Consolidated Financial Statements of

BRITISH COLUMBIA FERRY SERVICES INC.

Years ended March 31, 2014 and 2013

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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 statements of financial position as at March 31, 2014 and March 31, 2013, the consolidated statements of comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of British Columbia Ferry Services Inc. as at March 31, 2014 and March 31, 2013, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Accountants

June 20, 2014

Victoria, Canada

BRITISH COLUMBIA FERRY SERVICES INC.

Consolidated Statements of Financial Position
(Expressed in thousands of Canadian dollars)

	As at, March 31, 2014	As at, March 31, 2013
Assets		
Current assets		
Cash and cash equivalents (note 3)	71,365	36,641
Restricted short-term investments (note 4(e))	35,792	35,575
Other short-term investments	81,006	43,403
Trade and other receivables (note 6(a))	16,577	18,118
Prepaid expenses	6,934	10,706
Inventories (note 7)	25,073	23,257
	236,747	167,700
Non-current assets		
Long-term loan receivable (note 8)	24,515	24,515
Long-term land lease (note 9)	31,604	32,063
Property, plant and equipment (note 10)	1,539,162	1,552,062
Intangible assets (note 11)	53,164	47,942
	1,648,445	1,656,582
Total assets	1,885,192	1,824,282
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	48,134	51,803
Interest payable on long-term debt	19,634	18,063
Deferred revenue	14,563	13,634
Derivative liabilities	5,274	12
Current portion of long-term debt (note 4)	270,250	149,000
Current portion of accrued employee future benefits (note 12)	2,204	2,204
Current portion of obligations under finance lease (note 8)	1,120	1,072
Provisions (note 13)	51,801	50,839
	412,980	286,627
Non-current liabilities		
Accrued employee future benefits (note 12)	15,931	16,604
Long-term debt (note 4)	1,066,531	1,137,212
Obligations under finance lease (note 8)	44,821	45,941
	1,127,283	1,199,757
Total liabilities	1,540,263	1,486,384
Equity		
Share capital (note 15)	75,478	75,478
Contributed surplus	25,000	25,000
Retained earnings	246,142	234,187
Total equity before reserves	346,620	334,665
Reserves (note 16(a))	(1,691)	3,233
Total equity including reserves	344,929	337,898
Total liabilities and equity	1,885,192	1,824,282

Commitments (note 10(b))

See accompanying notes to the consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

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

	Years ended March 31, 2014	2013
Revenue		
Vehicle and passenger fares	489,305	468,780
Ferry service fees (note 17)	180,076	182,100
Retail	78,932	76,496
Federal-Provincial Subsidy Agreement (note 18)	28,373	28,078
Fuel surcharges	2,689	11,469
Regulated other income (note 19)	13,458	12,848
Other income	7,328	6,602
Total revenue	800,161	786,373
Expenses		
Operations	451,670	436,812
Maintenance	63,240	69,938
Administration	31,636	29,632
Cost of retail goods sold	30,860	29,500
Depreciation and amortization	136,896	135,675
Total operating expenses	714,302	701,557
Operating profit	85,859	84,816
Net finance and other expenses		
Net finance expenses (note 21)		
Finance income	3,721	2,922
Finance expenses	(71,030)	(72,076)
Total net finance expenses	(67,309)	(69,154)
Loss on disposal and revaluation of property, plant and equipment and intangible assets	(557)	(154)
Total net finance and other expenses	(67,866)	(69,308)
Net earnings	17,993	15,508
Other comprehensive (loss) income (note 16(b))		
Items not to be reclassified to net earnings	116	1,056
Items to be reclassified to net earnings	(5,040)	-
Total other comprehensive (loss) income	(4,924)	1,056
Total comprehensive income	13,069	16,564

See accompanying notes to the consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

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

	Years ended March 31, 2014	2013
Cash flows from operating activities		
Net earnings	17,993	15,508
Items not affecting cash		
Net finance costs recognized in net earnings	67,309	69,154
Depreciation and amortization of non-current assets	136,896	135,675
Loss on disposal and revaluation of property, plant and equipment and intangible assets	557	154
Other non-cash adjustments to property, plant & equipment	523	(791)
Change in derivative liabilities recognized in net earnings	222	-
Changes in		
Long-term accrued employee future benefits	(569)	(757)
Provisions	962	3,817
Long-term land lease	459	458
Accrued interest costs	(1,110)	246
Total non-cash items	205,249	207,956
Movements in operating working capital		
Trade and other receivables	1,541	24,223
Prepaid expenses	3,772	(3,981)
Inventories	(1,816)	(1,241)
Accounts payable and accrued liabilities	(3,669)	1,095
Deferred revenue	929	(150)
Change in non-cash working capital	757	19,946
Change attributable to capital asset acquisitions	(1,908)	6,653
Change attributable to contributed surplus	-	(25,000)
Change in non-cash operating working capital	(1,151)	1,599
Cash generated from operating activities	222,091	225,063
Interest rate support received (note 21(a))	-	742
Interest received	4,554	2,268
Interest paid	(71,402)	(73,471)
Net cash generated by operating activities	155,243	154,602

See accompanying notes to the consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

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

	Years ended March 31, 2014	2013
Cash flows from financing activities		
Proceeds from issuance of bonds	200,000	-
Repayment of long-term debt	(149,000)	(9,000)
Repayment of short-term debt	-	(17,737)
Repayment of finance lease obligations	(1,072)	(974)
Contributed surplus payment from Province	-	25,000
Dividends paid on preferred shares	(6,038)	(6,038)
Deferred financing costs incurred	(1,390)	-
Net cash generated by (used in) financing activities	42,500	(8,749)
Cash flows from investing activities		
Proceeds from disposal of property, plant and equipment	53	120
Purchase of property, plant and equipment and intangible assets	(125,252)	(100,639)
(Increase) decrease of debt service reserve	(217)	130
Purchase of short-term investments	(37,603)	(16,523)
Net cash used in investing activities	(163,019)	(116,912)
Net increase in cash and cash equivalents	34,724	28,941
Cash and cash equivalents, beginning of year	36,641	7,700
Cash and cash equivalents, end of year	71,365	36,641

See accompanying notes to the consolidated financial statements.

BRITISH COLUMBIA FERRY SERVICES INC.

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

	Share capital	Contributed surplus	Retained earnings	Total equity before reserves	Reserves (note 16 (a))	Total equity including reserves
Balance as at April 1, 2012	75,478	25,000	224,717	325,195	2,177	327,372
Net earnings for the year ended March 31, 2013	-	-	15,508	15,508	-	15,508
Other comprehensive income for the year ended March 31, 2013	-	-	-	-	1,056	1,056
Preferred share dividends	-	-	(6,038)	(6,038)	-	(6,038)
Balance as at March 31, 2013	75,478	25,000	234,187	334,665	3,233	337,898
Net earnings for the year ended March 31, 2014	-	-	17,993	17,993	-	17,993
Other comprehensive loss for the year ended March 31, 2014	-	-	-	-	(4,924)	(4,924)
Preferred share dividends	-	-	(6,038)	(6,038)	-	(6,038)
Balance as at March 31, 2014	75,478	25,000	246,142	346,620	(1,691)	344,929

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

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

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. Accounting policies:

(a) Basis of preparation:

British Columbia Ferry Services Inc. is a company domiciled in Canada. The address of the Company's registered office is Suite 500, 1321 Blanshard Street, Victoria, BC Canada, V8W 0B7. These consolidated financial statements of the Company as at and for the years ended March 31, 2014 and 2013 comprise the Company and its subsidiaries (together referred to as the "Group").

