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

Interest rate risk:

The Company is exposed to interest rate risk associated with short-term borrowings and floating rate debt. As at March 31, 2012, the Company's cash equivalents and short-term investments include fixed rate instruments with maturities of 185 days or less. Accordingly, the Company has exposure to interest rate movement that occurs beyond the term of the maturity of the fixed rate investments. The Company'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 Company maintains between 70% and 100% of its debt portfolio in fixed rate debt, in aggregate. Additionally, the Company may enter into interest rate agreements to manage its exposure on debt instruments. As at March 31, 2012, the Company has no interest rate agreements in place to offset interest rate risk and had approximately two per cent of total debt in variable rate instruments. A 50 basis point change in interest rates would not have had a significant effect on earnings for the twelve months ended March 31, 2012.

Foreign currency price risk:

The Company 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 Company reviews foreign currency denominated commitments and hedges through derivative instruments as necessary. As at March 31, 2012, the Company has foreign currency forward contracts of $1.5 million (2011: $1.2 million). A 10 per cent change in foreign exchange rates would not have had a significant effect on earnings for the twelve months ended March 31, 2012.

Fuel price risk:

The Company is exposed to risks associated with changes in the market price of marine diesel fuel. The Company may manage its exposure to fuel price volatility by entering into hedging instruments with certain financial intermediaries in order to reduce 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. Gains and losses resulting from fuel forward contracts are recognized as a component of fuel costs. Pursuant to the Company's Financial Risk Management Policy, the term of the contracts is not to extend beyond three years. This 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 and to 85% of anticipated monthly fuel consumption for the remaining 12 month period.

The Company is also allowed by regulatory order to use deferred fuel cost accounts to mitigate the impact of changes in fuel price on its earnings. Any differences between the per litre cost

(columnar dollars expressed in thousands)

4. Financial risk management (continued):

(c) Market risk (continued):

Fuel price risk (continued):

of fuel purchased and consumed (including hedge gains or losses) and the per litre cost of fuel included in the determination of price caps for the second performance term (note 6) are:

i) for those routes comprising the Northern Route Group;

a. one-half of the first 5 cents per litre of difference is recorded in expense for the period with the remaining one-half of the first 5 cents per litre of difference recorded in deferral accounts for recovery or settlement through future tariffs to customers (note 6(a)), and

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. one-half of the first 5 cents per litre of difference is recorded in expense for the period with all remaining differences per litre recorded in deferral accounts for recovery or settlement through future tariffs to customers (note 6(a)).

As a result of the use of deferred fuel cost accounts, the maximum effect on earnings from a change in fuel prices would be approximately $3.0 million.

During the year ended March 31, 2012, the amounts receivable from the Province in relation to fuel cost differences totalled $1.8 million (2011: $0.2 million receivable from the Province).

5. Capital management:

The Company'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 Company targets maintaining strong investment grade credit ratings (note 4(b)).

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

	As at March 31, 2012		As at March 31, 2011	
	$	%	$	%
Aggregate borrowings [1]	1,507,112	82.89	1,563,763	83.50
Shareholders' equity [2]	311,187	17.11	309,020	16.50
Total capital	1,818,299	100.00	1,872,783	100.00

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

[2] Shareholders' equity at March 31, 2011 excluded undesignated subsidiaries Pacific Marine Ventures Inc. and BCF Global Services Inc. both of which were designated during the year ended March 31, 2012.

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

(columnar dollars expressed in thousands)

5. Capital management (continued):

Debt service coverage (earnings before interest, taxes, depreciation, amortization, and rent) must be at least 1.5 times the debt service cost and the Company is required to maintain debt service reserves (notes 2 and 4). In addition to these restrictions and requirements, there are other covenants contained in the Master Trust Indenture (May 2004) available at www.SEDAR.com. The Company was in compliance with all of its covenants throughout the years ended March 31, 2012 and 2011.

