Marine Atlantic
Marine Atlantique

Canada

Corporate Plan Summary 2005 ~ 2009

Our Mission

To provide our customers with a safe, environmentally responsible and quality Newfoundland-mainland ferry service in a reliable, courteous and cost-effective manner.

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1.1. Mandate

Marine Atlantic's legislative mandate is the "acquisition, establishment, management and operation of a marine transportation service, a marine maintenance repair and refit service, a marine construction business and any service or business related thereto" (*Marine Atlantic Inc. Acquisition Authorization Act,* 1986*).* Marine Atlantic also fulfills a constitutional mandate originally established by the Terms of Union by which Newfoundland and Labrador joined the Canadian Confederation.

Marine Atlantic's importance within the Newfoundland and Labrador economy and to the people of the province has assured an even broader social and economic mandate for this service. It now plays an essential role in the province's tourism sector, in the importation and exportation of goods, and in the free movement of its citizens. As an extension of the Trans-Canada Highway, it forms a crucial bond within the Canadian confederation, connecting the province of Newfoundland and Labrador to the rest of the nation.

1.2. Legislative Authority

The origin of Marine Atlantic's legislative authority underscores its importance to the people of the Province. In 1949 when Newfoundland (and Labrador) joined the Canadian Confederation, the service was accorded special constitutional status under Term 32(1) of the Terms of Union (*The Newfoundland Act,* 1949). This Term guarantees that Canada will "maintain in accordance with the traffic offering a freight and passenger steamship service between North Sydney and Port aux Basques, which, on completion of a motor highway between Corner Brook and Port aux Basques, will include suitable provision for the carriage of motor vehicles."

The *Marine Atlantic Inc. Acquisition Authorization Act* (1986) established Marine Atlantic as a parent Crown corporation with a mandate to operate a marine transportation service, which it does under contract to Transport Canada.

The *Financial Administration Act* (1985) *(FAA)* requires that Marine Atlantic's records, systems and management practices are maintained to ensure that assets and transactions are safeguarded and controlled, and that the financial, human and physical resources of the Corporation are managed efficiently and effectively. The *Act* also sets out various reporting, governance and transaction authority provisions for Crown corporations.

The *Canada Marine Act* (1998) *(CMA)* and Transport Canada's National Marine Policy directs the Company to "substantially reduce its costs and increase efficiency" and to "commercialize its operations by exploring new vessel management and procurement practices, the commercial operation of vessels, and the streamlining of services". The *CMA* was reviewed in 2003 and “provides for the continuance of constitutional services and the provision of “similar services” on other routes.”

Revenue received from services provided is applied to fund Marine Atlantic’s operational and capital requirements. The balance of funding is provided through fixed-price contracts with Transport Canada. The Bilateral Agreement [1] with Transport Canada sets out the basic principles that govern the Corporation’s relationship with the federal department as well as the terms for executing specific subsidiary agreements under which the Corporation operates its ferry services. Certain other federal legislative and policy requirements - Official Languages, Employment Equity, Alternative Fuels, Privacy and Confidentiality and the Federal Identity program - also govern the Company’s conduct.

1.3. History

A regular steamship service has operated on the Cabot Strait between Nova Scotia and Newfoundland (and Labrador) for more than a hundred years. Begun by the Reid Newfoundland Company in 1898, it connected the Island’s railway to the Canadian system. The Canadian government began providing a subsidy for the service in 1911, which continued until 1924 after the Newfoundland government took over its operation. In 1949, under the Terms of Union between Newfoundland (and Labrador) and Canada, Canadian National Railways assumed responsibility for the service, in addition to the coastal boat service, the St. John’s dry dock and the Newfoundland Railway.

By the Terms of Union, Canada undertook to maintain the existing North Sydney, Nova Scotia to Port aux Basques, Newfoundland (and Labrador) service, and to accommodate the transportation of motor vehicles when a highway link was completed from Corner Brook. In 1968, a summer ferry service was inaugurated between Argentia, Newfoundland and North Sydney to meet a growing demand for this type of service.

The ferry and coastal boat service continued as a wholly owned subsidiary of the Canadian National Railway Company (later CN Marine) until Marine Atlantic Inc. was formed as a parent Crown corporation under the *Marine Atlantic Inc. Acquisition Authorization Act* (1986). The Prince Edward Island to New Brunswick service provided by the Company closed with the construction of the Confederation Bridge in 1997. As well, Transport Canada in its National Marine Policy (1995) and the *Canada Marine Act (1998)* instructed crown corporations to 'commercialize activities' as much as possible. As a result, Marine Atlantic sold all assets of Newfoundland Dockyard Corporation and divested itself of all ferry service routes except those between Newfoundland and Labrador and North Sydney, Nova Scotia.

[1] Bilateral Agreement between Her Majesty the Queen and Marine Atlantic Inc., Department of Transport, March 12, 1987.

Through this period of transition, the Corporation underwent a significant management restructuring in response to its changing mandate, from a regional ferry service to a dedicated Newfoundland-mainland service.

In 2003, Marine Atlantic operated up to four ice-breaking class ocean-going vessels on its year-round Port aux Basques route and its June to September Argentia route, and operated three ferry terminals, in North Sydney, Port aux Basques and Argentia.

1.4. Structure & Governance

Operations: Marine Atlantic's operations are located in both Nova Scotia and Newfoundland and Labrador. Its corporate head office is in St. John's, its finance, accounting and information technology functions are based in Port aux Basques, and its operations and human resources management are located in North Sydney. Operations staff are located in the Company's three ferry terminals at Port aux Basques, North Sydney and Argentia.

Marine Atlantic has one subsidiary company, Newfoundland Dockyard Corporation. With the sale of all its assets in 1997 (Order-in-Council PC 1997-692 and Treasury Board Decision 825331), the Newfoundland Dockyard Corporation exists in name only except for employee severance obligations and workers' compensation liabilities. The surplus distribution following the total wind-up of the Pension Plan[2] for Employees of Newfoundland Dockyard Corporation as of November 30, 1996 occurred in June 2004. The proceeds from that distribution of surplus to the Company amounted to $1,700,757.

Board of Directors*:* Marine Atlantic has a 12-person Board of Directors, which reports to the Parliament of Canada through the Minister of Transport. Board members are typically appointed for two to three-year terms, which can be extended at the discretion of the Crown. The Board meets quarterly and convenes additional meetings as the need arises.

The Board Chairman completed his term in December 2003. To date, a new Chairman has not been appointed by Privy Council. Therefore, the Vice-Chairman of the Board is currently the acting Chair.

Three committees function to support the role of the Board. These are the Audit Committee, the Pension Management Committee, and the Corporate Governance Committee.

Corporate Governance was a focus for the Board of Directors in 2004. All of the Board members participated in a corporate governance training session sponsored by the Privy Council. A strategic planning session was held as part of the CEO assessment process and a job description for the President was finalized. A

[2] The share of the distribution of the surplus was based on a 75/25 sharing formula, with 25 percent going to the company.

corporate operational plan was developed and an update will be provided at each Board meeting. As well, the Board now receives a weekly operations update from the President's office highlighting the major events from the previous week.

During 2004 the Board initiated a training session that focused on best practices for its Audit Committee. The session built on three primary responsibilities of an audit committee. These are: (1) integrity of financial reporting and accountability; (2) adequacy and effectiveness of risk management practices; and (3) adequacy and effectiveness of internal controls. The Board dedicated one day to the session, which was facilitated by a representative from a national public accounting firm.

The Board initiated or participated in various other good governance practices throughout 2004. A stakeholder meeting was held with the Board in June 2004. Representatives from the trucking, tourism, municipalities and economic development areas provided the Board with their view of the service. The Board of Directors continued to be very active in the refinement, development and approval of policies in 2004. Pension Management training is conducted annually by a human resources consulting firm. For the first time, the Board dedicated two days to meeting with senior management to review a draft corporate plan and provide direction before final review by the Board in October 2004.

The Office of the Auditor General (OAG) prepared a Special Examination Report in 2004. Representatives of the OAG met individually with some Board members and made representation on the status of the report to the Board at their regular meetings in 2004.

Management Structure: Organizational changes and management restructuring continued in 2004, as it had for the last number of years. The Director of Marine Operations, Director of Human Resources, Comptroller, Chief Information Officer, Corporate Counsel, Communications Officer, Internal Auditor and Senior Safety Officer report directly to the CEO. Under this structure the reporting levels within operations have been reduced by one senior level, which has streamlined communications within the organization.

1.5. Office of the Auditor General Special Examination 2004

The Office of the Auditor General (OAG) performed a special examination in 2003-2004 in accordance with Section X of the *FAA*. A final report was presented to the Board of Directors in September of 2004. The key areas of concentration for the examination included the safe and environmental responsibilities of the service, the quality service components, and the cost effectiveness of the service. Through the examination criteria, some of the topics discussed included the constitutional obligation, essential nature of the service, managing human resources, long-term asset planning, funding issues, and the historical context. The report commented that the examination had progressed well and there was reasonable assurance that there were no significant deficiencies in the systems and practices examined with the exception of the following items.

The report highlighted two significant deficiencies:

- The Corporation does not have reasonable assurance that its operations are efficient and economical; and
- Initial annual operating agreements with the Minister of Transportation have not reflected the known full cost of providing the contracted service.

From these findings four recommendations were presented to management for responses and these are noted below. These recommendations included:

- Performance expectations – the Corporation should develop and put in place performance measures and targets that will define service expectations and be the basis for accountability to the Board and the government;
  Management Response - Performance measures and targets have been finalized, approved by the Board of Directors and are in place;
- Labour relations – the Corporation should better align its collective agreements and operating requirements, with a view to improving the efficiency of operations;
  Management Response - The Corporation is committed to a long-term approach to improving the efficiency of operations, including increased efficiencies in its use of human resources;
- Vessel replacement – the Corporation should develop a comprehensive vessel replacement plan based on operating needs and full life-cycle costs;
  Management Response - The plan has been developed and the first stage is in place; and
- Annual operating agreements – Working in collaboration with Transport Canada, the Corporation should establish annual operating agreements with the Minister of Transport that include both the full cost of providing the contracted service and the planned level of service performance;
  Management Response - The process has been put in place for 2004 and will continue in the future.

