Washington State Ferries

Progress Report

July 1, 2001 – June 30, 2003

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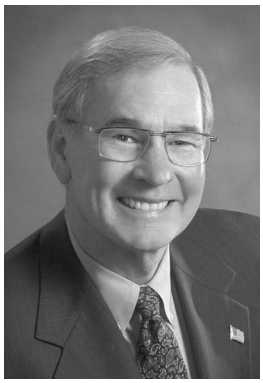
The ferry system continues to evolve

Welcome to Washington State Ferries Progress Report. Our goal is to provide taxpayers, elected officials, and ferry riders information about the ferry system and the specific progress we are making on various significant projects.

This report covers the time period of July 1, 2001 through June 30, 2003 and showcases the most significant events from that time period.



Accountability is an important aspect in government and state agency business. We feel an obligation to our customers and legislators in showing the stages of our progress and development on key projects. This report highlights recent accomplishments, and gives a brief look at next steps for these key projects.

The ferry system's green and white vessels are a symbol of the Northwest, having carried passengers over the waters of Puget Sound for 52 years. The ferry system continues to evolve to meet the demands of changing times, as we implement new ways of doing business that increased efficiency and customer satisfaction.

We thank you for your interest in the ferry system, and appreciate your continued support.

Mike Thorne
Director/CEO

I] Introduction

Washington State Ferries (WSF) is the nation's largest ferry system, serving eight counties in Washington and sailing international waters to Vancouver Island, British Columbia. The ferry system consists of ten routes, serving 19 terminals utilizing 28 vessels. Washington State Ferries is considered a marine highway, transporting thousands of commuters, students, commercial shippers and tourists across Puget Sound. Washington State Ferries is also one of Washington State's largest tourist attractions, and is a cultural icon of the Northwest.

the nation's largest ferry system

The Ferry System

Mission

It is Washington State Ferries' mission to provide safe, reliable, and efficient marine transportation for people and goods throughout Puget Sound.

Vision

It is our Vision to be the most efficient and affordable, customer focused ferry operator in the world.

Washington State Ferries is:

A marine highway
A transit agency
A mover of freight and goods
An environmental steward
A source of tourism and economic development
A key link in regional transit connections
A model employer with a highly skilled, professional workforce

A Marine Highway

The ferry system is an essential part of western Washington's highway network. It provides a critical link between the urban areas on the east side of Puget Sound and the growing communities to the west on the Kitsap Peninsula, as well as more rural destinations on the Olympic Peninsula.

- In 2003, nearly 11 million vehicles were transported along 200 miles of marine highways. During a peak hour, WSF has the capacity to move approximately 2,500 vehicles. During a typical day, WSF moves approximately 30,000 vehicles.

- WSF operates approximately 500 sailings per day, which provide for the movement of people and goods across Puget Sound. For the communities of Vashon Island and the San Juan Islands, WSF provides the only practical link for vehicles – personal and commercial - to the mainland.

A Transit Agency

The State Legislature defined WSF as a mass transportation system in 1974.

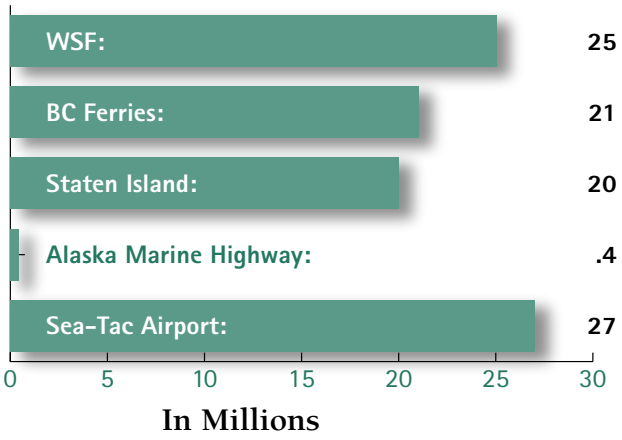
WSF is the largest ferry transit system in the United States and one of the busiest.

- WSF is the second largest transit system in Washington State, second only in ridership to King County Metro, and operates the largest fixed guideway transit system in the State.

- Commuters account for 50% of annual ridership. WSF connects people to jobs and spends a large part of the day taking people to and from work. On the busiest commuter route, Bainbridge to Seattle, WSF carries 18,000 people per day.