6. 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 Act, the tariffs the Company charges its customers are subject to price caps. The Commissioner may, under certain circumstances, allow increases in price caps over the set levels.

The accounting for regulated operations of the Company differs from non-regulated businesses following GAAP. 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 tariff reductions. 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.

If the Company was not a rate-regulated entity and did not record regulatory assets and liabilities, net earnings for the year ended March 31, 2012, would have been $3.1 million higher (2011: $1.7 million lower) as detailed below:

Impact of regulatory accounts on net earnings	Year ended March 31, 2012	2011
First performance term accounts:		
Deferred fuel costs (a)	$ (4,625)	$ (4,625)
Performance term submission costs (b)	(150)	(150)
Second performance term accounts:		
Deferred fuel costs (a)	3,046	7,393
Performance term submission costs (b)	95	148
Tariffs in excess of price cap (c)	(1,389)	(1,072)
Total (decrease) increase in net earnings resulting from regulatory accounts	$ (3,023)	$ 1,694
Unamortized training costs (note 8)	(99)	48
Total (decrease) increase in net earnings	$ (3,122)	$ 1,742

(columnar dollars expressed in thousands)

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

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

Regulatory accounts	As at March 31, 2012	2011
First performance term accounts:		
Balance at March 31, 2008:		
Deferred fuel costs (a)	$ 18,501	$ 18,501
Performance term submission costs (b)	600	600
	19,101	19,101
Accumulated amortization	(19,101)	(14,326)
Total of first performance term accounts	**-**	**4,775**
Second performance term accounts:		
Deferred fuel costs (a)		
Balance – beginning of year	(1,790)	(9,185)
Fuel costs deferred (including realized hedge gains and losses)	19,486	849
(Surcharges collected) rebates granted	(13,098)	8,593
Fuel price risk (recoveries from) payments to the Province (note 4 (c))	(1,799)	(196)
Other payments from the Province	(1,503)	(1,556)
Interest payable	(40)	(295)
Balance – end of year	1,256	(1,790)
Tariffs in excess of price cap (c)	(2,461)	(1,072)
Performance term submission costs (b)	327	232
Total of second performance term accounts	**(878)**	**(2,630)**
Total regulatory (liabilities) assets	**(878)**	**2,145**
Current regulatory (liabilities) assets	**(2,379)**	**3,703**
Total long-term regulatory assets (liabilities)	**$ 1,501**	**$ (1,558)**

(a) Deferred fuel costs:

As prescribed by regulatory order, the Company defers differences between actual fuel costs and 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 settlement in future tariffs. Also prescribed by regulatory order, the Company collects fuel surcharges or provides fuel rebates from time to time which are applied against deferred fuel cost account balances and has included interest in the amount to be recovered from or returned to customers.

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

(a) Deferred fuel costs (continued):

The Commissioner considered $18.5 million of unrecovered deferred fuel costs in the determination of the price caps set for the second performance term beginning April 1, 2008, and recovery occurred over this four year period. Accordingly, this $18.5 million was amortized to expense on a straight-line basis over the term. The difference between the balances in the deferred fuel cost accounts at March 31, 2008 and this $18.5 million, a $6.6 million credit, formed the opening balances of the fuel cost deferral accounts for the second performance term. It is expected that the fuel cost deferral accounts will continue and the balance of $1.3 million in these accounts at March 31, 2012 will be recovered during the third performance term, which commences April 1, 2012.

During the year ended March 31, 2012, the Province agreed to pay $1.5 million, to be applied against the balance of deferred fuel costs (2011: $1.6 million).

During the year ended March 31, 2012, the Company recognized $4.6 million in amortization expense for deferred fuel costs (2011: $4.6 million).