(b) Statement of compliance:

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

These consolidated financial statements were approved by the Board of Directors on June 20, 2014.

(c) Basis of measurement:

These consolidated financial statements have been prepared using the historical cost method, with the exception of the following assets and liabilities which are measured at fair value: land, derivatives, financial instruments held for trading and available-for-sale financial assets.

1. Accounting policies (continued):

(d) Functional and presentation currency:

These consolidated financial statements are presented in Canadian dollars ("Cdn") which is the Group's functional currency. All financial data is presented in Canadian dollars rounded to the nearest thousand.

(e) Use of estimates and judgements:

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

Significant estimates relate to:

(i) Property, plant and equipment and intangible assets

The calculation of depreciation and amortization involves estimates concerning the economic life and salvage value of property, plant and equipment and intangible assets.

(ii) Future employee benefits

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

(iii) Interest rate agreements

The calculation of the effectiveness of interest rate agreement(s) that have been designated for hedge accounting is based on key estimates for interest rates and discount rates.

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

(f) Basis of consolidation – subsidiaries:

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

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

1. Accounting policies (continued):

(f) Basis of consolidation – subsidiaries (continued):

The subsidiary holdings of the Group as at March 31, 2014 are:

Pacific Marine Leasing Inc.
BCF Captive Insurance Company Ltd.

All inter-Group transactions, balances and any unrealized income and expenses on inter-Group transactions are eliminated on consolidation.

(g) Foreign currency transactions:

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

(h) Property, plant and equipment:

Property, plant and equipment, excluding land assets, are valued at cost plus direct overhead and financing costs, less depreciation and impairment. Land is valued at fair value at each year-end using the annual assessed values for property tax purposes as being representative of the fair values of these assets.

The cost of self-constructed assets includes expenditures on materials, direct labour, financing costs and an allocated proportion of project overheads. When parts of an item of property, plant and equipment have different estimated useful lives, they are accounted for as separate items (major components) of property, plant and equipment. The cost of replacing an item of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the item will flow to the Group, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of the item of property, plant and equipment and are recognized in net earnings or loss. The costs of the day-to-day servicing of items of property, plant and equipment are recognized in net earnings or loss as incurred.

1. Accounting policies (continued):

(h) Property, plant and equipment (continued):

Where components of an asset have different estimated useful lives, depreciation is calculated on each separate component. Depreciation commences when an asset is available for use. Estimates of remaining useful lives and residual values are reviewed annually and adjusted if appropriate. Property, plant and equipment, including assets under finance leases, are depreciated on a straight-line basis over the estimated useful lives of the assets at the following rates:

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

(i) Intangible assets:

Intangible assets consist of acquired computer software and licenses and rights of use as well as internally developed computer software and website. These assets are valued at their acquisition cost plus direct overhead and financing costs, less amortization and impairment.

Software costs are capitalized if it is probable that the asset created will generate future economic benefits, the costs can be reliably measured, the product is technically feasible and the Group intends to, and has sufficient resources to, complete development and use the asset. Website costs are capitalized where the expenditure is incurred on developing an income generating website. Software and website costs capitalized include materials, direct labour and financing costs. Subsequent expenditure is capitalized only if it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognized in net earnings or loss as incurred.

Intangible assets with finite useful lives are amortized on a straight line basis over their estimated useful lives (3 to 7 years) since this most closely reflects the expected pattern of consumption of future economic benefits embodied in the asset. Rights of use intangible assets are amortized on a straight-line basis over their estimated useful lives of 10 to 30 years. Amortization is recognized in net earnings or loss from the date that intangible assets are available for use. The amortization methods and estimated remaining lives are reviewed annually.

1. Accounting policies (continued):

(j) Inventories:

Inventories are measured at the lower of cost and net realizable value. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale. No amounts are carried at net realizable value.

The cost of general and catering inventories is accounted for using the weighted average formula, while the cost of fuel inventories is based on the first-in–first-out principle. The cost of inventories includes expenditures incurred in acquiring the inventories and other direct costs incurred in bringing them to their existing location and condition.

(k) Employee benefits:

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

Defined contribution plan accounting is applied to the Group's multi-employer defined benefit pension and long-term disability plans. These multi-employer plans are administered by external parties and the Group does not have sufficient information to apply defined benefit plan accounting. The cost of these benefits is charged to net earnings or loss as contributions are made to the plans.

The actuarial determination of the accrued benefit obligations for retirement benefits 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). Under the projected benefit method, the cost of these benefits is charged to net earnings or loss so as to spread the regular cost over the service lives of employees in accordance with the advice of qualified actuaries who carry out a full valuation of the plans on a regularly scheduled basis. The pension obligation is measured as the present value of estimated future cash outflows using interest rates based on the yield of long-term high quality corporate bonds with maturities matching the pension obligation.

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

Actuarial gains (losses) arise from the difference between the actual 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 and from changes in actuarial assumptions used to determine the accrued benefit obligation. For the Group's retirement bonus and death benefit plans, the actuarial gain (loss) is recognized in other comprehensive income. The average remaining service period of the active employees covered by the retirement bonus and death benefit plans was 7.0 years as at March 31, 2011, the date of the most recent actuarial valuation.

1. Accounting policies (continued):

(k) Employee benefits (continued):

Past service costs arising from plan amendments are recognized immediately to the extent that the benefits are already vested but are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment where the benefits are not already vested. The full liability for all plan deficits is recorded, as adjusted for any past service costs still to be amortized.

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.

(l) Provisions:

A provision is recorded when:

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

If these conditions are not met, no provision is recorded.

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

(m) Revenues:

Tariff revenue is recognized when transportation is provided. The value of fares sold for which payment is received in advance of providing transportation is included in the statement of financial position as deferred revenue. These advance payments include prepaid vehicle and passenger fares, assured loading tickets and other reservation fees.

Retail revenue consists primarily of food services and gift shop sales. Parking revenues are received from both owned and subcontracted parking facilities and are recognized when service is provided. Revenue is generated from various advertising contracts and recognized according to the individual agreement.

Construction contract revenue is recognized using the percentage of completion method. At each reporting period, an estimate is made of the total profit or loss expected for the contract and the percentage of work completed. These estimates are used to measure the fair value of the consideration receivable for the contract and the amount of costs to be recognized in the period. If contract costs are not probable of being recovered they are immediately expensed.

1. Accounting policies (continued):

(n) Finance leases:

Assets held under finance leases are initially recognized as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments.

Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to produce a constant periodic rate of interest on the remaining balance of the liability.

(o) Operating leases:

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

(p) Taxes:

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

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

(q) Impairment of non-financial assets:

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

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

For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). The Group defines a cash generating unit as a route group. Price caps for each route group, as defined in the Coastal Ferry Services Contract with the Province of British Columbia (the "Province"), are set by the Commissioner based on the principle that the costs necessary to provide service system-wide are recovered.

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

1. Accounting policies (continued):

(r) Financial assets and liabilities:

Financial assets include trade receivables, loan receivables, derivatives with a positive market value, investment in securities and cash.

Financial liabilities include bank borrowings, bonds, obligations related to lease contracts, derivatives with a negative market value and trade payables.