As noted in the responses, management has implemented or are in the process of implementing the recommendations outlined in the report. The Board is active in monitoring management's performance on a regular basis to ensure the objectives of the Corporation are being met.

1.6. Fiscal Year-End

Marine Atlantic Inc.'s fiscal year is currently on a calendar year basis. All funding and reporting requirements with Federal Government Departments is on the Government fiscal year end of March 31. This situation involves developing special reports and constant reconciliation from Company and Federal Government fiscal year ends. In particular, this situation can result in confusion when discussing funding requirements. For the past number of years, the Corporation has been experiencing funding shortfalls and this has become particularly evident in the last quarter of the

Government fiscal year. This being the first quarter of the Company fiscal year, management usually expected to plan and prepare for the coming business season. When funding shortfalls exist these events are suspended for the most part until sufficient cash flow is generated.

In the June 2004 meeting of the Board of Directors, a motion was presented and a resolution was passed "to change the financial year-end of Marine Atlantic Inc. to match the Federal Government's fiscal year-end." Management will be pursuing this change with the relevant Federal Departments.

1.7. Services, Facilities & Assets

Service Levels: Marine Atlantic transports the majority of passenger vehicle traffic between Newfoundland and Labrador and mainland Canada.

Marine Atlantic also transports the majority of the province's freight traffic, with direct water carriers, principally operating out of Montreal and Halifax, carrying the balance. These carriers provide only container and drop trailer service while Marine Atlantic transports all driver-accompanied freight vehicles.

From 1997 to 2002, Marine Atlantic experienced substantial increases in passenger and passenger vehicle traffic, primarily driven by major Newfoundland and Labrador destination marketing and special events, and a strengthening provincial economy.

In 2003 and 2004, the passenger and passenger vehicle volumes regressed to pre-1999 levels. The major issues affecting Traffic in 2004 include:

- Increase in price of gasoline;
- Decrease in tourism volumes in Atlantic Canada;
- Appreciation of the Canadian Dollar;
- Public service strike in NL;
- Aliant strike in Atlantic Canada; and
- Competition from air carriers.

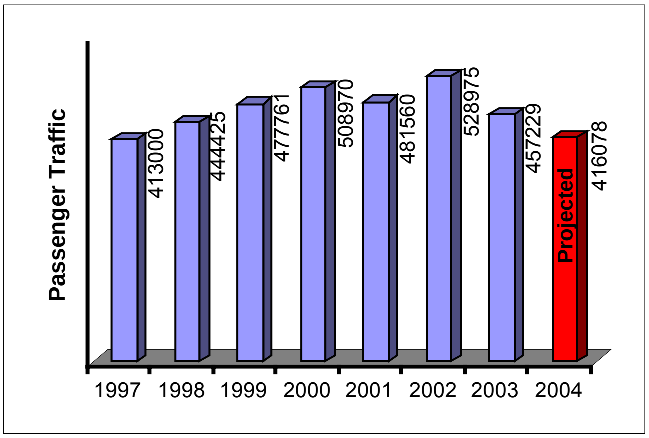

Figure 1: 2004 Passenger Volumes

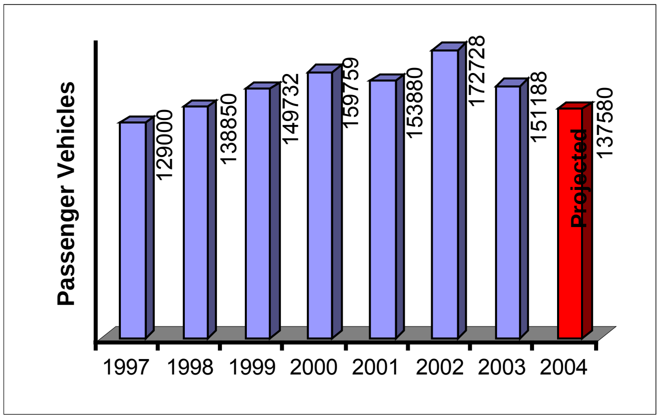

Figure 2: 2004 Passenger Vehicle Volumes

Commercial or freight traffic has continued a steady expansion since 1997, increasing from 68,000 units that year to a projected 85,227 units in 2004. This constitutes a 25 percent increase over this short period. Figures 2, 3 and 4 illustrate these traffic trends.

Overall, projected auto equivalent unit (AEU)[3] traffic expectations for 2004 are slightly below target – Figure 5. Although, the passengers and passenger related vehicles are down from expectations 14%, commercial vehicles have increased 3%.

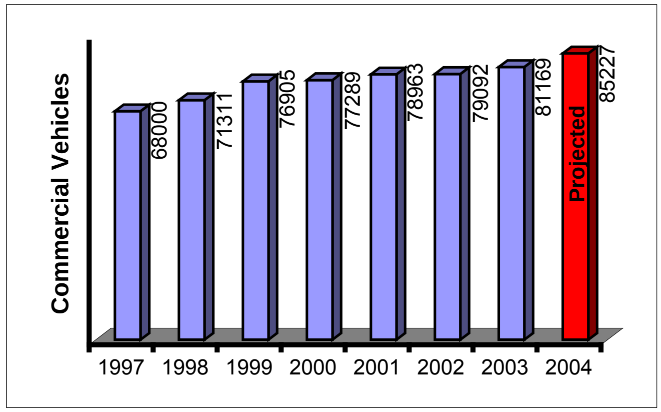

Figure 3: 2004 Commercial Vehicle Volumes

On average, the revenue per auto equivalent unit for a passenger related vehicle is $82.70, and the revenue per auto equivalent unit for a commercial related vehicle is $109.53. The result being that overall expected revenues for 2004 are not forecasted to be down at the same portion as the volumes of traffic.

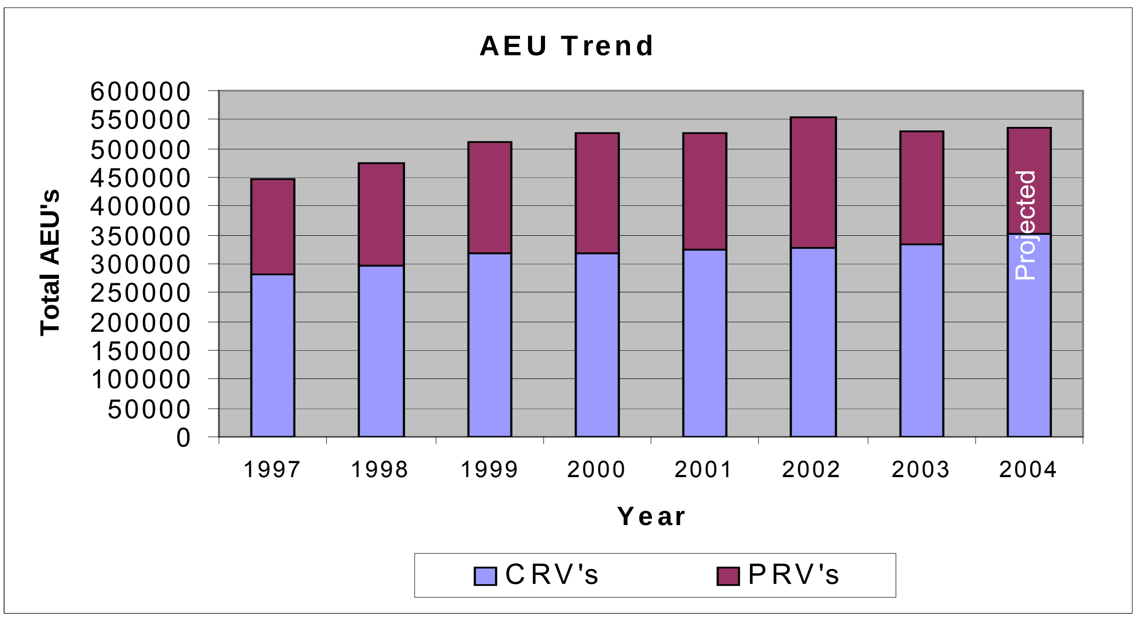

Figure 4: 2004 Auto Equivalent Unit Volumes

Routes: Marine Atlantic's ferries operate year round on the 100-nautical mile run between Port aux Basques and North Sydney (Figure 6). For passengers, passenger

[3] The term AEU (auto equivalent unit) is used in this Plan to indicate vessel capacity information. The company uses AEU as a way of standardizing the measurement of the various types of vehicles carried. I.e., A typical automobile space measuring 20 ft in length would be equivalent to one AEU. A tractor-trailer space measuring 80 feet is four AEUs. I.e., 20 feet of vehicle length equals one AEU.

vehicles and commercial vehicles this route is a continuation of the Trans-Canada Highway between Newfoundland and Labrador and the rest of the country.

The Company also operates a high-demand seasonal service (late June to late September) between North Sydney and Argentia, on Newfoundland's Avalon Peninsula. This 280-nautical mile run significantly reduces the 900-kilometer highway drive from Port aux Basques to the Avalon Peninsula where the majority of the provincial population resides. By providing a circle route across the island, entering on one coast and exiting on the other, visitors and other traffic avoid the need to repeat a ten-hour highway drive across the length of the island. This is a particularly attractive option for tourists.

Fleet: Marine Atlantic's current fleet consists of four ice-breaking class ocean-going vessels:

The *MV Caribou* was built at the Davie shipyard in Levis, Quebec and entered service in 1986 on the Port aux Basques run. It is 179 meters long, has a dead weight of 3,662 tons, and can carry 1,200 passengers and 350 autos. The vessel cost $128,800,000 to construct and has a current book value of $17,700,000.