- For comparison purposes, a Jumbo Mark II class ferry boat used on the Bainbridge to Seattle run has the equivalent carrying capacity of 208 12-seat vanpools, 59 - 40 ft buses or 17 commuter rail cars.

Number of Passengers Served in 2002



A Key Link in Regional Transit Connections

Customers want the ability to transfer seamlessly from ferries to other transit modes such as commuter rail, buses, and monorail. Transportation options and facilities that provide this transition are referred to as multi-modal.

WSF's vessels and facilities form a critical link in the State's network of multi-modal connections. WSF works with local transit providers to ensure seamless connections between marine transportation and vanpool, auto, pedestrian, bicycle, bus, trolley, commuter rail, monorail, freight and local transportation modes.

WSF encourages mass transit use by providing priority loading for freight, bicycles, vanpool and carpool, park & ride lots at ferry terminals, and schedule coordination with regional transit partners.

A Highly Skilled, Professional Workforce

WSF reexamines staffing levels on a regular basis to ensure they are appropriately meeting the ferry system's business requirements.

What is sometimes most telling in terms of gauging the appropriateness of staffing levels for an organization is how they compare to those of similar organizations. In 1998, a performance audit of the ferry system was conducted. The objective of the audit was to evaluate how efficiently, effectively, and economically WSF is operated.

The audit made comparisons between other ferry systems serving relatively large-scale passenger and vehicle markets (BC Ferries, North Carolina State Ferry System, Staten Island Ferry System, and Nantucket Steamship Authority). The study found that WSF compares favorably with other auto-passenger systems in terms of total cost per passenger, per vehicle, and per mile. In terms of operating cost per passenger and vehicle, WSF is the lowest of the five systems that were evaluated.

The study made a close comparison between WSF and BC Ferries, with respect to staff size. The audit report found that BC Ferries employs more people than WSF in almost every labor category, and in total, its staff outnumbers that of WSF more than two to one. Specifically, WSF at the time of the study employed 1,693, while the BC system employed nearly twice that, or 3,098, and a higher percentage of the WSF employees (39 percent vs. 31 percent) served in the fleet.

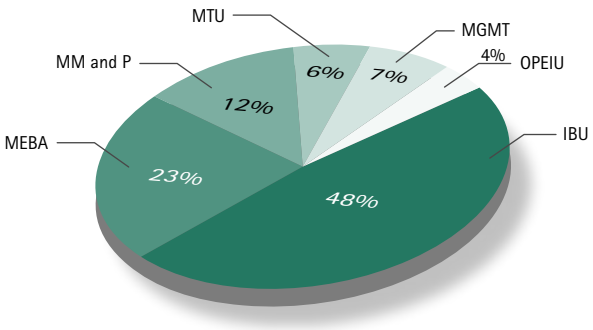
The study also found that, while WSF did employ a higher percentage of technical and engineering staff, the BC system had a correspondingly higher proportion of management and staff personnel.

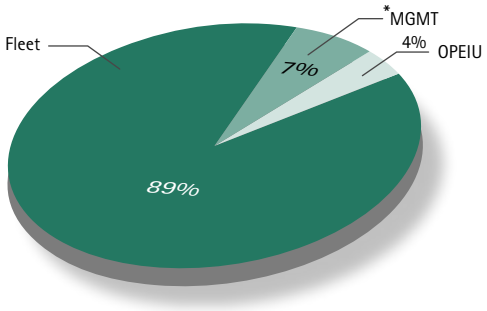
There are several factors that determine specific staffing levels at the ferry system, including an increased emphasis on protecting the public's investment in existing facilities, both vessels and terminals. As the vessels and terminals age, preserving and maintaining them requires a certain level of engineering, management, and administrative staffing to plan, design, and implement vital preservation projects.

The ferry system has publicly committed to frequently reviewing its staff levels to ensure efficiency.

Washington State Ferries Staffing Levels

As of: 30 June 2003





Key

IBU - Inlandboatmen's Union of the Pacific

MEBA - Marine Employees Beneficial Association

MM & P - (IOMM & P) - International Organization of Masters, Mates, and Pilots

MGMT - Includes managerial admin staff, vessel and terminal engineering, operations management, finance and human resources personnel.