Financial assets and liabilities presented are “non-current” except those with a maturity of less than twelve months from the period-end date. Those with maturities of less than twelve months are presented as “current assets” or “cash equivalents” depending on the circumstances.

(i) Recognition and measurement of financial assets (excluding derivatives)

In accordance with IAS 39, *Financial Instruments: Recognition and Measurement*, financial assets are classified into one of four categories:

- assets held-to-maturity (securities giving entitlement to fixed or fixable payments on set dates, and which the Group is able and intending to hold to maturity);
- loans and receivables (non-derivative financial assets subject to fixed or fixable payments, and which are not quoted on an active market);
- assets held–for-trading (investments and securities bought and held primarily with a view to a short-term resale); and
- assets held for sale (all financial assets not recognized in one of the three previous categories).

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

(ii) Loans and advances

When initially recognized, loans and advances are measured at fair value. These financial assets are then carried at amortized cost using the effective interest rate method. Loans and advances are subject to recoverable value tests, carried out whenever there are objective indicators that the recoverable value of these assets would be lower than the carrying value and, at the very least, on each statement of financial position date.

(iii) Trade and other receivables

Trade and other receivables are recorded at fair value (in most cases the same as nominal value) minus any loss of value recorded in a special impairment account. As receivables are due in less than one year, they are not discounted. If there is any indication that these assets may be impaired, they will be subject to an analysis based primarily on the following criteria: age of the receivable, the debtor’s financial position and negotiation of a payment schedule. The difference between the carrying amount and the recoverable value is recorded as a provision in net earnings or loss. Impairment may be reversed if the asset regains its value in future periods and the reversal is booked in the same item as the initial provision. Impairment is deemed permanent when the receivable itself is considered to be permanently non-recoverable and written off.

1. Accounting policies (continued):

(r) Financial assets and liabilities (continued):

(iv) Cash and cash equivalents

Cash and cash equivalents include cash on hand and demand deposits, with a maturity of less than three months, are held to maturity and 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. The instruments held in this category can be liquidated or sold on short notice, and do not bear any significant risk of loss in value.

(v) Borrowings and other financial liabilities

Trade and other debts are initially recorded at fair value, which is generally the same as nominal value. Bank borrowings and other financial liabilities are subsequently measured at amortized cost calculated using the effective interest rate method. Interest accrued on borrowings is included in “accounts payable and accrued liabilities” on the statement of financial position. Cash flows linked to short-term payable amounts are not discounted. Long-term cash flows are discounted whenever the impact is significant.

(vi) Recognition and measurement of financial derivatives

Financial derivatives are held from time to time to manage exposure to fuel price, interest rate and foreign exchange risks. Derivatives are initially recorded at fair value and associated transaction costs are recognized in net earnings or loss when incurred. After initial recognition, derivatives are measured at fair value based on market prices at each statement of financial position date. Changes in the fair value of these instruments are recorded in net earnings or loss. The Group derecognizes a financial liability when its contractual obligations are discharged, cancelled or expired.

1. Accounting policies (continued):

(r) Financial assets and liabilities (continued):

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

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

(s) Borrowing costs:

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

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

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

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

(t) Hedging relationships:

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

1. Accounting policies (continued):

(t) Hedging relationships (continued):

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

Realized and unrealized gains or losses associated with derivative instruments which have been terminated or cease to be effective prior to maturity are recognized in net earnings or loss in the period in which they have been terminated or cease to be effective. Realized hedge gains or losses related to non-financial assets or liabilities are reclassified from other comprehensive income and are included in the initial carrying amount of the non-financial asset or liability acquired.

(u) 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.

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

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

The Group's long-lived assets include certain vessels which contain undetermined amounts of asbestos. Under certain circumstances the Group may be required to handle and dispose of the asbestos in a manner required by regulations. It is the Group'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.

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.

1. Accounting policies (continued):

(w) Interest rate support:

The Group 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.

(x) Comprehensive income:

The Group recognizes increases in the fair values of land assets in other comprehensive income except to the extent that such an increase represents a reversal of a decrease for the same asset that was previously recognized in net earnings or loss. A decrease in the fair values of land assets is recognized in net earnings or loss to the extent the decrease exceeds the balance, if any, held in the land revaluation reserve relating to a previous revaluation.

The Group recognizes actuarial gains and losses on employee future benefits in other comprehensive income and does not reclassify these to net earnings or loss in subsequent periods.

(y) Segment reporting:

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

(z) Adoption of new accounting standards:

Employee benefits:

Effective April 1, 2013, the Group adopted IAS 19 *Employee Benefits* (amended). The amendments to this standard make certain changes to the recognition, presentation and disclosure of defined benefit plans. As a result of these amendments, actuarial gains and losses of defined benefit plans will be immediately recognized in other comprehensive income instead of net earnings or loss. The option to use the corridor approach to recognize these costs over time is no longer available. In addition, the amendments change the definition of both short-term and long-term employee benefits so it is clear that the distinction between the two depends on when the entity expects the benefits to become due to be settled. As at April 1, 2013, there were no unrecognized actuarial gains or losses of the Group's defined benefit plans. During the year ended March 31, 2014, the Group recognized actuarial gains of $0.1 million in other comprehensive income.

Fair value measurements:

Effective April 1, 2013, the Group adopted IFRS 13 *Fair Value Measurement.* This standard replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The adoption of this new standard has not had any impact on the Group's March 31, 2014 consolidated financial statements.

2. Future accounting changes:

Certain pronouncements were issued by the IASB that are mandatory for accounting periods after March 31, 2014.

(a) **IFRS 9 *Financial Instruments*:**

This standard replaces the guidance in IAS 39 *Financial Instruments: Recognition and Measurement*, on the classification and measurement of financial assets. The Standard eliminates the existing IAS 39 categories of held-to-maturity, available-for-sale and loans and receivables. Financial assets will be classified into one of two categories on initial recognition: financial assets measured at amortized cost; or financial assets measured at fair value.

In November 2013, the International Accounting Standards Board issued amendments to IFRS 9. The amendments include changes which will align hedge accounting more closely with risk management activities. Although the amendments do not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness; more hedging strategies used for risk management will qualify for hedge accounting. The amendments removed the mandatory effective date of January 1, 2015 for adoption of IFRS 9 with a new date to follow. In February 2014, the IASB decided on a mandatory effective date for IFRS 9 of January 1, 2018. Early adoption of IFRS 9 is permitted. The Group does not expect the application of IFRS 9 to have any impact on its consolidated financial statements and is considering the timing of its adoption.

(b) **International Financial Reporting Interpretations Committee (IFRIC) 21 *Levies:***

IFRIC 21, *Levies* provides guidance on when to recognize a liability for a levy imposed by a government. IFRIC 21 is to be applied retrospectively and is effective for the Group on April 1, 2014. The Group does not expect this guidance to have a significant impact on its annual consolidated financial statements.