The *MV Joseph and Clara Smallwood*, a sister ship to the *Caribou*, was also built at the Davie Shipyard in Levis and entered service in 1990. It operates during the winter to Port aux Basques as required, and splits its runs during the summer between Port aux Basques and Argentia. The vessel cost $157,700,000 to construct and has a current book value of $45,800,000.

The *MV Leif Ericson* is similar in vehicle carrying design but has somewhat less capacity and speed than the *Caribou* or *Smallwood*. The 155-meter vessel was built in Norway in 1991, has a dead weight of 4,486 tons and can carry 500 passengers and approximately 300 autos. The *Ericson* was purchased in March 2000 for $58,000,000 and following a thirteen-month charter back to its original owners (Stena Lines) entered service with Marine Atlantic on June 2, 2001. The vessel's registration was changed to Canadian prior to going into service. Including duty and taxes the total cost of the vessel was $76,700,000 and it currently has a current book value of $60,900,000.

The *MV Atlantic Freighter* was built in Asia in 1978 and was acquired for the Port aux Basques run in 1986. It primarily carries freight in the form of trailers without drivers (drop trailers), and dangerous commodities. It is 151 m long, has a dead weight of 8,661 tons and can carry 75 trailers. It can carry only 12 passengers, which limits the number of driver-accompanied tractor-trailers it can transport. In 2003, the Company completed substantial deck plating to enable the vessel to meet its certificate of class. This replacement has resulted in the vessel receiving its certificate and has extended the useful life of the vessel by at least 5 years. The vessel cost $11,900,000 and has a current book value of $2,200,000.

Terminal and Related Facilities: Marine Atlantic also owns three ferry terminals and associated facilities at North Sydney, Port aux Basques and Argentia. In addition to the docks, wharves, piers and vehicle marshalling areas, it also owns a variety of other structures, such as passenger terminals, ticket booths, maintenance facilities and administrative offices. There is also a variety of equipment needed to operate the ferry service, such as service vehicles, maintenance equipment and yard tractors. In Port aux Basques, the Company operates a bulk fuel storage facility with a capacity for 11 million litres of Bunker C and 6.5 million litres of marine diesel oil (MDO).

2. Year 2004 Results

2.1. Operational Performance

Marine Atlantic experienced lower than projected traffic volumes in 2004. The year-to-date traffic statistics[4] indicate an overall decrease in passenger and passenger vehicle traffic for 2004 compared to 2003. However, there is an increase in commercial vehicle traffic for the same period. Forecasted traffic volumes for 2004 compared to actual 2003 volumes are presented in Table 1. Based on forecasted traffic volumes, overall AEU's carried in 2004 are on par with last year.

As described, this drop in passenger traffic offering in 2004 could be a result of the many events that occurred nationally and internationally.

Table 1: Traffic Volume Variances by Type and Service - 2004 vs. 2003

	Port aux Basques Service			Argentia Service			Service Totals		
	2003 Actual	2004 Forecast	Variance %	2003 Actual	2004 Actual	Variance %	2003 Actual	2004 Forecast	Variance %
Passengers	417,965	382,685	(8)	39,264	33,393	(15)	457,229	416,078	(9)
Auto's/Trailers/Campers	133,211	121,476	(9)	13,483	11,707	(13)	146,694	133,183	(9)
Buses	570	537	(6)	109	72	(34)	679	609	(10)
Motorcycles/Bicycles	2,785	2,777	0	1,030	1,011	(2)	3,815	3,788	(1)
Straight Trucks	2,695	2,733	1	124	124	0	2,819	2,857	1
Tractor Trailers	39,314	41,172	5	23	18	(22)	39,337	41,190	5
Trailers Only & Other	38,763	40,968	6	250	212	(15)	39,013	41,180	6
Auto Equivalent Units	480,335	484,699	1	18,332	16,104	(12)	498,667	500,803	0
Trips	2,017	2,010	0	76	76	0	2,093	2,086	0

Of the 1,510 scheduled trips up to 31 August 2004, only 53 had to be rescheduled of which 26 were due to weather conditions. Overall, on-time performance was at 61 percent for this period. Ignoring weather-related delays and rescheduled trips, on-time performance was at 63 percent, a decrease of 2 percent compared to 2003. As

[4] Statistics for the Port aux Basques service are year-to-date ending August 2004 and estimates for remainder of 2004. Argentia service statistics are actual volumes carried in the year.

detailed below, various mechanical related incidents experienced in the year affected this performance.

The utilization of "Management Discretion Sailings" (MDS) in the year has been reduced. In the terminals and the passenger service departments on the vessels, the seasonal staffing levels were reduced from traditional levels. The decision was made to place the *Freighter* in cold lay up (not operating and no crew) earlier than planned.

The Company experienced a significant amount of mechanical and maintenance incidents in 2004. The cost of any of these repairs can be upwards of $100,000 to well over $1 million. These incidents reiterate the fact that there are additional costs associated with operating aging vessels.

With the added capacity of the *Ericson* in 2001, the Company was able to extend the concept of "Management Discretion Sailings" (MDS) again in 2004. This concept enables the Company to provide additional sailings that are included in the operating plan, but not in the published schedules, when demand warrants. The Company intends to increase the number of discretionary sailings in 2005.

There were no major capital projects planned for 2004, although it was a busy year for capital purchases with over 50 projects most of which were under $100,000. The financial profiling of these projects is presented in Section 7.3, Statements F and G.

The Company also made progress in addressing issues identified in the 2004 Corporate Plan. These issues were related to operational performance, customer service, safety and environment, employees and financial performance. A summary of achievements in these areas is provided in the following sections.

2.2. Customer Service

Marine Atlantic continued to build on the considerable momentum started in 2000 to improve all aspects of customer service and to enhance its corporate image with all stakeholders.

Marine Atlantic considers customer feedback as the primary benchmark for evaluating customer service. This is based on independent surveys conducted by an independent organization throughout the 2004 peak summer season. Overall, the 2004 satisfaction scores were on par with previous years. However, the decline in satisfaction relating to the price/cost criteria has fallen significantly from 74 percent in 2003 to 63 percent in 2004 which may in part be explained in Section 10.1. The Corporation will analyze the results and target areas for improvement. Table 2 presents the survey results; percentages indicate those respondents who were either "Completely Satisfied" or "Mostly Satisfied" with the quality of each service. The Company recognizes that maintaining these very high customer satisfaction levels is a performance target.

Table 2: Customer Satisfaction Survey Results

Indicator	Score (%)				
	2000	2001	2002	2003	2004
Overall Quality of Service	96	95	97	97	94
Overall Quality of Vessel Service	96	95	97	98	95
Food Service	96	97	87* / 93**	93* / 97**	95*/95**
Ticketing	94	97	98	99	98
Price/Cost	N/A***	N/A***	71	74	63
Terminal Quality	93	96	97	97	95
Traffic Processing	90	97	93	97	94
Reservations	90	92	97	98	96

* Terminal Food Service
**Onboard Food Service
*** N/A – this area was not assessed prior to 2002.

The use of a customer "Ombudsman" was effective again in 2004, ensuring prompt resolution of customer concerns. The ombudsman's contact information is prominently displayed at all Marine Atlantic locations.

Effective two-way communication with internal and external stakeholders was maintained and enhanced at Marine Atlantic in 2004.

In June 2004, the Code of Practice for Communication was launched by the Canadian Transportation Agency and all Federal Departments and Crown Corporations are expected to comply. The Code will focus on the Multiple Format Policy, website accessibility, telecommunication systems for reservations and information, telecommunications systems in terminals, signage, public announcements in terminals, arrival/departure monitors and other electronic signage, information on ground transportation, and designated seating at boarding gates and departure areas.

In September 2004, the Transportation Agency conducted a benchmark audit questionnaire at the North Sydney terminal for the Communication Code. The Port aux Basques and Argentia terminal will also be completed over the coming year. These survey results will be evaluated and areas for improvement will be identified to ensure compliance with the Code.

Marine Atlantic's independent advisory committee continues to work toward being a leader in providing accessibility to all its passengers. The committee is very active in making recommendations for improvement and communicating the need for accessible transportation options. During the National Transportation Week, two of our employees received the 2004 Awards of Excellence for their significant contributions to improved accessibility services for our passengers. In addition, the

Company continues to implement the requirements identified in the Canadian Transportation Agency's (CTA) Ferry Code of Practice.

Other notable areas for ongoing customer service improvement in 2004 include:

- Refurbished flooring, washrooms and lighting in the crew and passenger areas;
- Improved or upgraded service areas in the cafeterias;
- Improved or upgraded cafeteria and galley equipment,
- Banking machines installed on each ship for customer and crew convenience;
- Addition of our Marine Atlantic Visual Information Screen Show (Maviss) and Information Kiosks to the remainder of the passenger vessels; and
- New amenities for passenger comfort and convenience.

2.3. Safety and Environment

Marine Atlantic continued its commitment to ensure its passengers are transported in a safe and efficient manner. The Company is very committed to developing a safety culture that instills in all employees the concept that "safety comes first". The Company continues to provide a significant amount of safety training.

The Corporation has committed to the development of a complete Occupational Safety and Health program for the entire Company. A baseline audit has commenced which upon completion will provide a strategy for implementation.

The Document of Compliance and all Safety Management Certificates are valid and up to date. The five-year revalidation recognizes that the fleet is managed and operates in accordance with internationally recognized standards for safety. This comprehensive process entails the completion of a Work Instructions manual, Operations manual, Emergency Response manual, Safety Management manual and SOLAS Training manuals.

Some other safety initiatives for the year included the development of a Marine Evacuations System training program, assisting in the development of a Security Plan with a local port authority, developing risk assessment techniques, developing a vessel Safety Officer Program, and partnering with Transport Canada in the development of a Memorandum of Understanding for the Security of the Domestic Ferry Fleet.

2.4. Human Resources

Marine Atlantic Inc has approximately 1,278 employees (916 full time equivalent positions). Bargaining units represent approximately 98% of these employees.

