Atlantic Pilotage Authority

Administration de Pilotage de l'Atlantique

Atlantic Pilotage Authority

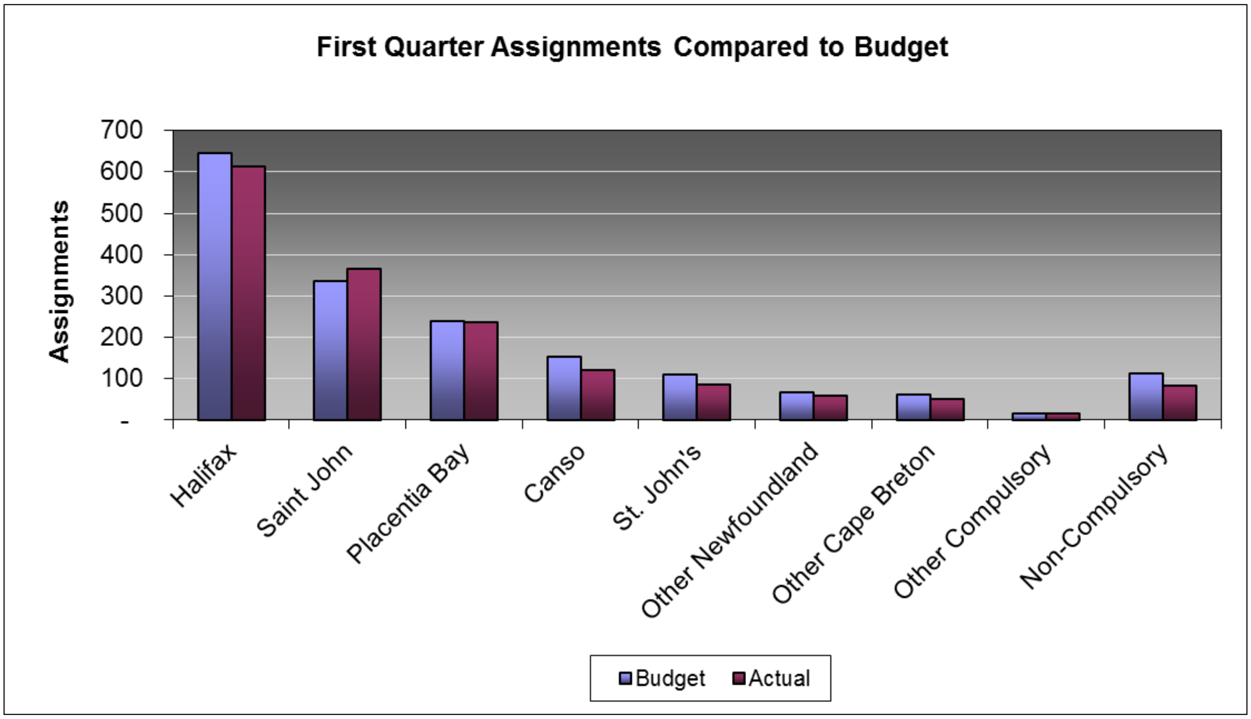
First Quarter 2013

Management's Discussion and Analysis

May 30, 2013

TRAFFIC REVIEW

Pilotage Area	Actual Traffic through 1st Qtr 2012	Budget Traffic through 1st Qtr 2013	Actual Traffic through 1st Qtr 2013	Variance from 2012	Percentage Variance 2012	Variance from Budget 2013	Percentage Variance from Budget 2013
Halifax	625	645	614	-11	-2%	-31	-5%
Saint John	320	337	367	47	15%	30	9%
Placentia Bay	274	239	238	-36	-13%	-1	0%
Canso	157	153	121	-36	-23%	-32	-21%
St. John's	59	112	88	29	49%	-24	-21%
Other Newfoundland	65	67	61	-4	-6%	-6	-9%
Other Cape Breton	63	63	52	-11	-17%	-11	-17%
Other Compulsory	21	17	18	-3	-14%	1	6%
Non-Compulsory	101	115	85	-16	-16%	-30	-26%
Total	1,685	1,748	1,644	-41	-2%	-104	-6%



The following discussion regarding the amount of activity in individual ports is referring to pilotage assignments only, and not the level of cargo or vessel traffic experienced by a port. There are several factors that may result in a difference between the activity reported by the Authority and that reported by another body such as a port authority. These factors include ships not subject to compulsory pilotage, ships utilizing mariners who have pilotage certificates, and the amount of cargo carried on a ship. The Authority reports on pilotage assignments performed by its pilots, but does not track the amount of cargo being carried on a vessel.