(columnar dollars expressed in thousands of Canadian dollars)

3. Cash and cash equivalents:

	As at: March 31, 2014	March 31, 2013
Cash	11,783	19,043
Cash equivalents:		
Held-for-trading investments	3	93
Held-to-maturity investments	59,579	17,505
Total	71,365	36,641

4. Loans:

Long-term debt:	As at. March 31, 2014	March 31, 2013
5.74% Senior Secured Bonds, Series 04-1, due May 2014 (effective interest rate of 5.92%)	250,000	250,000
6.25% Senior Secured Bonds, Series 04-4, due October 2034 (effective interest rate of 6.41%)	250,000	250,000
5.02% Senior Secured Bonds, Series 07-1, due March 2037 (effective interest rate of 5.06%)	250,000	250,000
5.58% Senior Secured Bonds, Series 08-1, due January 2038 (effective interest rate of 5.62%)	200,000	200,000
6.21% Senior Secured Bonds, Series 08-2, due December 2013 (effective interest rate of 6.33%)	-	140,000
4.70% Senior Secured Bonds, Series 13-1, due October 2043 (effective interest rate of 4.75%)	200,000	-
12 Year Loan, maturing March 2020		
Tranche A (effective interest rate of 5.17%)	45,000	52,500
Tranche B (floating interest rate of 1.52% at March 31, 2014)	20,625	13,125
12 Year Loan, maturing June 2020		
Tranche A (effective interest rate of 5.18%)	46,875	54,375
Tranche B (floating interest rate of 1.52% at March 31, 2014)	20,625	13,125
2.95% Loan, maturing January 2021 (effective interest rate of 3.08%)	63,000	72,000
	1,346,125	1,295,125
Less: Deferred financing costs and unamortized bond discounts	(9,344)	(8,913)
Current portion	(270,250)	(149,000)
Total	1,066,531	1,137,212

(columnar dollars expressed in thousands of Canadian dollars)

4. Loans (continued):

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

The Group has issued six series of obligation bonds under the Master Trust Indenture ("MTI") and entered into a credit facility agreement. In addition, the Group has entered into loan agreements which provided $288 million to partially finance the Group'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 Group. The following table shows the semi-annual interest payment dates for the obligation bonds each year through to maturity.

Bonds	Interest payment dates	
Series 04-1	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
Series 13-1	April 23	October 23

On July 24, 2013, the Group exercised its right to redeem the Series 08-2 Bonds. In accordance with the provisions of the MTI, the Group paid to the registered holders of the bonds a total of $143.2 million which reflects a redemption price of $1,016.70 per $1,000 together with unpaid interest accrued to the redemption date. The redemption was funded with draws on the credit facility of $88.0 million and cash on hand of $55.2 million. The bond redemption premium paid of $2.3 million was recognized in finance expense.

On October 25, 2013, the Group issued $200 million of senior secured bonds. The Series 13-1 bonds bear interest at 4.702% per annum, payable semi-annually and will mature October 23, 2043. A debt service reserve for these bonds has been established in the amount of $4.7 million. The bond issue is partially related to the early redemption in July 2013 of the $140 million bond Series 08-2. The net proceeds from the sale of the bonds was used to repay outstanding draws on the credit facility and to fund the reserve account, and will be used to partially fund capital expenditures and provide funding for general corporate purposes.

4. Loans (continued):

(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 Group, 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 (effective June 2013, CDOR plus 30 bps), which will vary depending on the interest payment period. During the quarter ended September 30, 2011, the Group 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 Group 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 until June 2014.

(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 Group has a credit facility with a syndicate of Canadian banks, secured by pledged bonds. This revolving facility, in the amount of $155.0 million, was amended on March 12, 2014 to extend the maturity date to April 2019. There were no draws on this credit facility as at March 31, 2014 and as at March 31, 2013.

Interest expensed during the year ended March 31, 2014, was $0.3 million (2013: less than $0.1 million). Letters of credit outstanding against this facility at March 31, 2014 totalled $0.1 million (March 31, 2013: $0.1 million).

(e) Debt service reserves:

The Group is required to maintain debt service reserves for the Series 04-1, 04-4, 07-1, 08-1 and 13-1 bonds equal to not less than six months forecast 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 forecast debt service, to be increased under certain conditions.

As a result of their redemption on July 24, 2013, the Group is no longer required to maintain a debt service reserve for the Series 08-2 bonds. As at March 31, 2014, debt service reserves of $35.8 million were held in short-term investments and have been classified as restricted short-term investments on the balance sheet (March 31, 2013: $35.6 million).

(columnar dollars expressed in thousands of Canadian dollars)

5. Financial instruments:

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

	As at March 31, 2014		As at March 31, 2013	
	Carrying Value	Approx Fair Value	Carrying Value	Approx Fair Value
Available for sale [1]				
Cash	11,783	11,783	19,043	19,043
Financial assets/liabilities at fair value through net earnings or loss[2]				
Cash equivalents	3	3	93	93
Derivative liabilities	7	7	12	12
Financial assets/liabilities at fair value through other comprehensive income[3]				
Derivative liabilities	5,267	5,267	-	-
Held-to-maturity [4]				
Cash equivalents	59,579	59,579	17,505	17,505
Restricted short-term investments	35,792	35,792	35,575	35,575
Other short-term investments	81,006	81,006	43,403	43,403
Loans and receivables [4]				
Trade and other receivables	16,577	16,577	18,118	18,118
Long-term loan receivable [5]	24,515	24,515	24,515	24,515
Other financial liabilities [4]				
Accounts payable and accrued liabilities	48,134	48,134	51,803	51,803
Interest payable on long-term debt	19,634	19,634	18,063	18,063
Provisions	51,801	51,801	50,839	50,839
Long-term debt, including current portion [6, 7]	1,336,781	1,515,137	1,286,212	1,486,749

[1] Measured at fair value with revaluation gains and losses included in other comprehensive income until the asset is removed from the statement of financial position. 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 Group would pay to settle the contract at the date of the statement of financial position.

[3] If the hedge is effective, measured at fair value with all gains and losses initially included in other comprehensive income in the period in which they arise and subsequently in net earnings or loss when realized or when the hedge ceases to be effective. If the hedge is ineffective, measured at fair value with all gains and losses recognized in net earnings or loss. Fair values for the derivative liabilities have been estimated using period-end market rates. These fair values approximate the amount that the Group would pay to settle the contract at the date of the statement of financial position.

[4] 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.

[5] 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.

[6] Carrying value is measured at amortized cost using the effective interest rate method.

[7] Fair value is calculated by discounting the future cash flows of each debt issue at the estimated yield to maturity for the same or similar issues at the date of the statement of financial position, or by using available quoted market prices.

(columnar dollars expressed in thousands of Canadian dollars)

5. Financial instruments (continued):

The following items shown in the consolidated statement of financial position at March 31, 2014 and March 31, 2013 are measured at fair value on a recurring basis using level 1 or 2 inputs. The fair value of the financial assets and liabilities at March 31, 2014 and at March 31, 2013, using level 3 inputs, was $nil.

	As at March 31, 2014		As at March 31, 2013	
	Level 1	Level 2	Level 1	Level 2
Asset (liability):				
Cash [1]	11,783	-	19,043	-
Cash equivalents [1]	3	-	93	-
Derivatives [2]	-	(5,274)	-	(12)
Long-term debt, including current portion [2]	-	(1,515,137)	-	(1,486,749)
	11,786	(1,520,411)	19,136	(1,486,761)

[1] Classified in level 1 as the measurement inputs are derived from observable, unadjusted quoted prices in active markets for identical assets.
[2] Classified in level 2 as the significant measurement inputs used in the valuation models are indirectly observable in active markets (derived from prices).

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates cannot be determined with precision as they are subjective in nature and involve uncertainties and matters of judgment. Where market prices are not available, fair values are estimated using discounted cash flow analysis based on the Group's current borrowing rate for similar borrowing arrangements.