2.4.1. Recruitment and Selection

Due to low employee turnover there was less need to recruit and select new employees in 2004. For entry-level union positions, new employees were selected from the previously established eligibility lists.

The Company has continued to place emphasis on attracting certified officers in engineering, electrical and deck positions.

Qualification requirements for all positions continue to be updated annually and prior to external recruitment campaigns to ensure that those new recruits meet regulatory requirements.

2.4.2. Collective Bargaining

Following the declaration by the Canada Industrial Relations Board (CIRB) in the dispute between Marine Atlantic Inc. and the Canadian Marine Officers Union (CMOU) that there be no reduction in service between the island of Newfoundland and Nova Scotia, CMOU agreed to proceed to binding arbitration to resolve the dispute. That arbitration was held in March 2004 and Marine Atlantic was successful in presenting its case that members of CMOU receive the same annual increases applied to all other employees of the Company.

The question on conflicts in the legislation between the Canada Labour Code and the Terms of Union for Newfoundland and Labrador raised before the CIRB at the inception of the essential services hearings is scheduled to be heard before the Supreme Court of Canada on 30 November 2004. The CIRB ruled it could only make a decision on the Canada Labour Code and not on constitutional issues in 2003.

In June 2004, the Public Service Alliance of Canada (PSAC) was granted a certification order by the CIRB to represent persons holding specified supervisory positions in the Company. Marine Atlantic advised the CIRB that the introduction of a sixth bargaining unit would trigger an application to consolidate bargaining units. That application was filed in August and was for two bargaining units, one to represent shore and one to represent vessel personnel. In addition the submission applied for exclusion of Masters from the bargaining units. Recently, the CIRB rejected the Company's application, and to date no reasons have been provided. The Company is investigating its options in respect to the Board's decision.

As at 31 December 2004, the collective agreements with CMOU, CMSG and CAW (shore and vessel personnel) expire. All unions have provided notice to bargain, however, to date bargaining has not commenced due to the request before the CIRB to defer bargaining until such time as a decision of the Board is received. The Company is reviewing its application to reduce the number of bargaining units as a result of the recent CIRB ruling. There is a potential four collective agreements and one first agreement will have to be bargained in 2005. In addition, the Company could again find itself before the CIRB on the essential service question. The decision of the Board in 2003 was only in respect to the dispute between Marine Atlantic and the CMOU.

2.4.3. Employee Survey

During the summer of 2004 and in line with operational objectives, Marine Atlantic undertook an independent and confidential employee survey. Approximately 800 surveys were completed. The research Company that was hired to administer the survey is presently collating the data and results will be available and released to both management and union personnel in early October.

The Corporation plans to form a committee composed of employees and management that will focus on developing strategies to address any issues that are identified in the results of the surveys.

2.4.4. Training

The majority of training conducted is for mandatory safety and regulatory requirements. The orientation and assessment of new employees to their position and to the organization, continues to be extremely effective. Greater use of onsite training techniques and continued development of recruitment practices is resulting in more effective and efficient use of the training budget.

2.5. Financial Performance

The financial results for 2004 are presented in Table 4. The decrease in passenger traffic resulted in decreased revenues of $2.6 million. The drop in revenues was offset by a decrease in planned expenses of $4.8 million. Capital spending is expected to decrease by $0.3 million, while restructuring costs are expected to remain the same.

Table 3: Financial Results (In $ Thousands)

	2004 Corporate Plan	2004 Forecast	Variance
Revenue	67,751	65,135	(2,616)
Expenses	128,553	123,791	4,762
Operating Subsidy Required	60,802	58,656	2,146
Capital projects	5,682	5,425	257
Restructuring	2,549	2,549	-
Total Operating Requirements	69,033	66,630	1,889

Major financial highlights:

- In 2004, the *Caribou, Smallwood* and *Ericson* continued to consume the less-expensive blended fuel.

- Due to the decrease in passenger traffic, fewer crossings were made creating further fuel savings.

- During 2004, the aging Marine Atlantic fleet experienced a number of mechanical breakdowns and maintenance that could not be anticipated during refit or planned maintenance work. This directly affected the on-time performance as presented in section 2.1.

- As a result of the decrease in passenger traffic, efficiencies were realized on the vessels in the passenger services department and on shore in the terminals and reservations. The labour efficiencies at the terminals and reservations were slightly offset by the extra costs of dealing with vessels off schedule as a result of weather and mechanical incidents.

3. Economic Context

3.1. Significance and Position of Marine Atlantic

The Gulf Service supports the transportation visions of Transport Canada as outlined in that department's strategic document "Straight Ahead"[5].

Transport Canada and Canadian National Rail decided in the late 1980's to eliminate the Newfoundland and Labrador rail service and to substantially reduce the rail service to the Cape Breton portion of Nova Scotia. Consequently, the Trans Canada Highway and Marine Atlantic's short-water service became crucial components in the intermodal and trade and passenger corridors of these areas.

There are only two modes of transportation for visitors to enter the province of Newfoundland and Labrador: by air, or by vehicular transportation using Marine Atlantic's ferry service. Without this alternative to air travel, the province's tourism and transportation sectors would suffer significantly.

The importance of the service to the province was solidified on 18 July 2003, when the Canadian Industrial Relations Board (CIRB) ruled Marine Atlantic provides an essential service. On November 27, 2003, the CIRB further ruled that in the event of a labour strike, there be no reduction in the level of regular ferry service between the island of Newfoundland and Nova Scotia.

[5] STRAIGHT AHEAD - A Vision for Transportation in Canada - Page 17, February 2003.

The Canadian Chamber of Commerce on a recommendation by the St. John's Board of Trade passed a resolution unanimously that the Federal Government should:

1. Designate the gulf link as part of the national highway system to ensure the smooth movement of people and products from province to province; and
2. Declare the gulf ferry service an essential service to avoid the “threat of” or actual labour disruptions.

Newfoundland and Labrador's *Department of Tourism, Culture and Recreation* (TCR) reports that since 1996 to the end of 2002, the province experienced a 47 percent increase in annual non-resident automobile visitors and a 40 percent increase in passenger-related vehicles. The ferry service carried 25 percent of all passengers to and from the province in 2003, providing access to the province for visitors and access to mainland Canada for Newfoundlanders and Labradorians.

The increasing importance of the integrated logistics of the road freight and the roll on roll off (ro-ro) vessels results in an effective combination that reduces logistics times and reduces costs. The commercial freight demand for Marine Atlantic's services has grown significantly. The ro-ro type vessels utilized on the service integrates well with the vehicle freight destined for the Province of Newfoundland and Labrador. In 2001, the Company carried 79,000 commercial-related vehicles carrying nearly 60 percent of all freight movements to and from the Island. In 2004, the number is expected to reach 85,227 units, a 29 percent increase since 1996.

The importance of just in time delivery to suppliers and customers has impacted the Company as it moves over 90 percent of all produce carried to the Island. The Company also schedules regular sailings for the transportation of dangerous or restricted goods carried in commercial units.

The Government of Newfoundland and Labrador reiterated the importance of the service in their report the "Royal Commission on Renewing and Strengthening Our Place in Canada". From the findings the view of Marine Atlantic and the Gulf Service was reported:

- In the view of the Commission, "Term 32(1) requires a quality and affordable Gulf ferry service at a level continually able to meet demand for its use. It is an essential infrastructure component in strengthening the province’s economy….”[6]

While the ferry service is clearly a vital part of the Newfoundland and Labrador economy and its economic capacity, it is also important to the economy of Canada. Visitors who enter Newfoundland by vehicle must also spend time and money in Nova Scotia and the Atlantic Provinces. Likewise, Newfoundlanders and Labradorians leaving and returning to the province benefit the Maritime Provinces’ economies. This is not the case for most air travel.

[6] Newfoundland and Labrador Royal Commission on Renewing and Strengthening Our Place in Canada; February 2003.

Based on these factors, decisions on the future of the service must factor the proper balance between social, economic and environmental elements of providing a sustainable transportation system. Moving people and goods efficiently, safely, securely and in an environmentally respectful way is vital to the national economy. A direct quote from "Straight Ahead" states "there is a growing recognition that passenger and freight rail and marine transportation offer an affordable alternative to other modes of transportation in some areas of the country while contributing to environmental and safety objectives."

3.2. Economic Analysis

3.2.1. World Economic Environment

The world economy recorded growth of 3.1% last year. Growth continued to improve, aided by an accelerating recovery in the U.S. and strong growth in East Asia, particularly China. The rapid appreciation of the Euro against the U.S. dollar was a significant drag on growth in Europe while Japan experienced slow, but improving growth. World GDP is expected to expand by roughly 4.0% in 2004. A strong recovery in the U.S. and robust growth in East Asia combined with lower interest rates in Europe will boost overall economic activity. However, last year's depreciation of the U.S. dollar and restraints on government spending will likely limit the pace of recovery in Europe.

3.2.2. Canadian Economic Environment

The Canadian economy is expected to grow by 2.8% in 2004 aided by a strong U.S. economy, low interest rates, rising commodity prices and further employment gains. Actual real GDP rose 4.3% in the second quarter of 2004, the most rapid growth since 2002. The strength of the Canadian economy in the near term is once again expected to come from consumption, business investment, and exports. Employment growth is not expected to keep pace with GDP growth as businesses strive to increase productivity. On average, forecasters expect employment to increase by 1.8%, down from 2.2% growth in 2003.

3.2.3. Newfoundland and Labrador Economic Environment

Development and production schedules of major projects will continue to have a significant influence on economic growth over the next several years. Real GDP is expected to decline in 2005, premised on the winding down of development work on White Rose and Voisey's Bay, and a further drop in oil production. In 2006, a leap in oil production (from White Rose production and a temporary spike in Terra Nova) and the start of Voisey's Bay production will cause GDP to grow substantially. GDP aside, many indicators are much more stable over the forecast period. This is because changes in mineral and oil production have a greater impact on GDP than on employment and income.