(b) Performance term submission costs:

The Commissioner has authorized the Company to defer costs of representation associated with the second and third performance terms. The Commissioner has considered, or will consider, these costs in the determination of the price caps set for the four years beginning April 1, 2008, and for the four years beginning April 1, 2012. The Commissioner has not included an allowance for a return on investment for the second or third performance term submission costs. The recovery periods are the four year period of the second performance term, commencing April 1, 2008 and the four year period of the third performance term, commencing April 1, 2012.

(c) 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. At March 31, 2012, tariffs charged to customers on the Major Route Group exceeded the price cap by $2.5 million (2011: $1.1 million).

(columnar dollars expressed in thousands)

7. Property, plant and equipment:

March 31, 2012	Cost	Accumulated amortization	Net book value
Vessels	$ 1,736,977	$ 693,244	$ 1,043,733
Berths, buildings and equipment	101,451	56,736	44,715
Berths, buildings and equipment under capital lease	733,900	272,837	461,063
Land	1,385	-	1,385
Land under capital lease	5,177	-	5,177
Construction-in-progress	21,636	-	21,636
	$ 2,600,526	$ 1,022,817	$ 1,577,709

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

During the year ended March 31, 2011, the Company received $119.4 million of duty remission, including related GST from the Government of Canada, relating to the purchase of four vessels built in Germany. This amount was recorded as a reduction of the cost of these assets.

During the year ended March 31, 2011, 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 year ended March 31, 2012, totalled $1.5 million (2011: $2.5 million). Amortization expense for assets under capital lease for the year ended March 31, 2012, totalled $23.2 million (2011: $20.2 million).

In addition to the construction-in-progress referenced above, the contractual commitments as at March 31, 2012 for capital assets to be constructed, totalled $13.1 million (2011: $48.7 million).

The Government of Canada, through the Infrastructure Stimulus Program, has agreed to provide funding to help offset the costs of sewage and waste water treatment and other major projects at certain of our terminals. The Company received a total of $8.7 million under this program. During the year ended March 31, 2012, $2.6 million (2011: $6.1 million) of this amount has been recorded as a reduction of the cost of property, plant and equipment.

(columnar dollars expressed in thousands)

7. Property, plant and equipment (continued):

During the year ended March 31, 2012, the Company received $0.7 million (2011: $0.8 million) of rental income earned from buildings held for leasing purposes. These buildings have a cost and accumulated amortization of $13.6 million and $2.2 million respectively, as at March 31, 2012.

8. Intangible assets:

March 31, 2012		Cost		Accumulated amortization		Net book value
Acquired software, licenses and rights	$	33,947	$	15,181	$	18,766
Internally developed software and websites		23,822		15,268		8,554
Work in progress		14,593		-		14,593
	$	72,362	$	30,449	$	41,913

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 year ended March 31, 2012 or the year ended March 31, 2011

Capitalized financing costs during construction for intangible assets for the year ended March 31, 2012 totalled $0.5 million (March 31, 2011 $0.4 million).

Included in the cost of intangible assets as at March 31, 2012, is $0.7 million of unamortized training costs (2011: $0.8 million). If the Company was not a regulated entity, these training costs would be expensed in the period incurred.

During the year ended March 31, 2012, intangible assets totalling $12.8 million (2011: $11.8 million) were acquired and $0.5 million (2011: $2.1 million) were internally developed. During this same period intangible assets with a cost and accumulated amortization of $11.2 million were retired (2011: $1.6 million). Amortization expense for the year ended March 31, 2012 totalled $6.3 million (2011: $5.3 million).

9. Long-term land lease:

On April 1, 2003, the Company's land and structures comprising its terminals were transferred by the Company to the BC Transportation Financing Authority ("BCTFA"), a British Columbia Crown Corporation and related party at the time of the transaction. In exchange, the Company 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 amortized in accordance with the Company's amortization 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 is reflected at the book values of the transferred terminal structures and land.

Since April 1, 2003, the Company has entered into various agreements with BCTFA to add lands to the existing terminal leases. During the years ended March 31, 2012 and March 31, 2011, no new land costs were added to the terminal leases.