No amounts have been reclassified into or out of fair value classifications in the year ended March 31, 2014. Financial assets have been pledged as security for liabilities under the MTI (note 4). The Group does not hold any multiple embedded derivative financial assets or liabilities. The ineffective portion of an unrealized hedge loss on an interest rate forward contract of $0.2 million was recognized in net earnings during the year ended March 31, 2014 (note 6(c)).

As at March 31, 2014, 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, 2014, 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 Group may use derivative instruments to hedge its exposure to fluctuations in fuel prices, interest rates and foreign currency exchange rates. The fair value of commodity derivatives reflects only the value of the commodity derivatives and not the offsetting change in value of the underlying future purchase of fuel. These fair values reflect the estimated amounts that the Group would receive or pay should the derivative contracts be terminated at the stated dates.

(columnar dollars expressed in thousands of Canadian dollars)

6. Financial risk management:

Exposure to credit risk, liquidity risk, and market risk arises in the normal course of the Group's business. The Group 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 Group does not utilize derivative financial instruments for trading or speculative purposes. At the inception of each hedge the Group determines whether it will or will not apply hedge accounting. As at March 31, 2014 the Group has entered into four interest rate forward contracts (note 6 (c)) and has applied hedge accounting to these contracts (2013: nil).

(a) Credit risk:

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

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

Accounts receivable by source are as follows:

	As at:			
	March 31, 2014		March 31, 2013	
Trade customers and miscellaneous	8,010	48.3%	8,305	45.8%
Federal and Provincial governments	8,567	51.7%	9,813	54.2%
Total	16,577	100.0%	18,118	100.0%

Accounts receivable from trade customers are primarily due from commercial customers and transportation operators. Credit risk is reduced by a large and diversified customer base and is managed through the review of third party credit reports on customers both before extending credit and during the business relationship. The Group manages its exposure to credit risk associated with all customers through the monitoring of aging of receivables, by collecting deposits from and adjusting credit terms for higher risk customers and customers who are not on a pre-authorized payment plan. Amounts due from tickets sold to passengers through the use of major credit cards are settled shortly after sale and are classified as cash and cash equivalents on the balance sheet.

Accounts receivable from trade customers are generally due in 30 days. As at March 31, 2014, 100% of trade receivables are current. As at March 31, 2014, the provision for credit losses was $0.1 million (2013: $0.1 million) and reflects management's estimate of uncollectible receivables from trade customers based on past experience and analysis of customer accounts.

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

6. Financial risk management (continued):

(a) Credit risk (continued):

The Group is exposed to credit risk in the event that a counter party to an investment contract or a derivative contract defaults on its obligation, including fuel commodity swaps and foreign exchange and interest rate forward contracts. The Group 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 Group has significant derivative transactions must be rated single A or higher. The Group does not expect any counter parties to default on their obligations.

(b) Liquidity risk:

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

The Group manages liquidity risk through daily monitoring of cash balances, the use of long-term forecasting models, maintaining access to a credit facility and the maintenance of debt service reserves (note 4). The Group targets a strong investment grade credit rating to maintain capital market access at reasonable interest rates. As at March 31, 2014 the Group's credit ratings were as follows:

	DBRS	Standard & Poor's
British Columbia Ferry Services Inc.:		
Senior secured long-term debt	A (March 31, 2013: A)	AA- (March 31, 2013: A+)

(columnar dollars expressed in thousands of Canadian dollars)

6. Financial risk management (continued):

(b) Liquidity risk (continued):

The following is an analysis of the contractual maturities of the Group's financial liabilities as at March 31, 2014:

Financial liabilities	< 1 year	2-3 years	4-5 years	> 5 years	Total
Accounts payable and accrued liabilities	48,134	-	-	-	48,134
Interest payable on long-term debt	19,634	-	-	-	19,634
Derivative liabilities	5,274				5,274
Provisions	51,801	-	-	-	51,801
Obligations under finance lease, including current portion	1,120	2,825	3,234	38,762	45,941
Long-term debt, including current portion (excluding deferred costs) [1]	270,250	48,000	48,000	979,875	1,346,125
Total financial liabilities – principal only	396,213	50,825	51,234	1,018,637	1,516,909
Interest payable – long-term debt[2]	61,989	106,639	102,590	911,822	1,183,040
Interest payable – obligations under finance lease	1,979	3,793	3,526	9,125	18,423
Total financial liabilities, including interest payable	460,181	161,257	157,350	1,939,584	2,718,372

[1] Carrying value at March 31, 2014, excludes unamortized deferred financing costs of $9.3 million. The majority of the Group's long-term debt relates to acquisition of property, plant & equipment and intangible assets.
[2] Interest payable on long-term debt excludes the variable rate interest payable on Tranche B of the 12 Year loans (note 4(b)).

(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 Group is exposed to interest rate risk associated with short-term borrowings, floating rate debt and the pricing of future issues of long-term debt. As at March 31, 2014, the Group's cash equivalents and short-term investments include fixed rate instruments with maturities of 185 days or less. Accordingly, the Group has exposure to interest rate movement that occurs beyond the term of the maturity of the fixed rate investments. The Group's credit facility and the second tranche of each of the two 12 year loans are at variable rates and are subject to interest rate risk. To manage this risk, the Group maintains between 70% and 100% of its debt portfolio in fixed rate debt, in aggregate. As at March 31, 2014, the Group had approximately three 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, 2014.

6. Financial risk management (continued):

(c) Market risk (continued):

Subsequent to March 31, 2014, the Group refinanced a portion of the Series 04-1 Bonds which matured in May 2014 by issuing a 30 year Cdn denominated fixed-rate bullet bond (note 26). The interest on the new bonds is based on the Government of Canada ("GoC") 30 year Cdn bond plus an applicable corporate spread. As at March 31, 2014, the Group has entered into interest rate forward contracts with a total notional value of $160 million to reduce its exposure to changes in the GoC 30 year Cdn bond benchmark interest rate and has applied hedge accounting. These agreements settle in April 2014 and the impact on net earnings or loss will occur over the next 30 years as the interest on the bond is expensed. During the quarter ended March 31, 2014 the unrealized hedge loss on these contracts was $5.3 million. The effective portion of this unrealized loss of $5.1 million has been recognized in other comprehensive income and the ineffective portion of $0.2 million has been recognized in net earnings.

Foreign currency price risk:

The Group is exposed to risk from foreign currency prices on financial instruments, such as accounts payable and future purchase commitments denominated in currencies other than the Canadian dollar. To manage exposure on future purchase commitments, the Group reviews foreign currency denominated commitments and hedges through derivative instruments as necessary. As at March 31, 2014, the Group has foreign currency forward contracts of $1.2 million (2013: $1.0 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, 2014.

Fuel price risk:

The Group is exposed to risks associated with changes in the market price of marine diesel fuel. The Group 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 Group'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.

6. Financial risk management (continued):

(c) Market risk (continued):
Fuel price risk (continued):

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

Prior to June 25, 2012, the regulatory deferred fuel cost accounts operated as follows:
Any differences between the per litre cost of fuel purchased and consumed (including hedge gains or losses) and the per litre cost of fuel included in the determination of price caps were:

i) for those routes comprising the Northern Route Group;
   a. one-half of the first 5 cents per litre of difference was 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 20(a)), and
   b. any difference beyond 5 cents per litre was 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 was 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 20(a)).