As announced by the Provincial Government of NL, it is continuing to increase the marketing dollars to promote the tourism product of the province. Tourism continues to be a growing services industry in the province. The province continues to target market the Maritimes, Ontario and the eastern seaboard of the US. The Department of Tourism operates on the belief "there's no such thing as an accidental tourist. It takes deliberate action to visit here….". For this reason, the stakeholders of the province expect MAI to provide a level of service that will provide sufficient capacity to bring all people to the island that want to visit. Therefore, the schedule will incorporate the capacity needed to handle the expected traffic offering throughout the entire year and be flexible enough to ensure that if additional capacity is required, extra sailings can be added. The goal is to provide the level of service required "in a safe, environmentally responsible, quality, reliable, courteous and cost-effective manner."

4. Demand Assessment and Projections

4.1. 2004 Traffic Outlook

Following a significant downturn in 2003, there are some encouraging signs that a recovery of demand may be ahead for the Canadian Tourism Industry. Results for the first half of this year demonstrate growth in travel from key foreign markets in Asia and in Europe. Slower growth occurred from the United States and it was confined largely to Ontario.

The Atlantic Provinces tourism outlook was mixed entering the peak season, in particular Nova Scotia's tourism statistics. The amount of traffic entering the province by land fell a total of 16% between 2001 and 2003, while visitors arriving at the Halifax International Airport increased by 21%. June 2004 activity levels lagged behind 2003 for the most part, and the first half of July suggested a further weakening in road traffic. Since 2002, an emerging trend shows more visitors arriving in Atlantic Canada by air and fewer by road. Cheaper airfares, greater air capacity into the provinces and, more recently, increases in gasoline prices, may be contributing to this trend.

Newfoundland and Labrador experienced a similar trend in its traffic over the past couple of years. In a recent article, Tourism numbers for the province are reported as being up in 2004. Traffic through the provincial airports is up 15% while Marine Atlantic Inc.'s traffic is down 9% from last year. With the reduction in road traffic entering the Atlantic Provinces, this obviously is impacting the tourists entering NL through the ferry system.

There were significant increases by direction and traffic type from 1983 to 2004 for Marine Atlantic Inc. traffic. On average, the passenger and AEU's levels have increased by approximately 2% per year. The Corporation's traffic estimates for the year did not materialize as anticipated. The traffic levels for passengers and passenger related vehicles (PRV's) have declined by 9% to the end of August 2004. The major issues affecting traffic in 2004 include the:

- Atlantic Canada road tourism numbers down;
- Price of gasoline;
- Appreciation of the Canadian Dollar;
- Public service strike in NL;
- Aliant strike in Atlantic Canada; and
- Competition from air carriers.

Despite the decrease in passenger related vehicles, commercial traffic increased beyond expectation. Overall CRV traffic is up 5% over last year and 3% above budget. Potential reasons for this increase include:

- NL real GDP growth continues however not at levels experienced early in the new millennium;
- Employment is continuing to grow led by increased construction activity on the White Rose and Voisey's Bay projects and notable on the west coast is the Humber Valley Resort;
- Retail sales were expected to grow by 3.0%;
- Capital investment was expected to increase by 10.5% to almost $4.2 billion in 2004. This increase reflects significant activity at White Rose and Voisey's Bay as well as more offshore oil exploration; and
- Fish landings are expected to remain on par with last year.

Based on these findings, the auto equivalent units (AEU's) for the entire year are forecasted to be 12% down from expected levels for passenger related vehicles and 3% up for commercial related vehicles. The net result is a two-percentage decline in the AEU's anticipated in 2004 – Table 6.

Table 4: 2004 AEU Projections

	2004 Budget	2004 Projection	Variance Units	Variance Percentage
Passenger related vehicles (AEU's)	172,669	152,010	(20,669)	(12%)
Commercial related vehicles (AEU's)	337,224	348,793	11,569	3%
Total	509,893	500,803	(9,090)	(2%)

4.2. Future Traffic Expectations

To predict future passenger and vehicle traffic growth by direction, passenger and vehicle type, Marine Atlantic Inc. utilizes simple linear regression (Linear regression is a statistical calculation used to project future trends based on past volumes).

The analysis this year focused on seasonal periods within the operating year (January to December). The operating year was divided into eight seasonal periods. These periods display unique traffic patterns within the year. These seasonal periods were trended with regression analysis for the past nine years to assist in preparing the expected traffic projections. The Corporation considers this approach a more accurate prediction of future traffic levels. The seasonal approach eliminates anomalies that can potentially exist with the shorter three-week analysis. The seasonal approach analyzes growth in the seasonal blocks throughout the year, thus providing an improved estimation of future traffic expectations. Based upon this analysis, the forecasted percentage traffic growth is shown in Table 7. These growth forecasts are percentage increases above expected 2004 levels and assume no restraints imposed by capacity limitations.

4.3. Operating Plans and Ferry Schedules

The fleet operating plan for 2004 provides for year round ferry service between North Sydney and Port aux Basques, and a seasonal service between North Sydney and Argentia from June to September. The Company plans to maintain this annual number of trips over the planning period unless traffic growth trends and demand patterns warrant adjustments.

Table 5: Traffic Projections by Service

	Taffic Type	Jan-Mar	Apr-May	Jun	July	Aug	Sep	Oct-Nov	Dec
		Annual Growth							
		2005							
PAB Service	Passengers	1.6%	1.9%	1.7%	7.0%	7.0%	0.8%	1.4%	1.4%
	PRV's	2.6%	2.7%	2.4%	7.0%	7.0%	1.8%	1.9%	2.4%
	CRV's	1.8%	2.7%	2.6%	3.0%	3.0%	2.7%	2.7%	2.6%
ARG Service	Passengers			1.7%	7.0%	7.0%	0.8%		
	PRV's			2.4%	7.0%	7.0%	1.8%		
	CRV's			0.0%	0.0%	0.0%	0.0%		
		2006							
		Jan-Mar	**Apr-May**	**Jun**	**July**	**Aug**	**Sep**	**Oct-Nov**	**Dec**
PAB Service	Passengers	1.6%	1.9%	1.7%	4.0%	4.0%	0.8%	1.3%	1.3%
	PRV's	2.6%	2.6%	2.3%	4.0%	4.0%	1.8%	1.8%	2.3%
	CRV's	1.8%	2.7%	2.6%	1.9%	1.6%	2.6%	2.6%	2.5%
ARG Service	Passengers			1.7%	4.0%	4.0%	0.8%		
	PRV's			2.3%	3.0%	3.0%	1.8%		
	CRV's			0.0%	0.0%	0.0%	0.0%		
		2007							
		Jan-Mar	**Apr-May**	**Jun**	**July**	**Aug**	**Sep**	**Oct-Nov**	**Dec**
PAB Service	Passengers	1.6%	1.8%	1.7%	4.0%	4.0%	0.7%	1.3%	1.3%
	PRV's	2.5%	2.6%	2.2%	4.0%	4.0%	1.8%	1.8%	2.3%
	CRV's	1.8%	2.6%	2.5%	2.7%	2.3%	2.5%	2.6%	2.5%
ARG Service	Passengers			0.0%	3.3%	4.0%	0.0%		
	PRV's			0.0%	3.0%	0.0%	0.0%		
	CRV's			0.0%	0.0%	0.0%	0.0%		
		2008							
		Jan-Mar	**Apr-May**	**Jun**	**July**	**Aug**	**Sep**	**Oct-Nov**	**Dec**
PAB Service	Passengers	1.5%	1.8%	1.7%	4.0%	4.0%	0.7%	1.3%	1.3%
	PRV's	2.4%	2.5%	2.2%	4.0%	4.0%	1.7%	1.8%	2.2%
	CRV's	1.7%	2.5%	2.4%	2.7%	2.3%	2.5%	2.5%	2.4%
ARG Service	Passengers			0.0%	0.1%	2.2%	0.0%		
	PRV's			0.0%	3.0%	0.0%	0.0%		
	CRV's			0.0%	0.0%	0.0%	0.0%		
		2009							
		Jan-Mar	**Apr-May**	**Jun**	**July**	**Aug**	**Sep**	**Oct-Nov**	**Dec**
PAB Service	Passengers	1.5%	1.8%	1.6%	2.9%	1.8%	0.7%	1.3%	1.3%
	PRV's	2.4%	2.4%	2.1%	4.0%	4.0%	1.7%	1.7%	2.2%
	CRV's	1.7%	2.5%	2.4%	2.6%	2.2%	2.4%	2.4%	2.4%
ARG Service	Passengers			0.0%	0.1%	0.0%	0.0%		
	PRV's			0.0%	3.0%	0.0%	0.0%		
	CRV's			0.0%	2.0%	0.0%	0.0%		

5. Fleet Renewal and Capacity Upgrade Requirements

Marine Atlantic must satisfy Canada's constitutional obligation to transport all ferry traffic demand "commensurate with traffic offering". The decline in traffic volumes experienced in 2003 and 2004 is not projected to continue into the future. Based on the future traffic projections, the Company could possibly require additional capacity in 2008. However, if traffic growth returns to 2002 levels faster than anticipated, and a constant annualized traffic growth materializes over the plan period, a requirement to address fleet capacity may happen prior to 2008. Establishing appropriate strategies and options to ensure the Company has the capabilities to handle the traffic offering over the five-year planning period and beyond will be very challenging.

Continuing forecasted growth in traffic demand over the next 20 years requires that additional ferry capacity be added. This need must also be viewed in concert with an orderly replacement program required to renew the existing aging fleet.

Fleet renewal and upgrade options are straightforward:

- Purpose-built new build in Canada;
- Purpose-built new build outside of Canada;
- Acquisition of existing vessel(s) built to Canadian standards or European-equivalent standards (with subsequent "Canadianization" requirements) through purchase;
- multiyear full-time charter; or
- multiyear seasonal charter.