Overall, pilotage assignments traffic levels for the Authority are under budget for the first quarter of 2013. Of the four major ports, only the Strait of Canso, NS is significantly below budgeted activity over this period as it is 21% under budget on assignments and 29% under budget on revenue.

The decline in Canso continues a trend that began with a significant reduction in oil tanker activity in the port. The area has a transshipment terminal that supplies refineries along the eastern seaboard of the United States. In the fall of 2011, a refinery in Pennsylvania closed leading to a sharp reduction in shipments to and from Canso. Oil Tanker assignments and revenues for this port have fallen by 70% from the same period just two years ago, the first quarter of 2011.

Piloted assignments for the port of Halifax, NS have declined slightly from the previous year as there were a number of offshore supply vessels needing pilotage in 2012 that have not returned in 2013. The assignments that have been performed have been on larger vessels than the previous year which has made up for the small decline in assignments by earning more revenue per assignment. This is because of a 41% increase in oil tanker pilotage assignments and a 12% increase in container ship pilotage assignments.

In Saint John, NB, the Authority has had 9% more pilotage assignments in the first quarter of 2013 compared to 2012. Pilotage assignments have increased on container ships by 53% and on oil tankers by 29% over the previous year.

Traffic in St. John's has been lower than anticipated. The Authority was expecting increased traffic due to various offshore oil and seismic projects, but the projects have not begun to date. Pilotage assignments in the area had declined recently as masters on regular callers in the port have acquired pilotage certificates allowing them to pilot their own vessels.

FINANCIAL AND STATISTICAL REVIEW

COMPARATIVE REVIEW		
FINANCIAL AND STATISTICAL DATA		
For the quarter ended March 31, 2013		
	2013	2012
FINANCIAL (000'S)		
Total Revenue	$ 4,479	$ 4,464
Operating Expenses		
Salaries, Fees and Benefits	3,005	2,917
Pilot Boats	1,276	1,252
Other	550	549
Total Operating Expenses	4,831	4,718
Loss	$ (352)	$ (254)
STATISTICAL		
Pilotage Assignments	1,644	1,685
Shipping Incidents	1	0
% of incident free assignments	99.94%	100.00%
Customer Complaints Filed	17	8
% of complaint free assignments	98.97%	99.53%

The revenue for the Authority has been very similar to 2012 through the first quarter. A rebound from a poor 2012 is anticipated for 2013, but may not be as strong as budgeted as new projects in several ports have been delayed.

Salaries, fees, and benefits for the first quarter of 2013 have increased from the same period of 2012. This is due to an extra pilot boat crew being added in the third quarter of 2012 for safety purposes, as well as inflationary increases on wages. Pilot boat costs have also increased as the Chebucto Pilot, a new pilot boat, was launched at the beginning of the third quarter of 2012. The first quarter of 2013 includes depreciation and carrying costs of this new vessel.

The tanker traffic lost in Canso is not expected to return in the short or medium term. The Authority is expecting activity in St. John's to rebound later in the year with additional business and expects Saint John to remain strong. Placentia Bay traffic is expected to be down slightly from expectations in the second and third quarter, but should end the year in a solid position. It is still early in 2013, but even with a significant loss in the quarter, the Authority is currently projecting a profit for the year.

The Authority developed a structured methodology for handling complaints several years ago in response to the Ministerial Review of Outstanding Pilotage Issues. The mechanism is designed to be as user friendly as possible, and the goal of the Authority is to ensure that timely feedback is provided to the complainant. The most common reason for a complaint to be submitted is due to a delay in an assignment. In some cases, the delay is caused by factors beyond the control of the Authority, such as weather or delays caused by the non-availability of port services such as tugs.