Commencing June 25, 2012, the regulatory deferred fuel cost accounts operate as follows:
Any differences between the per litre cost of fuel purchased and consumed (including hedge gains or losses) and the per litre cost of fuel included in the determination of price caps are:

i) for those routes comprising the Northern Route Group;
   a. the first 5 cents per litre of difference is recorded in deferral accounts for recovery or settlement through future tariffs to customers (note 20(a)).
   b. any difference beyond 5 cents per litre is recorded in accounts receivable or payable for subsequent recovery from or payment to the Province, and

ii) for all other routes;
   a. recorded in deferral accounts for recovery or settlement through future tariffs to customers (note 20(a)).

If the Group was permitted under IFRS to recognize the effects of rate regulation, there would be no effect on comprehensive income from changes in fuel prices.

During the year ended March 31, 2014, the amounts receivable from the Province in relation to fuel cost differences totalled $1.7 million (2013: $1.0 million receivable from the Province).

(columnar dollars expressed in thousands of Canadian dollars)

7. Inventories:

	As at: March 31, 2014	March 31, 2013
Food and retail inventories	4,052	3,436
Fuel inventories	4,433	4,140
Consumable parts and supplies	16,588	15,681
Total	25,073	23,257

8. Obligations under finance lease:

During the year ended March 31, 2011, agreements which constitute a finance 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 Group's proportion of total rentable area.

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

	Minimum lease payments	Executory costs	Imputed interest (4.44%)	Obligation
Less than one year	4,799	1,700	1,979	1,120
Between one and five years	20,527	7,149	7,319	6,059
Later than five years	36,798	13,426	9,125	14,247
Purchase option	24,515	-	-	24,515
Total	86,639	22,275	18,423	45,941
Current portion				(1,120)
Non-current portion				44,821

9. Long-term land lease:

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

Since April 1, 2003, the Group has entered into various agreements with BCTFA to add lands to the existing terminal leases. During the years ended March 31, 2014 and March 31, 2013, no new land costs were added to the terminal leases.

(columnar dollars expressed in thousands of Canadian dollars)

10. Property, plant and equipment:

(a) Continuity of property, plant and equipment:

	Vessels	Berths, building & equipment under finance lease	Berths building & equipment	Land under finance lease	Land	Construction in progress	Total
Cost:							
Balance at April 1, 2012	1,143,640	483,283	52,512	5,412	15,514	21,355	1,721,716
Additions	-	-	-	-	-	84,030	84,030
Revaluation	-	-	-	-	936	-	936
Disposals	(11,043)	(288)	(192)	-	-	(79)	(11,602)
Reclassification	(297)	(73)	73	-	-	-	(297)
Transfers from construction in progress	41,752	25,989	6,897	-	-	(74,638)	-
Balance at March 31, 2013	**1,174,052**	**508,911**	**59,290**	**5,412**	**16,450**	**30,668**	**1,794,783**
Additions	-	-	-	-	-	117,303	117,303
Revaluation	-	-	-	147	(563)	-	(416)
Disposals	(16,469)	(1,459)	(103)	-	-	(45)	(18,076)
Reclassification	45	(67)	-	-	-	-	(22)
Transfers from construction in progress	67,512	41,380	13,300	-	-	(122,192)	-
Balance at March 31, 2014	**1,225,140**	**548,765**	**72,487**	**5,559**	**15,887**	**25,734**	**1,893,572**

(columnar dollars expressed in thousands of Canadian dollars)

10. Property, plant and equipment (continued):

(a) Continuity of property, plant and equipment (continued):

	Vessels	Berths, building & equipment under finance lease	Berths, building & equipment	Land under finance lease	Land	Construction in progress	Total
Accumulated depreciation:							
Balance at April 1, 2012	94,950	22,280	7,979	-	-	-	125,209
Depreciation for the year	96,224	24,443	8,257	-	-	-	128,924
Disposals	(10,945)	(288)	(179)	-	-	-	(11,412)
Reclassification	-	(73)	73	-	-	-	-
Balance at March 31, 2013	**180,229**	**46,362**	**16,130**	**-**	**-**	**-**	**242,721**
Depreciation for the year	96,935	24,575	7,963	-	-	-	129,473
Disposals	(16,257)	(1,459)	(68)	-	-	-	(17,784)
Reclassification	8	(8)	-	-	-	-	-
Balance at March 31, 2014	**260,915**	**69,470**	**24,025**	**-**	**-**	**-**	**354,410**
Net carrying value:							
As at April 1, 2012	**1,048,690**	**461,003**	**44,533**	**5,412**	**15,514**	**21,355**	**1,596,507**
As at March 31, 2013	**993,823**	**462,549**	**43,160**	**5,412**	**16,450**	**30,668**	**1,552,062**
As at March 31, 2014	**964,225**	**479,295**	**48,462**	**5,559**	**15,887**	**25,734**	**1,539,162**

(columnar dollars expressed in thousands of Canadian dollars)

10. Property, plant and equipment (continued):

(b) Other disclosures - property, plant and equipment:

During the year ended March 31, 2014 capitalized financing costs during construction amounted to $1.8 million (March 31, 2013: $0.7 million) with an average capitalization rate of 5.59% (March 31, 2013: 5.64%). The contractual commitments at March 31, 2014 for assets to be constructed totalled $25.9 million (March 31, 2013: $23.1 million).

During the year ended March 31, 2014, the Group received $0.8 million (March 31, 2013: $0.7 million) of rental income earned from buildings held for leasing purposes. These buildings have a cost and accumulated depreciation of $11.9 million and $1.3 million respectively, as at March 31, 2014.

11. Intangible assets:

(a) Continuity of intangible assets:

	Acquired software, licenses & rights	Internally developed software & website	Assets under development	Total
Cost:				
Balance at April 1, 2012	22,785	10,779	14,477	48,041
Additions	-	-	12,935	12,935
Disposals	(357)	-	-	(357)
Transfers from assets under development	1,941	32	(1,973)	-
Balance at March 31, 2013	**24,369**	**10,811**	**25,439**	**60,619**
Additions	-	-	12,701	12,701
Disposals	(152)	-	(56)	(208)
Transfers from assets under development	7,156	705	(7,861)	-
Balance at March 31, 2014	**31,373**	**11,516**	**30,223**	**73,112**

(columnar dollars expressed in thousands of Canadian dollars)

11. Intangible assets (continued):

(a) Continuity of intangible assets (continued):

	Acquired software, licenses & rights	Internally developed software & website	Assets under development	Total
Accumulated amortization and impairment:				
Balance at April 1, 2012	4,050	2,233	-	6,283
Amortization for the year	4,509	2,242	-	6,751
Disposals	(357)	-	-	(357)
Balance at March 31, 2013	**8,202**	**4,475**	-	**12,677**
Amortization for the year	4,852	2,571	-	7,423
Disposals	(152)	-	-	(152)
Balance at March 31, 2014	**12,902**	**7,046**	-	**19,948**
Net carrying value:				
As at April 1, 2012	**18,735**	**8,546**	**14,477**	**41,758**
As at March 31, 2013	**16,167**	**6,336**	**25,439**	**47,942**
As at March 31, 2014	**18,471**	**4,470**	**30,223**	**53,164**

(b) Other disclosures - intangible assets:

There was no impairment of intangible assets during the year ended March 31, 2014 or the year ended March 31, 2013.

