Reprint
Island Tides
Visit www.islandtides.com for more interesting articles on other BC, national & international topics
Reprint from Volume 14 Number 2 January 31, 2002

Special Report by Patrick Brown

Ferry report recommends privatization, increased tariffs, even bridges

Fred Wright's December report on the fast ferries and the ferry corporation recommends privatization but otherwise provides little that is new since the stakeholder studies of the '90s.

Wright also concludes that, under the current fifteen-year plan for renewal of the fleet, the ferry corporation may not generate sufficient cash flow to pay for the new ships and facilities it will need, even with the new subsidy structure put in place two years ago.

The report, developed to advise the government on its policy towards the ferries, arose out of an election promise to hold an enquiry to determine why the three high-speed catamaran ferries had experienced severe cost overruns and subsequently could not be used on the BC Ferries' routes for which they were intended.

While the enquiry idea was abandoned and this consultant's report substituted, the terms of reference were expanded to include an examination of the structure, finances, and operations of the BC Ferry Corporation. Conversely, the review of the fast ferry project was limited to examining alternative futures for the vessels ranging from selling them to scrapping them, and summarizing what was learned from the experience.

Sale of Pacificats Supported

Separate investigations by Hugh Gordon and the provincial auditor-general, George Morfitt, established that lack of planning and project financial control, combined with a reluctance to report that anything was going wrong, caused the downfall of the fast ferries project. The three Pacificat ferries are now for sale and are used occasionally as back-up on the Nanaimo-Horseshoe Bay route.

After examining a wide range of alternatives, Wright concludes that the best (or rather, least bad) financial return would result from the sale of the three ferries, and recommends that the sales agent, PricewaterhouseCoopers, be given at least two more years to accomplish this.

Cross-subsidization opposed

Wright makes it clear that he feels that each separate route should break-even financially. He is opposed to the historic cross-subsidization of the smaller routes by the Mainland to Vancouver Island routes. His emphasis is on increasing revenue and reducing costs, noting that the Southern Gulf Islands routes 'require six vessels and ten terminals to serve five Island communities with a combined population of $15,000 and lose over $20 million ($1,333 per capita) per year before overhead.'

He goes on to say: 'It is clear from the public input that residents of these Islands are not satisfied with the current level of service. It is equally clear that the existing level of service at the existing tariff is not financially viable. Four of the six vessels serving these routes must be replaced at an estimated cost of over $100 million over the next 15 years. Clearly, now is the time to address this situation.'

The Stakeholder Studies

Stakeholder representatives who spent many days and weeks during the late nineties exploring solutions to these problems will find all this rather familiar.

Wright was probably unaware of the significant efforts made by stakeholder groups and BC Ferries staff to design a schedule for the Southern Gulf Islands that reduced deadhead runs and increased the load factor. This came to nought when it appeared that relocating ferry staff and changing refuelling patterns presented considerable difficulties.

Wright identified some aspects of the Ferry Workers' Union contract, particularly those relating to overtime and split shifts, as contributing to extra costs. These were also discussed by the Stakeholder meetings (sometimes including union representatives) but the corporation identified them as collective bargaining issues.

The Stakeholder recommendations, which were adopted by the government, were:

1. The ferry system represented highway access to Island communities, and this access represented a commitment by the government to the Islands (the government allocated a portion of the gasoline tax to the support of BC Ferries).
2. The ferry system is interdependent and must be considered as a whole, so more profitable routes support less profitable routes but it should break-even overall.
3. Fares should rise at no more than the cost of living. Fares should be equalized on a cost per mile basis, over time. (In the last fare increase, this led to fares on some routes rising by a greater percentage than others.)
4. BC Ferries' debt, which at the time included the costs of the fast ferries and operating losses incurred during a time when the provincial government was trying to reduce subsidies, should be

Island Tides, Box 55, Pender Island, BC, Canada. Phone: 250-629-3660. Fax: 250-629-3838.
Email: islandtides@islandtides.com. Website: http://www.islandtides.com

transferred to the books of the province.