The two primary driving forces in the determination of fleet vessel requirements are:

i. The life cycle status of each vessel and its operational condition; and
ii. The overall fleet capacity requirements based on existing and projected traffic demand.

Proper forward planning will ensure that an orderly fleet renewal and capacity upgrade program is carried out efficiently, economically and effectively.

A total fleet replacement strategy is currently being developed which analyzes previously considered strategies and will consider any new strategy that may present itself over the planning period. There is a combination of factors that severely limits the selection of available vessels in the market. In addition, as evidenced in the past and in previous planning documents, with the ever-changing circumstances around the world, consideration has to be given to the fact that there are dynamics at play that either reassert the envisioned strategy or causes a reassessment of that strategy. Therefore, assuming the 25-year life cycle norm for ferries, ignoring any impact of capacity issues, and recognizing the 4-5 years needed for design, regulatory approvals, construction and delivery, funding approvals for a new build for a *Caribou* replacement would be required no later than 2007 with initial expenditures commencing that year. The approval date for a *Smallwood* replacement would be 2012 assuming a shortened design and approval stage. If the *Ericson* were to be replaced with a new build, the funding approval date would have to be no later than 2013.

It is important to note that the availability of suitable passenger ferries changes from year to year on world ferry markets. It is extremely important that purchase or charter approvals be received at least 1-2 years prior to need to ensure a reasonable chance of securing the right vessel at a reasonable price.

6. Operational Plan

The overall Corporate Plan outlines the long-term direction of Marine Atlantic and the operational plan focuses on the operational goals and strategies. The operational plan encompasses components of the previously approved Board Strategic Plan of 2002 and expands on this document to address the key operational areas of the Company. The operational plan outlines the Corporation's Vision Statement, Values Statement, Mission Statement and Service Level Goal.

During 2004, the Board was very active in setting its operational objectives through senior management performance criteria. The plan was reviewed and a process initiated to identify acceptable levels of performance and to identify relevant performance measures to assess the key components of these operational objectives. These sessions resulted in well-defined organizational performance criteria and new performance measures were established.

The Plan defines Marine Atlantic's vision:

> *"To achieve excellence in fulfilling the Federal mandate to provide a ferry service between the mainland of Canada and the province of Newfoundland and Labrador."*

The Plan also includes discussion on the values of the organization. Consistent with the Mission Statement, all decisions and activities at Marine Atlantic are based on the following core values.

Values

Safety - Ensuring the safe passage of all passengers and goods, plus a safe and healthy working environment for all employees.

Environmental Responsibility - Taking appropriate measures to protect our environment, to reduce adverse environmental impact, and to incorporate best practices in all operations.

Quality Service - Ensuring customer satisfaction through the efficient and professional delivery of accessible service.

Reliability - Providing consistent and reliable transportation to our customers, fair and open procurement of goods and services, and equitable hiring and employment practices.

Courtesy - Fostering a working environment that promotes meaningful communication, together with mutual respect, cooperation, honesty, and integrity.

Cost-effectiveness - Ensuring appropriate utilization of resources, and full accountability to our shareholder, the people of Canada.

As affirmed by the Board of Directors, Marine Atlantic's ferry service goal is

"To continue to provide a year round service between Port aux Basques, NL and North Sydney, NS and a seasonal service between Argentia, NL and North Sydney, NS."

Operational Goals and Strategies have been defined and are outlined in Appendix C. These will help guide the organization toward the appropriate actions to accomplish the objectives set for safety, the environment, cost effectiveness, customer service and human resources.

The Board recognizes the operational plan will be reviewed on a periodic basis to ensure its focus is aligned with Board direction for the organization. For this reason, the operational plan is very dynamic and will change to accomplish the long-term objectives of the Corporate Plan.

7. Financial Projections and Borrowing Plan

7.1. Borrowing Plan

7.1.1. Bank Line of Credit

Marine Atlantic has a bank line of credit. Marine Atlantic had to use this line of credit in the first quarter of 2004 and it is a possibility that the company will need to utilize it in the future given the current funding pressures with the increase in pension payments, operating and maintenance costs.

7.1.2. Letters of Credit

On occasion, commercial transactions require letters of credit (typically large-dollar long-lead-time or specialty orders from suppliers) for which the guarantor bank requests a sufficient level of deposits or a bank line of credit as security. Of particular significance, the Province of New Brunswick has requested a standby letter of credit as security against long-term disability liabilities arising from Marine Atlantic's injury claims and its status as a deposit account Company with that Worker's Compensation Board. The bank line of credit supports this letter of credit with the New Brunswick Board.

7.2. Financial Statements

The following Tables (Statements A through G) present Marine Atlantic's financial position and projections over the planning period.

7.2.1. Income Statement, Company Fiscal Year

Statement A

Marine Atlantic Inc.
Corporate Plan 2005 –2009
Income Statement - Year Ended December 31
In $ Thousands

	2003	Plan 2004	Forecast 2004	Plan 2005	2006	2007	2008	2009
Revenues	64,032	67,751	65,135	67,431	69,147	70,918	72,611	74,219
Expenses	104,994	128,553	123,791	123,812	130,283	130,762	144,947	133,223
Depreciation & write down of assets	21,639	21,783	21,504	22,297	22,868	23,158	23,566	26,334
Reduction in provision for capital Assistance	(21,639)	(21,783)	(21,504)	(22,297)	(22,868)	(23,158)	(23,566)	(26,334)
Operating subsidy, Federal Government	40,962	60,802	58,656	56,381	61,136	59,844	72,336	59,004
Newfoundland Dockyard pension distribution	-	(1,700)	(1,701)	-	-	-	-	-
Restructuring payments	2,797	2,549	2,549	1,898	1,180	496	125	15
Federal Government subsidy	43,759	61,651	59,504	58,279	62,316	60,340	72,461	59,019

Note: Restructuring expenses are the severance costs for employees resulting from discontinued operations. They are allocated to fiscal years on a cash basis for corporate plan purposes. For audited financial statements, they are an expense of the year in which the liability is known.

7.2.2. *Funding from Government, Company Fiscal Year*

Statement B

Marine Atlantic Inc.
Corporate Plan 2005 -2009
Funding Required from Government - Year Ended December 31
In $ Thousands

Marine Atlantic	**Plan 2004**	**Forecast 2004**	**2005**	**2006**	**2007**	**2008**	**2009**
Operating expenses	128,553	123,791	123,812	130,283	130,762	144,947	133,223
Less: Revenues	67,751	65,135	67,431	69,147	70,918	72,611	74,219
Operating subsidy	60,802	58,656	56,381	61,136	59,844	72,336	59,004
Restructuring payments	2,549	2,549	1,898	1,180	496	125	15
Capital spending	5,682	5,425	13,806	11,412	5,801	8,162	55,364
Funding through working capital	(7,537)	(9,557)	(15,278)	—	—	—	—
Payment on *Leif Ericson*	9,940	9,940	9,940	9,940	9,940	9,940	21,940
	71,436	67,013	66,747	83,668	76,081	90,563	136,323
Newfoundland Dockyard							
Distribution of pension surplus	(1,700)	(1,701)	—	—	—	—	—
Total Requirement	69,736	65,312	66,747	83,668	76,081	90,563	136,323

Note: Restructuring expenses are the severance costs for employees resulting from discontinued operations.

7.2.3. *Funding from Government, Government Fiscal Year*

Statement C

Marine Atlantic Inc.
Corporate Plan 2005 –2009
Funding from Government, Government Fiscal Year
In $ Thousands

Marine Atlantic Funding Requirement	**2004-2005**	**2005-2006**	**2006-2007**	**2007-2008**	**2008-2009**	**2009-2010**
Operating expenses	124,451	124,516	131,006	131,542	145,684	133,912
Less: Revenues	65,328	67,981	69,697	71,468	73,161	74,769
Operating subsidy	59,123	56,535	61,309	60,074	72,523	59,143
Restructuring payments	2,437	1,711	1,014	346	91	5
Capital spending	5,425	13,806	11,412	5,801	8,162	55,364
Newfoundland Dockyard pension distribution	(1,701)	—	—	—	—	—
Funding requirement deficiency	5,823	—	—	—	—	—
Funding through working capital	—	(1,800)	—	—	—	—
Total Funding Requirement	**71,107**	**70,252**	**73,735**	**66,221**	**80,776**	**114,512**
Government Funding Available						
Reference level available	36,920	36,920	36,920	36,920	36,920	36,920
TC funding of Marine Atlantic (excess)/deficiency	45,927	(2,447)	(4,490)	(4,273)	(3,945)	6,596
Leif Ericson payment	(9,940)	(9,940)	(9,940)	(9,940)	(9,940)	(21,940)
Total Government Funding Available	**72,907**	**24,533**	**22,490**	**22,707**	**23,035**	**21,576**
Funding Requirement Excess (Deficiency)	**1,800**	**(45,719)**	**(51,245)**	**(43,514)**	**(57,741)**	**(92,936)**
Cumulative 2003-2008						**(291,155)**

Note: Restructuring expenses are the severance costs for employees resulting from discontinued operations.