Capitalized financing costs during construction for intangible assets for the year ended March 31, 2014 totalled $1.4 million (March 31, 2013: $1.1 million).

During the year ended March 31, 2014, intangible assets totalling $12.6 million (March 31, 2013: $12.4 million) were acquired and $0.1 million (March 31, 2013: $0.5 million) were internally developed.

(columnar dollars expressed in thousands of Canadian dollars)

12. Accrued employee future benefits:

(a) Description of benefit plans:

	Funding status	Administrator	Plan type	Basis of accounting
Public Service Pension	funded	Third Party	Multi-employer defined benefit	Defined contribution
Retirement bonus	unfunded	Group	Defined benefit	Defined benefit
Death benefit	unfunded	Group	Defined benefit	Defined benefit
Long-term disability	funded	Third Party	Multi-employer defined benefit	Defined contribution
Supplemental executive retirement plan	unfunded	Group	Defined benefit	Defined benefit
Sick Bank obligation	unfunded	Group	Defined benefit	Defined benefit
WCB obligation	unfunded	Third Party	Defined benefit	Defined benefit

The Group and its employees contribute to the Public Service Pension Plan (the "Plan"). The Pension Corporation of the Province of British Columbia administers the Plan, including the payment of retirement and post-employment benefits on behalf of employers. The Plan is a multi-employer defined benefit pension plan. Under joint trusteeship, which became effective January 1, 2001, the risk and reward associated with the Plan's unfunded liability or surplus is shared between the employers and the plan members and will be reflected in their future contributions. Sufficient information is not available for this plan to be accounted for as a defined benefit plan.

In addition, eligible employees are entitled to other retirement and future benefits as provided for under the collective agreement and terms of employment. A retirement bonus and a death benefit, both unfunded defined benefit plans and both administered by the Group, 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. Sufficient information is not available for this plan to be accounted for as a defined benefit plan.

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

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

(columnar dollars expressed in thousands of Canadian dollars)

12. Accrued employee future benefits (continued):

(b) Total cash payments:

Total cash payments for employee future benefits for the year ended March 31, 2014, consisting of cash contributed by the Group to its multi-employer defined benefit plans, cash payments directly to beneficiaries for its unfunded other benefit plans, and cash contributed to a third party administrator of an unfunded plan, was $29.0 million (2013: $28.9 million).

(c) Defined benefit plans:

All of the Group's defined benefit plans, except its multi-employer plans, are currently unfunded. The most recent actuarial valuation of the retirement 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. 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 happened on or before December 31, 2013. The most recent actuarial valuations of the WCB obligation, the supplemental executive retirement plan and the Sick Bank obligation are as at March 31, 2013, March 31, 2014 and March 31, 2001, respectively.

During the year ended March 31, 2014, a gain of $0.1 million was recognized in other comprehensive income to reflect the actuarial valuation of the residual liability at March 31, 2013 for workers' compensation claims arising from the Workers' Compensation Board deposit class coverage system.

	Other benefit plans	
Accrued benefit obligations	2014	2013
Balance, beginning of year	18,808	19,565
Current service cost	689	648
Interest cost	760	801
Benefits paid	(2,018)	(2,200)
Actuarial gains	(104)	(6)
Balance, end of year	18,135	18,808

(columnar dollars expressed in thousands of Canadian dollars)

12. 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 2014	Other benefit plans 2013
Fair value of plan assets	-	-
Accrued benefit obligation	18,135	18,808
Funded status of plans – deficit	(18,135)	(18,808)
Accrued benefit liability	(18,135)	(18,808)
Current portion of accrued employee future benefits	2,204	2,204
Accrued employee future benefits	(15,931)	(16,604)

Elements of defined benefit costs recognized in the year	Other benefit plans 2014	Other benefit plans 2013
Current service cost	689	648
Interest cost	760	801
Actuarial gains	(104)	(6)
Defined benefit costs recognized	1,345	1,443

Significant assumptions

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

	2014	2013
Accrued benefit obligation as of March 31:		
Discount rate	5.1%	5.0%
Rate of compensation increase	1.7%	1.9%
Annual employee retention rate	96.2%	96.0%
Employees with eligible dependents at pre-retirement death	43.0%	43.0%
Benefit cost for years ended March 31:		
Discount rate	5.1%	5.0%
Rate of compensation increase	1.7%	1.9%
Annual employee retention rate	96.2%	96.0%
Employees with eligible dependents at pre-retirement death	43.0%	43.0%
Average remaining service period of active employees (years)	7.0	7.0

(columnar dollars expressed in thousands of Canadian dollars)

12. Accrued employee future benefits (continued):

(d) Multi-employer plans:

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

	2014	2013
Public Service Pension Plan contributions (i)	22,129	21,269
Long-term disability plan contributions	4,879	5,477
Long-term disability plan amortization of surplus (ii)	-	64
Total	27,008	26,810

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 funding policy for this plan calls for amortization of individual participating employer deficits and surpluses over 5 years and a 110% funding target for each participant in 5 years. As a result the employer contribution rate was 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 of Canadian dollars)

13. Provisions:

	Wages payable	Claims payable	Total
Balance at April 1, 2012	45,745	1,277	47,022
Provisions arising during the year	55,296	712	56,008
Provisions settled during the year	(51,895)	(296)	(52,191)
Balance at March 31, 2013	49,146	1,693	50,839
Provisions arising during the year	55,280	692	55,972
Provisions settled during the year	(54,623)	(387)	(55,010)
Balance at March 31, 2014	49,803	1,998	51,801

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

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

14. Capital management:

The Group's principal business of ferry transportation requires ongoing access to capital in order to fund operations, satisfy outstanding long-term debt obligations and fulfill future capital asset acquisition obligations. In order to ensure capital market access is maintained, the Group targets maintaining strong investment grade credit ratings (note 6(b)).

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

	As at: March 31, 2014		March 31, 2013	
	$	%	$	%
Aggregate borrowings [1]	1,547,066	81.70	1,497,138	81.73
Total equity before reserves	346,620	18.30	334,665	18.27
Total	1,893,686	100.00	1,831,803	100.00

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

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

Debt service coverage (earnings before interest, taxes, depreciation, amortization, and rent) must be at least 1.25 times the debt service cost and the Group is required to maintain debt service reserves (notes 4 and 6). Incurrence of additional debt is restricted if the debt service coverage ratio is less than 1.5 times the debt service cost and distributions are restricted if the debt service coverage ratio is less than 1.3 times. In addition to these restrictions and requirements, there are other covenants contained in the MTI (May 2004) available at www.SEDAR.com. The Group was in compliance with all of its covenants throughout the years ended March 31, 2014 and 2013.

(columnar dollars expressed in thousands of Canadian dollars)

15. Share capital:

(a) Authorized:

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

(b) Issued and outstanding:

	As at March 31,			
	2014		2013	
	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.