MTU - Consortium (PSMTC - Puget Sound Metal Trades Council)

OPEIU - Office and Professional Employees International Union

SEIU - Service Employees International Union

II] Key Accomplishments

Every accomplishment is meant to align with the ferry system's strategic goals, preparing the ferry system to be more self-sufficient and to provide a high level of service that continues into the future.

Accomplishments align with ferry system goals

The Strategic Plan

In the fall of 2002, following an analysis of business and financial fundamentals, Washington State Ferries defined four Strategic Goals. They are:

1. Continually improve and refine our business processes
2. Broaden our revenue base and reduce costs
3. Promote and assist in the planning of regional transportation centers
4. Re-define who we are

The Strategic Goals acknowledge that traditional funding sources will be limited in the future. The Strategic Goals assume that the ferry system must identify and generate new sources of funding to provide a sustainable future.

To carry out these goals, Washington State Ferries formulated the Business and Capital Funding Plans.

The "5+5+5" Business Plan means that the ferry system is responsible for reducing costs by 5%, capping ferry fare increases at 5%, and generating 5% in new revenues with a comprehensive retail, marketing, and advertising program. Under this new plan, the ferry system proposes to recover 90% of its operating costs by 2008 with revenues generated by the ferry system (in fiscal year 2003 we covered approximately 73%).

The Capital Funding Plan builds on the Business Plan to address the ferry system's urgent capital needs. The plan provides funding for much-needed major maintenance projects and new vessel construction. It's a straightforward formula:

Service reductions + vessel retirements = less preservation work
Less preservation work = funding for critical capital investments

The Strategic Plan provides a sustainable future for the state ferry system through a focus on refining our business practices, broadening our revenue base and investing in our capital infrastructure. Facts, figures and more information on the Strategic Plan can be found in Chapter Four, page 20.

Safety and Security

For the past eight years, the ferry system has been working on a comprehensive set of safety enhancements in response to Coast Guard requirements regarding lifesaving measures (known as Title 46, Code of Federal Regulations, Subchapter W.)

The regulations of Subchapter W stipulate the required lifesaving equipment, plans, and training for all vessels, including all WSF vehicle ferries.

WSF submitted a comprehensive Safety Risk Assessment and Alternative Compliance Strategy to satisfy these new Subchapter W lifesaving rules.

But, on September 11, 2001, Washington State Ferries, along with the rest of the nation, was compelled to re-examine the security of its operation.

During 2001-2002, WSF tightened overall security and partnered with federal regulators and law enforcement agencies to coordinate threat and emergency response efforts.

The WSF Security Committee was formed to facilitate appropriate implementation of security measures, accurate/timely communications and reaction to pertinent emerging security issues. In July 2002, WSF's CEO, USCG Captain of the Port, and the Chief of the Washington State Patrol (WSP), signed the charter governing this joint security committee.

The Committee's work has spanned two years thus far and continues on a monthly basis, working to meet new security regulations and both federal and local legislation. An in-depth review of security issues the ferry system faced over the last year is covered in Chapter Five, Security & Safety, page 24.

Customer Service

Customer Satisfaction and Amenities Survey

In 2002, Washington State Ferries conducted the first-ever system-wide customer survey to measure customer satisfaction with Washington State Ferries' service and to measure interest in potential new services and amenities aboard the ferries and at the terminals.

WSF received nearly 7,000 responses from ferry passengers between August 19 and September 20, 2002. Customers expressed a broad level of interest in potential new services, especially on board the vessels.

Three quarters of all Washington State Ferries passengers describe themselves as "extremely satisfied" or "somewhat satisfied," overall, with Washington State Ferries. The satisfaction rating is slightly higher among full-fare passengers (79%) than among commuters (71%).

The most popular new service ideas, for both ferries and the terminals, are food courts, beverages such as espresso, wine and beer, newsstands and bookstores.

Washington State Ferries intends to use the information to improve its level of service wherever possible, and to assist with decisions about new services and amenities.

Accepting Credit Cards at Terminals

In a major improvement to customer service, WSF began accepting credit cards at all terminals where payment is rendered.

WSF Information Technology staff began implementing point-of-sale credit card acceptance at select terminals in October 2001. All terminals, with the exception of the San Juan Island terminals, were online by January 2002.