10. Accrued employee future benefits:

(a) Description of benefit plans:

The Company 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.

In addition, eligible employees are entitled to other retirement and future benefits as provided for under the collective agreement and terms of employment. A retirement bonus and a death benefit, both unfunded defined benefit plans and both administered by the Company, are based on years of service and final average salary. A funded long-term disability multi-employer plan provides disability income benefits after employment, but before retirement.

The Company also administers an unfunded accumulated sick leave bank ("Sick Bank obligation") consisting 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 Company'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 Company participated in the Workers' Compensation Board deposit class coverage system. Subsequent to March 31, 2003, the Company 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. Currently this obligation is unfunded.

(columnar dollars expressed in thousands)

10. Accrued employee future benefits (continued):

(b) Total cash payments:

Total cash payments for employee future benefits for the year ended March 31, 2012, consisting of cash contributed by the Company 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 $26.5 million (2011: $25.8 million).

(c) Defined benefit plans:

All of the Company's defined benefit plans, except its multi-employer plans, are currently unfunded. The most recent actuarial valuation of the retirement bonus and death benefit plans is as at March 31, 2011. A plan amendment at December 31, 2007 restricts exempt employees from joining the retirement bonus and death benefit plans. This has resulted in a negative past service cost which is being amortized over the average remaining service period of the active employee group covered by the plans commencing January 1, 2008. 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 bonus, provided the transfer happens on or before December 31, 2013. The most recent actuarial valuations of the WCB obligation and the Sick Bank obligation are as at March 31, 2011 and March 31, 2001, respectively.

	Other benefit plans	
Accrued benefit obligations	2012	2011
Balance, beginning of year	$ 13,162	$ 13,221
Current service cost	557	530
Interest cost	804	827
Benefits paid	(1,871)	(1,466)
Actuarial losses (gains)	958	50
Balance, end of year	$ 13,610	$ 13,162

(columnar dollars expressed in thousands)

10. Accrued employee future benefits (continued):

(c) Defined benefit plans (continued):

Reconciliation of funded status of the benefit plans to the amounts recorded in the financial statements	Other benefit plans 2012	2011
Fair value of plan assets	$ -	$ -
Accrued benefit obligation	13,610	13,162
Funded status of plans – deficit	(13,610)	(13,162)
Unamortized net actuarial loss	1,417	1,835
Unamortized plan amendment – past service cost	(578)	(780)
Accrued benefit liability	(12,771)	(12,107)
Current portion of accrued employee future benefits	1,600	1,200
Accrued employee future benefits	$ (11,171)	$ (10,907)

Elements of defined benefit costs recognized in the year	Other benefit plans 2012	2011
Current service cost	$ 557	$ 530
Interest cost	804	827
Actuarial losses	1,378	488
Plan amendments	(202)	(202)
Defined benefit costs recognized	$ 2,537	$ 1,643

Significant assumptions

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

	2012	2011
Accrued benefit obligation as of March 31:		
Discount rate	5.0%	5.7%
Rate of compensation increase	2.0%	2.0%
Annual employee retention rate	94.6%	94.0%
Employees with eligible dependents at pre-retirement death	43.0%	43.0%
Benefit cost for years ended March 31:		
Discount rate	5.0%	5.7%
Rate of compensation increase	2.0%	2.0%
Annual employee retention rate	94.6%	94.0%
Employees with eligible dependents at pre-retirement death	43.0%	43.0%
Average remaining service period of active employees (years)	7.0	6.8

(columnar dollars expressed in thousands)

10. Accrued employee future benefits (continued):

(d) Multi-employer plans:

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

	2012	2011
Public Service Pension Plan contributions (i)	$ 19,656	$ 19,230
Long-term disability plan contributions	4,952	5,068
Long-term disability plan amortization of surplus (ii)	64	64
	$ 24,672	$ 24,362

i) The March 31, 2011 actuarial valuation report for the Public Service Pension Plan was received by the Public Service Pension Board of Trustees on December 6, 2011. This report indicated that the pension fund has a deficit of $275 million. Under the terms of the plan's joint trust agreement, plan members and employers share in any increase or decrease in contribution rates. Effective April 1, 2012 the plan trustees increased the member and employer contribution rates to the basic account from 7.78% to 8.18% of pensionable earnings. This increase is primarily due to changes in the investment return and demographic assumptions. The contribution rates to the inflation adjustment account decreased for members from 1.50% to 1.25% and increased for employers from 2.5% to 2.75%, effective April 1, 2012. The next valuation, expected to be received during the fiscal year ended March 31, 2015, will be as at March 31, 2014.

ii) Contribution rates for the long-term disability plan are actuarially determined every three years as a percentage of covered payroll. The most recent valuation, as at March 31, 2011, determined an overall fund surplus. The newly established funding policy 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 increased from 3.09% to 3.5% of covered payroll effective April 1, 2012. The next scheduled valuation, expected to be received during the fiscal year ended March 31, 2015, will be as at March 31, 2014.

(columnar dollars expressed in thousands)

11. Head office property and other capital leases:

During the year ended March 31, 2011, agreements which constitute a capital lease for space in a new downtown Victoria, BC head office building took effect following the completion of construction of the new building. The initial term of the new 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 Company's proportion of total rentable area. In addition, the Company has entered into lease agreements with terms of three or four years for computer equipment and for a ten year term for a training facility. During the year ended March 31, 2012, the Company did not add any leased computer equipment to property, plant and equipment (2011: $nil).

Loan and purchase option:

During the year ended March 31, 2012, the Company's wholly-owned subsidiary, Pacific Marine Leasing Inc., advanced $0.3 million (2011: $24.2 million) to the developer of the new head office property to finalize the loan amount at $24.5 million. The term of the loan is fifteen years, secured by a second mortgage of 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 Company was granted an option to purchase up to fifty percent of the owner's equity interest in the new building at a price of $24.5 million. The purchase option expires at the end of the loan term.

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

	Head office lease				Other leases		
Year ended March 31	Minimum lease payments	Executory costs	Imputed interest (5.04%)	Obligation	Minimum lease payments	Executory costs and imputed interest	Total obligations
2013	$ 4,996	$ 1,709	$ 2,325	$ 962	$ 77	65	974
2014	5,030	1,743	2,277	1,010	18	18	1,010
2015	5,064	1,777	2,226	1,061	-	-	1,061
2016	5,249	1,813	2,172	1,264	-	-	1,264
2017	5,435	1,850	2,103	1,482	-	-	1,482
Thereafter	49,839	17,874	14,284	17,681	-	-	17,681
Purchase option	24,515	-		24,515	-	-	24,515
Total	$ 100,128	$ 26,766	$ 25,387	$ 47,975	$ 95	$ 83	$ 47,987
Current portion				(962)			(974)
				$ 47,013			$ 47,013

(columnar dollars expressed in thousands)

12. 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 Company's ability to issue shares and to declare dividends.

(b) Issued and outstanding:

	As at March 31,			
	2012		2011	
	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.

13. Contributed surplus:

On March 30, 2012, the Province confirmed that it had approved a contribution to the equity of the Company in the amount of $25 million payable as at March 31, 2012. This amount has been included in accounts receivable at March 31, 2012 and was received on April 20, 2012.

14. Ferry service fees:

The Company entered into an agreement with the Province commencing April 1, 2003 to provide ferry services that would not be commercially viable under the current regulated tariff structure. In exchange for fees, the Company provides agreed ferry service levels on specified routes and administers certain social policy initiatives on behalf of the Province. 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 was amended on June 30, 2007 and March 31, 2008 to, among other things, establish the ferry service levels and the fees for the provision of such service for the second performance term ending March 31, 2012.