(columnar dollars expressed in thousands of Canadian dollars)

16. Other comprehensive (loss) income:

(a) Continuity of reserves:

	Land revaluation reserves[1]	**Employee future benefit revaluation reserves**	**Hedging reserves**	**Total**
Balance at April 1, 2012	2,177	-	-	2,177
Land revaluation	1,056	-	-	1,056
Balance at March 31, 2013	**3,233**	**-**	**-**	**3,233**
Land revaluation	12	-	-	12
Actuarial gains on defined benefit plans (note 12 (c))	-	104	-	104
Hedge losses on interest rate forward contracts (note 6 (c))	-	-	(5,040)	(5,040)
Balance at March 31, 2014	**3,245**	**104**	**(5,040)**	**(1,691)**

[1] Land revaluation reserves represent the cumulative surplus resulting from changes in fair value of land assets. Land reserve increases during the years ended March 31, 2013 and March 31, 2014, are shown above. During the year ended March 31, 2014 $0.4 million (March 31, 2013: $0.2 million) was recognized in net earnings reflecting a reduction in the fair value of land for which either a reserve had not been established or the balance in the reserve was less than the reduction in fair value.

(b) Other comprehensive (loss) income:

	Years ended March 31, 2014	2013
Items not to be reclassified to net earnings:		
Land revaluations	12	1,056
Actuarial gains on defined benefit plans (note 12 (c))	104	-
Items to be reclassified to net earnings:		
Hedge loss on interest rate forward contracts (note 6 (c))	(5,040)	-
Total other comprehensive (loss) income	**(4,924)**	**1,056**

17. Ferry service fees:

The Group 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 Group 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 has been amended from time to time to, among other things, establish the ferry service levels and the fees for the provision of such service for the second performance term ending March 31, 2012 and for the third performance term ending March 31, 2016.

18. Federal-Provincial Subsidy Agreement:

The Group receives revenue provided to the Province from the Government of Canada pursuant to a contract between the federal and provincial governments 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.

19. Regulated other income:

In May 2012, the Province enacted changes to the Act (Bill 20) that, among other things, includes reservation fees as a regulated tariff for the purposes of determining adherence to price caps established by the Commissioner effective April 1, 2012. These fees were not regulated by the Commissioner prior to April 1, 2012.

20. Economic effect of rate regulation:

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

IFRS does not have a standard for rate-regulated activities and therefore does not allow the recognition of regulatory assets and regulatory liabilities that result from the regulated price cap setting process. Regulatory assets generally represent incurred costs that have been deferred for purposes of rate regulation 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 Group’s regulatory assets are probable of future recovery by considering such factors as applicable regulatory changes. Management believes the regulatory assets at March 31, 2014 detailed below are probable of future recovery and that the obligations represented by the regulatory liabilities will be settled through future tariff reductions.

(columnar dollars expressed in thousands of Canadian dollars)

20. Economic effect of rate regulation (continued):

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

		As at,
Regulatory accounts	March 31, 2014	March 31, 2013
Deferred fuel costs (a):		
Balance – beginning of year	(1,415)	1,256
Fuel costs deferred	14,521	11,266
Surcharges collected	(2,690)	(11,469)
Fuel price risk recoveries from the Province	(1,675)	(1,023)
Other payments from the Province	(1,396)	(1,449)
Interest receivable (payable)	-	4
Tariffs in excess of price cap (b)	(1,195)	-
Balance – end of year	6,150	(1,415)
Performance term submission costs (c)	163	245
Total of regulatory accounts	**6,313**	**(1,170)**
Total regulatory assets (liabilities)	**6,313**	**(1,170)**
Current regulatory assets	**82**	**82**
Total long term regulatory assets (liabilities)	**6,231**	**(1,252)**

(a) Deferred fuel costs:

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

During the year ended March 31, 2014, the Province agreed to pay $1.4 million, to be applied against the balance of deferred fuel costs (2013: $1.5 million).

(columnar dollars expressed in thousands of Canadian dollars)

20. Economic effect of rate regulation (continued):

(b) Tariffs in excess of price cap:

The Act contains provisions which ensure that if tariffs charged by the Group exceed established price caps, the excess amounts collected will be returned to customers through future tariffs. At March 31, 2014, tariffs charged to customers exceeded the price cap by $1.2 million. In accordance with the Commissioner's Memorandum 45, this $1.2 million has been applied to reduce the deferred fuel costs account balance. Tariffs charged to customers on all route groups were below established price caps at March 31, 2013.

(c) Performance term submission costs:

The Commissioner has authorized the Group to defer costs of representation associated with the third performance term. The Commissioner has considered these costs in the determination of the price caps set for the four years beginning April 1, 2012. The Commissioner has not included an allowance for a return on investment for the third performance term submission costs. The recovery period is the four year period of the third performance term, commencing April 1, 2012.

If the Group was permitted under IFRS to recognize the effect of rate regulation and to record regulatory assets and regulatory liabilities, total comprehensive income for the year ended March 31, 2014 would have been $7.5 million higher (2013: $0.3 million lower) as detailed below:

Effect of rate regulation on total comprehensive income	Years ended, March 31, 2014	2013
Regulatory accounts:		
Deferred fuel costs	8,760	(2,671)
Performance term submission costs	(82)	(82)
Tariffs in excess of price cap	(1,195)	2,461
Total increase (decrease) in total comprehensive income	7,483	(292)

(columnar dollars expressed in thousands of Canadian dollars)

21. Net finance expenses:

	Years ended March 31, 2014	2013
Finance expenses		
Long-term debt	70,560	70,605
Short-term debt	663	409
Finance leases	2,027	2,325
Amortization of deferred financing costs and bond discounts	959	981
Interest capitalized in the cost of qualifying assets	(3,179)	(1,856)
Interest rate support (a)	-	(388)
Total finance expenses	71,030	72,076
Finance income	(3,721)	(2,922)
Total	67,309	69,154

(a) Interest rate support:

During the years ended March 31, 2012 and 2011, the Government of Canada agreed to provide $1.6 million and $1.0 million respectively in the form of interest rate support to the Group for major refurbishment of one vessel in each year. During the year ended March 31, 2014 interest rate support recorded as a reduction of interest expense was nil (March 31, 2013: $0.4 million).

The Group 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.

22. Operating Expenses:

During the year ended March 31, 2014, the Group recorded $316 million (March 31, 2013: $309 million) for wages and benefit expenses.

During the year ended March 31, 2014, the Group recorded $126 million (March 31, 2013: $121 million) for fuel expenses.

(columnar dollars expressed in thousands of Canadian dollars)

23. Related party transactions:

(a) Management compensation:

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

	Years ended, March 31, 2014	March 31, 2013
Short-term benefits	1,822	1,731
Post-employment benefits	341	290
Total	2,163	2,021

(b) B.C. Ferry Authority:

In accordance with the Act, the Group is responsible for paying any expenses that are incurred by the Authority, without charge. During the year ended March 31, 2014, the Group paid $175, 218 (March 31, 2013: $165,265) of such expenses.

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

24. Other commitments:

The Group has entered into operating leases for certain building spaces, land and equipment. Lease payments charged to expense during the year ended March 31, 2014 were $0.9 million (2013: $1.1 million).

Future minimum lease payments are as follows:

Less than one year	667
Between one and five years	1,138
More than five years	18
Total	1,823

25. Contingent liabilities:

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

26. Subsequent event:

On April 28, 2014, the Group issued $200 million of senior secured bonds. The Series 14-1 bonds bear interest at 4.289% per annum, payable semi-annually and will mature April 28, 2044. A debt service reserve for these bonds has been established in the amount of $2.3 million.

The net proceeds from the sale of these bonds were, together with additional cash on hand, used to repay the $250 million Series 04-1 bonds, which matured May 27, 2014 and to fund the related debt service reserve.