Wright does not consider point #1, rejects the cross-subsidization implied in #2, says that fare increases under #3 may be insufficient and suggests what he calls a 'demand management' (not explained) model for fare-setting, and identifies the amortization and interest costs of the historical debt that was transferred (#4) as a continuing subsidy.

Privatization Recommended

Wright proposes two forms of privatization: the main routes, he says, should be sold to the private sector; and the minor routes should be put out to contract, with decreasing subsidies. First, he says ferry services should be restructured to 'optimize their commercial value' (this is not explained).

For all routes, he states, 'It is significant to note that the primary source of cost savings realized by commercial operations worldwide, as a result of an arm's length relationship with government, derives from the clearer operational focus, reduced overhead, improved operating efficiency and increased labour productivity.'

For the main routes, he offers the following justification: 'Because of the 30 year government monopoly (sic) the market price for ferry service tariffs is unknown. A review of tariffs in other jurisdictions was not conclusive and provided little assistance in this regard. However, it is clear that the private sector would gladly relieve the Province of the burden of providing this segment of the service.'

This is the total of the arguments advanced in the report to justify Wright's privatization recommendations. He provides no details.

Alternatives to Gov. Ferries

'It is important to recognize that the existing level of government subsidy to BC Ferries undermines the viability of alternative delivery models whether they be marine, air, or fixed link alternatives,' says Wright. He suggests that other carriers have access to BC Ferry terminals, and increasing tariffs and/or 'rationalizing' (reducing?) service levels to stimulate private sector participation.

Finally, he suggests that, particularly in the Southern Gulf Islands, the construction of inter-Island toll bridges be considered.

Aside from the expressed wishes of Islanders not to be connected by bridges (this is put most clearly in the Islands Trust Policy Statement), the Stakeholders' Group examined this possibility, and concluded that the only location that this might be cost-effective was between Mayne and Saturna Islands. Even so, studies showed that a simple, small, frequent ferry system run by a couple of Saturna Islanders would be cheaper.

Make the Ferry Corporation Independent of Government

Wright comments that while the Board of Directors and the management of the Ferry Corporation are theoretically responsible for its financial performance, all major management and strategy decisions are still made by the provincial cabinet. These decisions include setting fares and routes, and major capital expenditures, including the purchase and construction of new vessels.

He recommends a 'truly-accountable, independent Board of Directors with responsibility for governing, exempt from political and bureaucratic interference.'

During its work, the Stakeholder group had identified this as a problem, particularly since the Board of Directors proved inaccessible and unresponsive to efforts to discuss many issues. Essentially, however, the government made no changes.

The Strategic Plan

Since the financial changes recommended by the Stakeholders were put into effect, the management of the corporation has developed a strategic financial plan which attempts to forecast ridership, revenue, expenses, and capital expenditure financing for fifteen years in the future. Wright's team analyzed this two ways: they attempted to apply it to the last ten years, and came to the conclusion it would not have prevented losses by the corporation.

Then Wright conducted a sensitivity analysis (a spreadsheet exercise) of the plan covering the next fifteen years, and concluded that the plan, if it worked out, would still result in an accumulated debt of some $325 million at the end of the fifteen-year period.

This appeared to have two causes: the plan aimed at a break-even after depreciation, but the depreciation charged on the existing fleet would not be sufficient to fund the borrowings necessary for scheduled fleet replacements; and the plan assumed that fares would increase at only 75% of the increase in the cost of living, rather than 100%. If fares rose at 100%, the result would be a predicted accumulated debt of $155 million after fifteen years. (For context, consider that the corporation would have spent $1.877 billion on new vessels and terminals during that time, and carried 350 million passengers.)

Wright's team finally designed a series of negative scenarios, ending with a worst case scenario where everything went wrong. This was estimated to result in the rebuilding of BC Ferries debt to $1.2 billion over the next fifteen years.

Wright's conclusion was that the strategic plan would fail, and the corporation would not be able to afford all the new ships it would need, hence, presumably, his recommendations—though he provides no comparable analysis of alternatives. ✐

Island Tides, Box 55, Pender Island, BC, Canada. Phone: 250-629-3660. Fax: 250-629-3838.
Email: islandtides@gulfislands.com. Website: http://www.islandtides.com