In July 2002, credit card sales represented 19% of all transactions and $2.4 million on 67,000 transactions.

Monthly Passes Available at Retail Locations

Washington State Ferries first offered the "ferry-only monthly pass" in 2001.

Early in 2002, WSF began selling the ferry-only pass at convenient retail locations near ferry terminals. This allowed for flexibility in payment type, and gave customers the ability to purchase the pass at a storefront.

Smart Cards

On April 29, 2003 seven public transportation agencies, including Community Transit, Everett Transit, King County Metro Transit, Kitsap Transit, Pierce Transit, Sound Transit, and Washington State Ferries, authorized a new fare system that will allow passengers to move more easily between buses, trains, and ferries across four counties in Puget Sound.

The new fare collection system uses "smart-card technology," featuring a fare card containing a microchip. The chip can be loaded with a cash value or any amount equal to a pass sold by the partner agencies. The cards are read at the farebox, terminal, or station with the fare automatically deducted.

Public introduction of the Smart Card is scheduled for 2006. The card will streamline the purchasing process for commuters, and eliminate more than 300 types of tickets, passes and tokens currently used by the transit systems.

Vanpool/Carpool

Washington State Ferries promotes Carpooling and Vanpooling as an alternative to single-occupancy vehicle travel. Ridesharing reduces traffic congestion and air pollution in our community. Through marketing and promotion efforts, participation in WSF's Carpool and Vanpool Program increased dramatically in Fiscal Year 2003. Through the combined effort of King County Metro, Kitsap Transit, and Washington State Ferries, Carpools on the ferries increased 34%; Vanpools on the ferries increased 19%; and VanShare groups (vans that drive to and/or from the ferry terminals, but do not board) increased 82%.

Lifesavings/rescues

Washington State Ferries gives Life Ring Awards to those employees involved in saving the life of a customer or fellow co-worker. WSF vessel employees receive training in first aid and rescues at sea, and are trained in the use of the vessel's on-board automatic external defibrillator (AED) for heart attack victims. Because of this training, WSF employees are able to assist during life or death situations by responding with immediate assistance and by properly communicating the emergency so that victims are able to receive additional assistance as quickly as possible.

In 2002, Life Ring Awards were given to crewmembers from the *MV Elwha* (March 12), *MV Walla Walla* (July 7), *MV Hyak* (July 20), *MV Yakima* (July 29), and *MV Chelan* (Dec. 2) for their lifesaving efforts.

In 2003, several WSF employees earned Life Ring Awards: Crewmembers on the *MV Evergreen State* (Jan. 26) for rescuing an overturned kayaker from rough waters, the *MV Elwha* (May 9) for aiding a choking victim, the *MV Chelan* (May 22) for saving a man who had jumped overboard, the *MV Tacoma* (Sept. 9) for saving a heart attack victim, Port Townsend/Keystone crew (April 7) for using CPR to resuscitate a customer, Southworth terminal employees (Oct. 6) for rescuing a seizure victim from a burning vehicle.

Environmental Stewardship

Eelgrass Mitigation at the Clinton Ferry Terminal

As part of a comprehensive terminal maintenance and preservation program, the Clinton Ferry Terminal was recently expanded to accommodate increasing service demands. The conventional approach to dock expansion would involve simply widening the dock to provide more vehicle holding area on the dock. However, the original design would have resulted in the loss of a substantial amount of eelgrass, which is an important habitat for juvenile salmon.

WSF decided to use this project as an opportunity to gain a comprehensive understanding of the impacts of ferries and ferry terminals on eelgrass. Researchers from the Battelle Marine Sciences Laboratory and the University of Washington, members of the Marine Resources Coordination Board, and employees from federal resource agencies worked directly with WSF Terminal Design engineers to develop a new dock design that would avoid and minimize the impact on eelgrass. This collaborative effort also identified experimental methods for eelgrass mitigation, such as the installation of glass blocks in the dock. As a result of this unique partnership, the final permitted design impacted only one third of the original estimate.