7.2.4. Balance Sheet

Statement D

Marine Atlantic Inc.
Corporate Plan 2005 -2009
Balance Sheet - Year Ended December 31
In $ Thousands

	2003	Forecast 2004	2005	2006	2007	2008	2009
Assets							
Cash	8,037	15,778	500	500	500	500	500
Current assets	11,502	11,500	11,500	11,500	11,500	11,500	11,500
Deferred pension asset	42,281	42,281	27,281	22,281	22,281	22,281	22,281
Fixed assets and deferred charges - net	190,879	174,800	166,309	154,853	137,496	122,092	151,122
Total Assets	252,699	244,359	205,590	189,134	171,777	156,373	185,403
Liabilities and Equity							
Current liabilities	9,982	10,000	10,000	10,000	10,000	10,000	10,000
Other liabilities	49,350	54,522	37,346	36,166	35,670	35,545	35,530
Provision for capital assistance	190,879	174,800	166,309	154,853	137,496	122,092	151,122
Capital stock	258,530	258,530	258,530	258,530	258,530	258,530	258,530
Deficit	(256,042)	(253,493)	(266,595)	(270,415)	(269,919)	(269,794)	(269,779)
Total Liabilities and Equity	252,699	244,359	205,590	189,134	171,777	156,373	185,403

7.2.5. *Statement of Cash Flow*

Statement E

Marine Atlantic Inc.
Corporate Plan 2005 –2009
Statement of Cash Flow - Year Ended December 31
In $ Thousands

	2003	Forecast 2004	2005	2006	2007	2008	2009
Operating Activities							
Net operating costs	(48,862)	(58,656)	(56,381)	(61,136)	(59,844)	(72,336)	(59,004)
Net restructuring costs	(3,012)	(2,549)	(1,898)	(1,180)	(496)	(125)	(15)
Government operating subsidy	51,778	67,225	43,001	62,316	60,340	72,461	59,019
Distribution of subsidiary pension surplus	—	1,701	—	—	—	—	—
Change in non-cash working capital	—	20	—	—	—	—	—
Cash provided by operations	(96)	7,741	(15,278)	—	—	—	—
Financing Activities							
Government capital assistance	4,182	5,425	13,806	11,412	5,801	8,162	55,364
Investing Activities							
Capital assets and deferred charges	(4,182)	(5,425)	(13,806)	(11,412)	(5,801)	(8,162)	(55,364)
Increase (Decrease) in Cash	(96)	7,741	(15,278)	—	—	—	—
Cash, Beginning of Year	8,133	8,037	15,778	500	500	500	500
Cash, End of Year	8,037	15,778	500	500	500	500	500

7.2.6. Capital Plan, Company Fiscal Year

Statement F

Marine Atlantic Inc.
Corporate Plan 2005 –2009
Capital Expenditure - Year Ended December 31
In $ Thousands

	Project	Forecast 2004	2005	2006	2007	2008	2009
Caribou mid-life refit (estimate)	46,739	—	—	—	—	—	46,739
Alternate dock - Port aux Basques	11,031	—	6,357	—	—	—	4,674
Halon replacement (*Caribou*/*Smallwood*/*Freighter*)	4,863	—	1,879	2,984	—	—	—
Second level alternative dock – North Sydney	4,674	—	—	—	—	4,674	—
Refurbish terminal building – North Sydney	2,991	—	—	2,991	—	—	—
Dock fendering	2,804	—	1,215	1,075	514	—	—
Deck replacement - *Freighter*	1,215	—	—	—	—	1,215	—
Pavement upgrades (Port aux Basques, North Sydney)	1,029	—	—	—	—	397	632
Computer system upgrade	1,870	150	500	—	—	—	—
Emerging projects & small projects	18,699	5,275	3,855	4,362	5,287	1,876	3,319
Total Capital Requirements		5,425	13,806	11,412	5,801	8,162	55,364
Cumulative 2004 - 2008							**94,545**

* Emerging projects and small projects are a collection of smaller projects valued under $1 million.

7.2.7. *Capital Plan, Government Fiscal Year*

Statement G

Marine Atlantic Inc.
Corporate Plan 2005 –2009
Capital Expenditure - Government Fiscal Year Ended March 31
In $ Thousands

	Project	Forecast 2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010
Caribou mid-life refit (estimate)	46,739	—	—	—	—	—	46,739
Alternate dock - Port aux Basques	11,031	—	6,357	—	—	—	4,674
Halon replacement (*Caribou*/*Smallwood*/*Freighter*)	4,863	—	1,879	2,984	—	—	—
Second level alternative dock – North Sydney	4,674	—	—	—	—	4,674	—
Refurbish terminal building – North Sydney	2,991	—	—	2,991	—	—	—
Dock fendering	2,804	—	1,215	1,075	514	—	—
Deck replacement - *Freighter*	1,215	—	—	—	—	1,215	—
Pavement upgrades (Port aux Basques, North Sydney)	1,029	—	—	—	—	397	632
Computer systems upgrade	1,870	150	500	—	—	—	—
Emerging projects & small projects	18,699	5,275	3,855	4,362	5,287	1,876	3,319
Total Capital Requirements		5,425	13,806	11,412	5,801	8,162	55,364
Cumulative 2004 - 2008							**94,545**

* Emerging projects and small projects are a collection of smaller projects valued under $1 million.

8. Factors Affecting Operations

The 2000 - 2004 Corporate Plan focused almost exclusively on identifying potential vessels to alleviate the capacity issues of the late 1990's. In early 2000, the Company received authority from the Federal Government to purchase the *Leif Ericson.*

In that plan, the Company suggested it could operate the additional ferry and meet all funding needs with the existing reference level that was set in 1998. The decreases to the reference level are too high to sustain. Since the production of the 2000 Plan many pressures beyond the control of Marine Atlantic Inc. have impacted the financial situation of the Company. Additionally, many of the estimates in the 2000 - 2004 Plan for the operation and maintenance of the additional vessel were not realistic. The 2004 – 2008 Corporate Plan provided a detailed analysis of these differences. Consequently, Marine Atlantic is experiencing significant funding pressures and has been since 2001, the first year the *Ericson* entered service.

8.1. Revenue Considerations

8.1.1. Other Services

A proposed direct water service between Belledune, New Brunswick, and Corner Brook, Newfoundland, was scheduled to begin operation in the spring of 2002. However, as of the date of this report, operations have not commenced, though the selected operator of the service has recently commented in the media that progress is continuing on establishing the service. The focus of this service is exclusively the drop trailer freight business.

A proposed cruiseferry service is being considered from Quebec City with stops in ports throughout Eastern Canada including stops in Newfoundland and Labrador. A Quebec company suggested the cruiseferry idea is very popular in other parts of the world and would work well in eastern Canada. The concept is to transport people in a luxury cruise vessel that also has the capability to carry freight.

Oceanex is a limited purpose trust that operates roll-on, roll-off vessels carrying goods through the ports of St. John's and Corner Brook. The company will take possession of a new 150-metre vessel in the spring of 2005. This ship will increase Oceanex's cargo capacity by 55 percent on the Montreal-St. John's route.

The Provincial Government has commissioned a pre-feasibility study to determine if the idea of building a sub-sea rail tunnel connecting the Northern portion of the province with Labrador is worth consideration. The idea would use trains to carry vehicles between the island and Labrador. This project, if feasible, would take an estimated 12 years to complete therefore it is outside the planning scope of this report.

If these service achieve a successful startup it could impact the plan's projections of traffic for the Gulf service.

8.2. Operating Expense Considerations

8.2.1. Inflation

Canada's inflation policy, as set out by the federal government and the Bank of Canada, aims to keep inflation within a target range of 1 to 3 percent. Therefore, this plan will continue to assume a 3 percent general inflation annually over the planning period.

8.2.2. Fuel Prices

Fuel is the major commodity consumed by Marine Atlantic vessels, accounting for 17 percent of its total expenditures. Since early in 2002, the Company is consuming blended fuel in 3 of its 4 vessels. Since implementation of the project, the Company has realized significant savings due to the consumption of blended fuel.

OPEC's crude oil target pricing is set at US$23-$28 per barrel and expectations were that it would maintain prices at these levels. However, in 2004, prices actually topped the US$53 a barrel mark. The OPEC crude oil target range translates into Marine Atlantic fuel costs of approximately CDN$0.35 to $0.41 per litre for Bunker C and $0.45 to $0.51 per litre for marine diesel oil (MDO). OPEC's long-term strategy team is currently studying the suggestion to raise its price band of $22–28, given the current price trends and the existing range had been set in 2000. With the many factors that can influence the market price of fuel, price volatility will continue to be a reality in the future. Therefore, Marine Atlantic assumes that prices will remain at the current high levels over the planning period.

8.2.3. Pension Plan for Marine Atlantic Employees

The Company has enjoyed a pension contribution holiday since 1 January 1997 however, due to the volatility of the stock market in 2001 and 2002 the market value of the pension plan for solvency purposes has been reduced. While the plan's solvency position has been weakened, the impact has been less severe than for most pension plans due to the plan's investment structure.

Based on this valuation of solvency and funding ratios, future annual Company contributions will again be required in 2004. Actual contributions will vary according to market conditions, therefore for plan purposes the Company will assume these annual contributions.

8.2.4. Workers' Compensation

Workers' compensation benefits are provided in accordance with the *Workers' Compensation Act* of each of the four Atlantic Provinces. Workers injured on the job are provided benefits in accordance with the then current workers' compensation legislation for their province of assigned regular employment. The general arrangements involve claim reporting with the applicable provincial Boards with each Board billing Marine Atlantic for claim payments made plus a loading for administration charges. Such self-insured arrangements apply to Marine Atlantic in all the Atlantic Provinces. The Workers'

Compensation self insured arrangements reflect the cost of the current Gulf Service as well as all predecessor services of Marine Atlantic.

Due to changes in policy at the Workers' Compensation Board of Nova Scotia (WCBNS), Marine Atlantic was required to transfer from a self-insured basis to a payroll assessment basis effective 1 January 2003. The change is on a prospective basis, which means the Board insures future accidents, whereas claims with respect to pre-2003 accidents are on a self-insured basis.

8.2.5. Insurance

In 2004, the financial markets performed relatively well, however the insurance loss ratios have been larger than anticipated. Consequently, this has resulted in decreased insurance company reserves. It is clear that these insurance costs will again be significantly higher for Marine Atlantic in the coming years.

8.2.6. Maintenance Expense

The introduction of the *Ericson* to the fleet in 2001 simply stated added 25 percent to the annual maintenance costs. The increase in capital expenditures and increase in maintenance expenses experienced by the Company over the last few plans reflects the requirement of an increased annual investment in preventative maintenance to ensure the vessels operate safely and effectively.