The Authority received a total of 17 complaints out of a total of 1,644 assignments during the first quarter of 2013. The remaining 98.97% of assignments were performed without receiving a complaint from the customer. For the same period of 2012, there were 8 complaints received out of 1,685 assignments, with the remaining 99.53% of the assignments performed without complaint. All complaints received are included in the above totals, including those submitted that involved delays not caused by the Authority.

Through the first quarter of 2013 the Authority had one minor shipping incident. There were no incidents at this point in 2012.

RISK ANALYSIS

The major financial risk faced by the Authority is the variability of traffic in major ports. The Authority is currently dealing with the significant decline in Canso and is anticipating a decision regarding the sale of the Dartmouth Oil Refinery by year end which may cause a significant variation in traffic for Halifax. The cost structures in these ports are not easily adjusted. Due to the specialized nature and training required to be a marine pilot, reducing the work force in a port is not done to offset short term declines. A reduction in the number of pilots can have significant consequences on the shipping industry with the potential for delays during peak periods, or if the port experiences an unexpected surge in activity. The Authority has also made a significant investment in new vessels that have to be supported through tariff revenue in the ports of Placentia Bay, Halifax, and Saint John.

One major financial risk faced by the Authority has been mitigated by prior action. The increasing cost of fuel, which had a significant negative impact on the cost of operating pilot boats, has been offset by a fuel recovery charge applied to assignments in Halifax, Saint John, Placentia Bay and Canso.

From 2009 through 2011 the Atlantic Pilotage Authority had very strong financial results that offset prior losses and put the Authority in a sound financial position. The Authority had a small accounting loss for 2012, but was able to maintain a strong cash flow while building two new pilot boats. The Authority will be able to absorb a weaker than anticipated 2013 due to its financial health, but will need to take steps to return to a stronger financial position.

First Quarter 2013

Interim Unaudited

Condensed Financial Statements and Notes

Management's Responsibility for Financial Reporting

Management is responsible for the preparation and fair presentation of these quarterly financial statements in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations, and for such internal controls as management determines is necessary to enable the preparation of quarterly financial statements that are free from material misstatement. Management is also responsible for ensuring all other information in this quarterly financial report is consistent, where appropriate, with the quarterly financial statements.

Based on our knowledge, these unaudited quarterly financial statements present fairly, in all material respects, the financial position, results of operations and cash flows of the corporation, as at the date of and for the periods presented in the quarterly financial statements.

R.A. McGuinness Chief Executive Officer	P. MacArthur, CMA Chief Financial Officer

Halifax, Canada
May 30, 2013

ATLANTIC PILOTAGE AUTHORITY

Statement of Financial Position

Unaudited

(in thousands of Canadian dollars)		March 31, 2013	December 31, 2012
Assets			
Current			
	Cash	$ 566	$ 466
	Trade receivables	2,574	3,002
	Prepaid expenses	91	69
		3,231	3,537
Non-current			
	Intangible assets	244	235
	Pilot boats and equipment	11,120	11,137
		11,364	11,372
		$ 14,595	$ 14,909
Liabilities			
Current			
	Trade and other payables	$ 1,579	$ 2,475
	Bank loans	343	1,330
	Employee severance benefits	75	62
		1,997	3,867
Non-current			
	Bank loans	3,912	2,003
	Employee severance benefits	1,382	1,383
		5,294	3,386
		7,291	7,253
Equity			
Retained earnings		7,304	7,656
		7,304	7,656
		$ 14,595	$ 14,909

The accompanying notes are an integral part of these financial statements.

ATLANTIC PILOTAGE AUTHORITY

Statement of Comprehensive Income

Unaudited

(in thousands of Canadian dollars)		Three Months Ended March 31 2013	2012
Revenues			
	Pilotage charges	$ 4,458	$ 4,451
	Other income	21	13
		4,479	4,464
Expenses			
	Pilots' fees, salaries and benefits	2,254	2,225
	Pilot boats, operating costs	1,022	1,047
	Staff salaries and benefits	376	349
	Pilot boat crews' salaries and benefits	375	343
	Amortization and depreciation	254	195
	Transportation and travel	145	142
	Professional and special services	177	165
	Utilities, materials and supplies	94	71
	Rentals	67	75
	Finance costs	35	45
	Communications	27	30
	Training	5	31
		4,831	4,718
Loss for the period		(352)	(254)
Other comprehensive loss		-	-
	Actuarial loss on employee severance benefits		
Other comprehensive loss		-	-
Comprehensive loss		$ (352)	$ (254)

The accompanying notes are an integral part of these financial statements.