(columnar dollars expressed in thousands)

15. Federal-Provincial Subsidy Agreement:

The Company receives revenue provided to the Province from the Government of Canada pursuant to a contract between the federal and provincial governments for the provision of ferry, coastal freight and passenger services in the waters of British Columbia. The annual payment increases with the Vancouver Consumer Price Index.

16. Interest rate support:

During the year ended March 31, 2012, the Government of Canada agreed to provide $1.6 million in the form of interest rate support to the Company for major refurbishment of one vessel (2011: $1.0 million for major refurbishment of one vessel). During the year ended March 31, 2012, $1.5 million of these amounts have been recorded as a reduction of interest expense (2011: $0.5 million) and $0.2 million as a reduction of capitalized interest (2011: $0.1 million).

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.

17. Other commitments:

The Company has entered into operating leases for certain building spaces, land and equipment. Lease payments charged to expense during the year ended March 31, 2012 were $1.0 million (2011: $1.5 million).

Future minimum lease payments are as follows:

Year ended		
2013	$	851
2014		486
2015		279
2016		45
	$	1,661

18. Related party transactions:

In accordance with the Act, the Company is responsible for paying any expenses that are incurred by the Authority without charge. During the year ended March 31, 2012, the Company paid $181,363 (2011: $71,361) 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.

19. Contingent liabilities:

The Company, in conducting its usual business activities, is involved in various legal proceedings and litigation, the outcome of which is indeterminable. It is the Company’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 Company. Any additional future costs or recoveries which differ from the accrued amounts will be recognized in net earnings as determined.

(columnar dollars expressed in thousands)

20. Supplemental cash flow information:

	Years ended March 31, 2012	2011
(a) Changes in non-cash operating working capital:		
Change in working capital		
Accounts receivable	$ (21,722)	$ (1,787)
Prepaid expenses	(1,077)	40
Inventories	(2,060)	(1,917)
Regulatory assets	3,703	1,072
Accounts payable and accrued liabilities	736	12,365
Interest payable on long-term debt	(12)	(58)
Accrued employee costs	1,010	(450)
Deferred revenue	(1,812)	(427)
Regulatory liabilities	2,379	-
Employee future benefits	400	400
Change in non-cash working capital	(18,455)	9,238
Change attributable to capital asset acquisitions	(6,863)	(7,779)
Change attributable to contributed surplus (note 13)	25,000	-
Change in non-cash operating working capital	$ (318)	$ 1,459
(b) Cash paid during the year for interest	$ 74,508	$ 74,329
(c) Non-cash transactions:		
Capital assets acquired under capital lease	$ 268	$ 49,247

21 Subsequent Event:

On May 31, 2012, the Province enacted the *Coastal Ferry Amendment Act, 2012* (Bill 47) amending the Act. The amendments include changes to the regulatory framework within which the Company operates. Among other things, the Bill 47 amendments to the Act expanded the authority and responsibilities of the Commissioner to include: approval of permanent changes to service levels, authority to order a temporary or permanent service reduction in certain circumstances, authority to require the Company to seek approval in advance of making certain capital expenditures, and the responsibility to set price caps sufficient to enable the Company to maintain access to borrowing rates that in the opinion of the Commissioner are reasonable.

When the Bill 47 amendments were initially introduced on May 9, 2012, the Province also announced that it would provide additional payments to the Company totalling $79.5 million. These payments are intended to reduce the pressure for future fare and price cap increases. The first payment of $25.0 million received April 20, 2012, was approved by the Province on March 30, 2012 as a contribution to the equity of the Company and was payable as at March 31, 2012. A further $54.5 million is expected to be received in annual payments of $21.5 million in the year ending March 31, 2013, $10.5 million in the year ending March 31, 2014, $11.0 million in the year ending March 31, 2015 and $11.5 million in the year ending March 31, 2016.