The Company has worked with Transport attempting to alleviate funding pressures, through strict budgetary control and deferral of capital spending. During these times, the Corporation has in no way compromised the maintenance requirements for its fleet. The maintenance expenses in the plans reflect the actual spending expected based on the anticipated preventative maintenance programs that are in place.

8.3. Additional Operating Expense Considerations

8.3.1. Capacity Utilization

During the summer of 1999, the Company's vessel capacity utilization was 100 percent during the busiest weeks of the summer. Consequently, during this time the cost recovery percentage of the Company ignoring capital and restructuring was 75 percent. The result of this was long line-ups, protests and very dissatisfied customers. In 2000, additional capacity was added with a temporary fast ferry and in 2001 the *Ericson* arrived as a permanent solution to the capacity problem.

With the addition of capacity, traffic will not materialize immediately to bring the capacity utilization up to the immediate desired levels. The correlation is not one to one. Adding capacity does not generate sufficient immediate revenues to offset the extra costs of this capacity. The maintenance and operating expenses to operate a vessel are significant; consequently, additional capacity affects the cost recovery percentage drastically. The expected capacity utilization in 2004 is 77 percent whereas the desired capacity is between 75 - 85 percent for the entire year. However, during the summer period, this utilization rate approaches 85 percent utilization. It is the summer period that will continue to exert pressure on capacity.

8.3.2. Regulatory Requirements

The international marine industry is heavily regulated to ensure the safe operation of vessels at sea. The *Marine Safety Division* of Transport Canada closely monitors the marine industry in Canada. Various acts and regulations govern these activities including the *Canada Labour Code, Marine Occupational Safety and Health, Transportation of Dangerous Goods Act and Regulations, Marine Liability Act and Regulations, Canada Shipping Act and Regulations, Canada Marine Act, and Coasting Trade Act* just to mention a few. Marine Atlantic also falls under the umbrella of the International Maritime Organization (IMO) and was one of the very first companies in North America to voluntarily comply with the International Safety Management (ISM) Code in July 1996. The ISM code is recognized internationally as one of the highest standards for safety and the protection of the environment for shipping related organizations.

Marine Atlantic operations must adhere to the rules and regulations set forth by the various governing bodies mentioned above. These organizations are very dynamic and constant improvements and changes are implemented to regulations and policies to improve the safety of life at sea.

Regulatory requirement changes that have impacted Marine Atlantic include, ship board personnel for A-1 and B -1 survival craft certificates and emergency preparedness at sea training. Changes to the *Canada Labour Code Part II* in 2002 and 2003 resulted in familiarization training for all employees. Other regulatory training requirements conducted include confined spaces, equipment operation, first aid and Marine Advanced first aid.

8.3.3. Succession Management

While the present workforce is well trained and qualified, succession planning and recruitment issues are critically important for Marine Atlantic. For example, there is an industry shortage of certain vessel officer ratings such as chief engineers and second engineers, and recruiting for these positions must now extend beyond the traditional regional and national pools of available candidates. Exacerbating this situation, the Company must compete with the offshore oil industry which offers attractive compensation packages. In addition, there is a worldwide shortage of licensed officers.

The age and service profile for critical positions such as captains, chief engineers, chief officers suggest that a high rate of retirements will occur in the next few years. Marine Atlantic is working to meet the projected shortfall with a continuous recruitment and selection process for engineering officers. The Company must carefully balance the cost-savings from seasonal crew reductions with the risk of losing critical personnel, such as Chief Engineers, 2nd Engineers and Deck Officers who may seek more employment stability. Succession planning is therefore critical to Marine Atlantic's future.

To ensure that the company continues to meet our staffing requirements for shore and vessels, the succession plan is regularly monitored and updated.

8.3.4. Income Security Agreement

Marine Atlantic was a subsidiary of the Canadian National Railway (CNR) until 1986. During the transition to an independent Crown Corporation, many of the collective agreements negotiated with Canadian National became the labour agreements between Marine Atlantic and its unionized workers. A component of all the collective agreements is the Income Security Agreement. The arbitrator at the interest arbitration to resolve the dispute for the first collective agreement between the Company and the Canadian Merchant Service Guild in 2002 also included the Income Security in that agreement.

The purpose of that agreement is to assist employees who are laid off or who are affected by a technological operational and organizational change. The Income Security Agreement provides salary and or retirement benefits if there is a regular or permanent change in the workplace as a result of a technological, operational or an organizational change. The magnitude of the benefits is dependent on the position and whether the change is temporary or permanent.

A temporary change will result in the employee receiving supplemental unemployment benefits. This benefit ensures the employee receives at least 80 percent of their salary if the person is entitled to Employment Insurance benefits.

A permanent change will result in negotiations with the union to sever or restructure the position within the Company. The amount of severance negotiated will be dependent on the age of the employee, the number of years of service, the position, pensionable years of service, etc.

Careful consideration is needed when changes in the work force are being contemplated to ensure expensive permanent changes are weighed against the long-term benefits that will occur.

9. Capital Expenditures

Capital expenditures over the plan period of 2005 - 2009 are profiled in Section 7.3, Statements F and G.

The capital projects relate to capacity, asset renewal, life extension and customer service and have been deferred as much as possible to assist in the funding pressures currently being experienced. For example the alternate dock for Port aux Basques was identified for completion in 2000, however it is now slotted for consideration in 2005. The 2005 Plan outlines the projects that are required over the plan period to ensure the operation continues to provide an effective and efficient, quality service. The deferral of projects jeopardizes the Company's assets and the overall quality of service provided. This point was reiterated in the Office of the Auditors General’s 2004 Special Examination.

There are nine projects within the capital plan each exceeding $1 million.

10. Revenue Options

10.1. Rate Increase

As the major surface link between the province of Newfoundland and Labrador and mainland Canada, Marine Atlantic's role is to accommodate the surface traffic demand for passengers, passenger-vehicles and commercial vehicles. The service is effectively the only highway link to the island province.

A recent survey of North American ferry rates demonstrate that Marine Atlantic's are the lowest for passenger related vehicles and among the two lowest in North America for commercial related vehicles when compared on a cost-per-kilometer basis. The Argentia route has the lowest fare per kilometer for commercial traffic.

Marine Atlantic does not heavily market its services or offer significant promotions. It has concluded that these activities do not provide a positive financial contribution, are contrary to the Company's mandate to accommodate existing demand, and in certain circumstances are subject to criticism by service users and competing private carriers.

Marine Atlantic's ferry service fare structure provides uniform fares for all categories of passenger and vehicular traffic throughout the year. Within this structure, fare discounting is provided for "youth" and "senior" passenger categories, and volume discounting is available for passengers and bus tours. It has been determined that seasonal and time-of-day/week pricing strategies will not result in net additional revenues or operations-delivery improvements. Furthermore, as an essential public transportation service, users and other customer stakeholder groups would criticize many of these alternative fare structure strategies.

This is a very sensitive issue within the province of Newfoundland and Labrador where public focus on Marine Atlantic is constant, both on the level and quality of the service and particularly on our fare structure. In 2004, the rate increases received negative publicity with their announcement in late 2003. Newfoundland and Labrador federal politicians, provincial government departments, municipal governments, stakeholder groups, and the general public in Newfoundland and Labrador communicated their displeasure. With the announcement, the Coalition for Affordable and Assessable Gulf Ferry Service was formed. The group is composed of the Newfoundland and Labrador Carrier's Association, the Newfoundland and Labrador Independent Trucker's Association, the Atlantic Provinces Trucker's Association, the Atlantic Provinces Chamber of Commerce, the Newfoundland and Labrador Manufacturers' Association and the Newfoundland Construction Association. Members of this group met with the previous Minister of Transportation to voice their concern over the rising fares. From this meeting, the Minister suggested that the stakeholders, Transport Canada representatives and Marine Atlantic representatives meet to discuss options for future rate increases and to ensure that the service was an "economic enabler", to the province. Increasing rates beyond existing levels would certainly be seen as an obstacle to that agreed objective. This session is scheduled for the fall of 2004.

The trucking and bus tour industries require significant advance notice of rate changes to factor these additional costs into their tariff structures. It should also be noted that Marine Atlantic has a standing commitment with the trucking industry to give them 60 days notice of any rate increases.

10.2. Fuel Surcharge

In the winter of 2001, the Company implemented an 8.5 percent fuel surcharge. This was introduced to offset the drastic increase in world fuel prices that had commenced in 1999. Marine Atlantic experienced substantially higher fuel expenses as a result of these increases. This percentage increase did not result in a full cost recovery but was a measure to recoup a portion of the escalating expense of fuel. The surcharge remains a component of Marine Atlantic's fare structure despite public pressure to reduce or eliminate it altogether. In consultation with Transport Canada officials, Marine Atlantic implemented a formula-based approach to adjusting the surcharge based on the future price of fuel. However, fuel prices have increased again above 2000 levels, and current fuel prices are still above the formula thresholds necessary to reduce the surcharge.

Based on the OPEC's targeted market price of fuel, the likelihood of fuel prices returning to pre-1999 levels is not expected. Late in 2003, the Company received approval from the Minister of Transport to reduce the 8.5 per cent fuel surcharge by 2.5 per cent with an equal percentage increase amount to the base tariff rate. This proposal was completed in consultation with the Company's commercial customers.

10.3. Marketing and Promotions

Other than this limited promotion activity, Marine Atlantic has concluded that significant marketing and promotion of its services is not appropriate to its mandate and is not effective in generating additional net financial benefits. The Company will nevertheless continue to explore any promotion opportunities that will generate a positive contribution for the Company.

10.4. Ancillary Revenues

Identifying new revenue opportunities is a difficult exercise since the current vessels have limited space available to accommodate additional service initiatives. These vessels are reaching peak passenger capacity during busy periods of the summer tourist season. However, despite these limitations, the Company continues to investigate the market place and explore new revenue generation activities to add value to the bottom line and reduce subsidy requirements.