ATLANTIC PILOTAGE AUTHORITY

Statement of Changes in Equity

Unaudited

(in thousands of Canadian dollars)	Three Months Ended March 31 2013	2012
Retained earnings, beginning of the period	**$ 7,656**	$ 7,861
Loss for the period	**(352)**	(254)
Other comprehensive loss	**-**	-
Total comprehensive loss	**(352)**	(254)
Retained earnings, end of the period	**$ 7,304**	$ 7,607

The accompanying notes are an integral part of these financial statements.

ATLANTIC PILOTAGE AUTHORITY

Statement of Cash Flows

Unaudited

	Three months ended March 31	
	2013	2012
Operating Activities		
Receipts from customers	**$ 4,886**	$ 5,188
Payments to and on behalf of employees	**(3,167)**	(3,303)
Payments to suppliers	**(1,544)**	(1,508)
Other income received	**21**	13
Net cash provided by operating activities	**196**	390
Investing Activities		
Purchases of intangible assets	**(23)**	(1)
Purchases of pilot boats and equipment	**(995)**	(503)
Net cash used in investing activities	**(1,018)**	(504)
Financing Activities		
Proceeds from bank loan	**1,000**	-
Repayment of bank loan	**(78)**	(62)
Net cash provided by (used in) financing activities	**922**	(62)
Increase (decrease) in cash	**100**	(176)
Cash, beginning of the period	**466**	3,356
Cash, end of the period	**$ 566**	$ 3,180
Supplementary Disclosure		
Finance costs paid	**$ 35**	$ 45

The accompanying notes are an integral part of these financial statements.

1. General Information and Basis of Presentation

The Atlantic Pilotage Authority (the Authority) was established in 1972 pursuant to the *Pilotage Act*. The principal registered address of the Authority is 2000 Barrington Street, Halifax, Nova Scotia. The objects of the Authority are to establish, operate, maintain, and administer a safe and efficient pilotage service within designated Canadian waters. The *Pilotage Act* provides that pilotage tariffs shall be fair, reasonable, and sufficient, to permit the Authority to operate on a self-sustaining financial basis. Under the *Pilotage Act*, no payment to the Authority may be made under an appropriation by Parliament to discharge an obligation or liability.

The Authority is a Crown corporation listed in Schedule III, Part I of the *Financial Administration Act* and is not subject to the provisions of the *Income Tax Act*.

The Atlantic Pilotage Authority is classified as a Government Businesses Enterprise (GBE). As a GBE, the Authority prepares its statements in accordance with International Financial Reporting Standards (IFRS), as issued by the Accounting Standards Board (AcSB).

These financial statements have been prepared in accordance with the Treasury Board of Canada Standard on Quarterly Financial Reports for Crown Corporations. In accordance with the Treasury Board of Canada Standard, these financial statements do not include all of the financial statement disclosures required for annual financial statements and should be read in conjunction with the Authority's Canadian GAAP annual consolidated financial statements for the year ended December 31, 2012. In management's opinion, the financial statements reflect all adjustments that are necessary for a fair presentation of the results for the interim period presented.

The Authority has historically experienced greater demand for its services in the second and third quarters of the calendar year and lower demand in the first and fourth quarters. This demand pattern is principally a result of the high number of cruise vessels visiting the area during the summer and autumn months. The Authority has substantial fixed costs in its cost structure that do not meaningfully fluctuate with pilotage demand in the short term.

2. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies are as follows:

(a) Financial instruments

Trade receivables, classified as loans and receivables, and trade and other payables, classified as other financial liabilities, are initially measured at fair value and subsequently measured at amortized cost. Due to their short-term nature, the amortized cost of these financial instruments approximates their fair value.

Bank loans are classified as other financial liabilities and are initially measured at fair value. After initial recognition, bank loans are measured at amortized cost using the effective interest method.

The Authority is not party to any derivative financial instruments or hedges.

(b) Intangible assets

The Authority's intangible assets are comprised of purchased software. When the software does not form an integral part of the machinery or computer hardware to which it relates, it is separately accounted as an intangible asset. Intangibles are carried at cost less accumulated amortization and impairment losses. Amortization is charged on a straight-line basis over the estimated useful lives of the intangible assets. Estimated useful lives and amortization methods are reviewed at the end of each year.

The useful lives used in the calculation of amortization for purchased software is 5 to 10 years.

Intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amounts may not be recoverable. Assets not in use are tested for impairment annually. Any impairment is recognized in comprehensive income and is measured as the amount by which the carrying amount exceeds its fair value.

(c) Pilot boats and equipment

Pilot boats and equipment are recorded at cost. The cost of pilot boats under construction includes design, project management, legal, material, direct labour, and interest on construction loans. Amounts included in pilot boats under construction are transferred to the appropriate pilot boat classifications upon completion, and depreciation commences. Depreciation of pilot boats and equipment is calculated on a straight-line basis and is based on the estimated useful life of the assets as follows:

Pilot boat hulls and structures	10 to 25 years
Pilot boat equipment	10 years
Pilot boat generators	5 years
Pilot boat engines	5 to 10 years
Pilot boat inspections	4 to 5 years
Furniture and equipment	4 to 10 years
Leasehold improvements	10 years

Assets that are not in use are tested for impairment annually. Any impairment is measured as the amount by which the carrying amount exceeds its fair value and is recognized in comprehensive income. Gains or losses arising on the disposal of pilot boats and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognized in profit or loss. Gains are recognized within other income, while losses are recognized in pilot boats, operating costs, or utilities, materials and supplies depending on the assets that were disposed.

(d) Employee severance benefits

Employees are entitled to specified severance benefits as provided for under collective agreements or employment contracts, based on their years of service and final salary. The liability for these payments is estimated and recorded in the accounts as the benefits accrue to the employees.

The costs and the benefit obligation are actuarially determined using the projected unit credit method prorated on service that incorporates management's best estimate of the rate of employee turnover, retirement age, future salary and benefit levels, and other actuarial factors.

Actuarial gains and losses are recognized in the period in which they occur and are included in other comprehensive income.

(e) Pension plan

Substantially all of the employees of the Authority are covered by the Public Service Pension Plan (the "Plan"), a contributory defined benefit plan established through legislation and sponsored by the Government of Canada. Contributions are required by both the employees and the Authority to cover current service cost. Pursuant to legislation currently in place, the Authority has no legal or constructive obligation to pay further contributions with respect to any past service or funding deficiencies of the Plan. Consequently, contributions are recognized as an expense in the year when employees have rendered service and represent the total pension obligation of the Authority.

(f) Revenue recognition

Revenues from pilotage charges are recognized when pilotage services are provided.

(g) Accounting standards issued but not yet effective

Accounting standards issued but not yet effective which are expected to be relevant to the Authority include:

IAS 19, "Employee benefits" (amended)

The International Accounting Standards Board (IASB) has revised the standard for employee benefits. Actuarial gains and losses will be recognized immediately in other comprehensive income and may no longer be deferred and amortized. The new standard is effective for fiscal years beginning on or after January 1, 2013. The Authority has recognized the actuarial gains and losses immediately in other comprehensive income since the transition to IFRS. Therefore, this amended standard will have no impact on the financial statements.

3. USE OF ESTIMATES AND JUDGEMENTS

The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, and revenue and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and further periods if the review affects both current and future periods.

Judgments made by management in the application of IFRS that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the current and following fiscal year are discussed as follows.

(a) Critical accounting estimates

Critical accounting estimates are estimates and assumptions made by management that may result in material adjustments to the carrying amount of assets and liabilities within the next year. Management has made the following critical accounting estimates or assumptions in preparation of these financial statements:

Employee severance benefits

The Authority engaged an external actuary to assess the fair value of its employee severance benefits. The Authority assesses this obligation at December 31 each year.

(b) Critical accounting judgments

Critical accounting judgments are accounting policies that have been identified as being complex or involving subjective judgments or assessments.

Amortization and depreciation rates

Refer to Notes 2(b) and 2(c) for the estimated useful lives of pilot boats and equipment and intangible assets.