Testing Cleaner Fuels on the Ferries

The exhaust from diesel engines is a substantial source of air pollution in the Puget Sound Region. As such, the WSF Vessel Maintenance and Preservation Department, with technical and financial support from the Puget Sound Clean Air Agency and Region 10 of the U.S. Environmental Protection Agency, embarked on a study to evaluate the potential benefits and the likely costs associated with burning cleaner fuels in the WSF fleet. The goals of the study were to:

1. Develop an emission factor for successively cleaner grades of diesel fuel and one diesel fuel blend
2. Compare the economies of each fuel
3. Assess the compatibilities of each fuel with WSF existing equipment
4. Give WSF personnel experience handling each fuel

Using the *MV Rhododendron* as a test platform, WSF tested four different diesel fuels and fuel blends.

The data generated from this test indicates that teh ferry system can potentially achieve substantial reductions in emissions from the fleet by burning cleaner fuels.

The Diesel Fuel testing indicated:

- The quantity of particulate matter emitted from the stack of the *MV Rhododendron* was reduced by between 55 and 75% when burning low sulfur diesel, B20, and ultra low sulfur diesel fuel, respectively.

- The quantity of sulfur dioxide emitted from the stack was reduced between 85 and 92% when burning low sulfur diesel, B20 and ultra-low sulfur diesel, respectively.

- The quantity of nitrogen oxides, carbon monoxide, and non-methane, non-ethane hydrocarbon emissions were not significantly changed by sulfur content in the fuel.

WSF is currently working to compare these test results with results generated by other organizations, to determine how to apply the results of these tests to the diesel engines on other vessels in the fleet, and to evaluate the costs and benefits associated with moving toward burning cleaner fuels and exploring grant-funding opportunities.

Schel-chelb Bay Estuary Mitigation (Bainbridge Island)

WSF's Eagle Harbor Repair facility has been the site of shipbuilding activities that span nearly a century. Historically, shipbuilding activities contributed pollutants to the land, water, and sediments in the vicinity of their operations.

In the early 1990's the U.S. Environmental Protection Agency (EPA) declared WSF's Eagle Harbor Repair facility part of a superfund site - The Eagle Harbor/Wykoff site. Cleanup of this site was completed in the late 1990's and the Schel-chelb Estuary wetland construction/restoration project was completed to replace habitat lost due to site cleanup activities. The primary goal of the estuary construction/restoration plan was to restore the intertidal and estuarine habitats that historically existed at the Schel-chelb site.

The Schel-chelb Estuary Mitigation Project won an award at the Shared Strategy for Puget Sound Salmon Recovery Conference in Tacoma, Washington.

Removal of Creosote Treated Timbers From the Marine Environment

WSF's Terminal Engineering Department has made a commitment to design, construct and maintain terminals in an environmentally responsible manner, using the best available practices and material. As part of this commitment, the Department decided to incorporate creosote removal into all ongoing ferry terminal replacement and improvement projects. The creosote-treated wood is being replaced with pilings made from steel and concrete, and the removed creosote is disposed of in a way that ensures it does not get re-used in the aquatic environment.

Creosote is a complex mixture of many chemicals and has been found to be potentially toxic to fish, other marine organisms and humans. Approximately 300 chemicals have been identified in coal-tar creosote, and there may be 10,000 other chemicals present in the mixture. The major chemicals that can cause harmful health effects are polycyclic aromatic hydrocarbons (PAHs), phenols and cresols.

Since the year 2000, WSF's Terminal Engineering department has removed 2.5 million board feet of creosote-treated timber and piling from Puget Sound. (A board foot is one inch thick by one foot wide by one foot long.) WSF is committed to continue to remove creosote-treated lumber and timber during major maintenance activities and construction projects at all of our terminals over the next ten years.

III] Operational Overview

WSF's ridership consists of three categories: vehicles and their drivers, passengers in vehicles, and passengers that walk on the vessels. Total system wide ferry ridership has been declining since 1999 due to a combination of factors including a downturn in the regional economy, minor service reductions and fare increases.

ridership consists of three categories

Between July 1, 2001 and June 30, 2002, 25.6 million people traveled on Washington State Ferries compared to 26.6 million the previous year, a 4.2 percent decrease. WSF saw a further decline in fiscal year 2003 (July 1, 2002 through June 30, 2003), when WSF carried 24.5 million customers, a decrease of 3.7 percent from the year before.

System Wide Ridership Trends

1999 7,627,000 walk-on passengers
7,491,000 vehicle passengers
11,378,000 vehicles/drivers

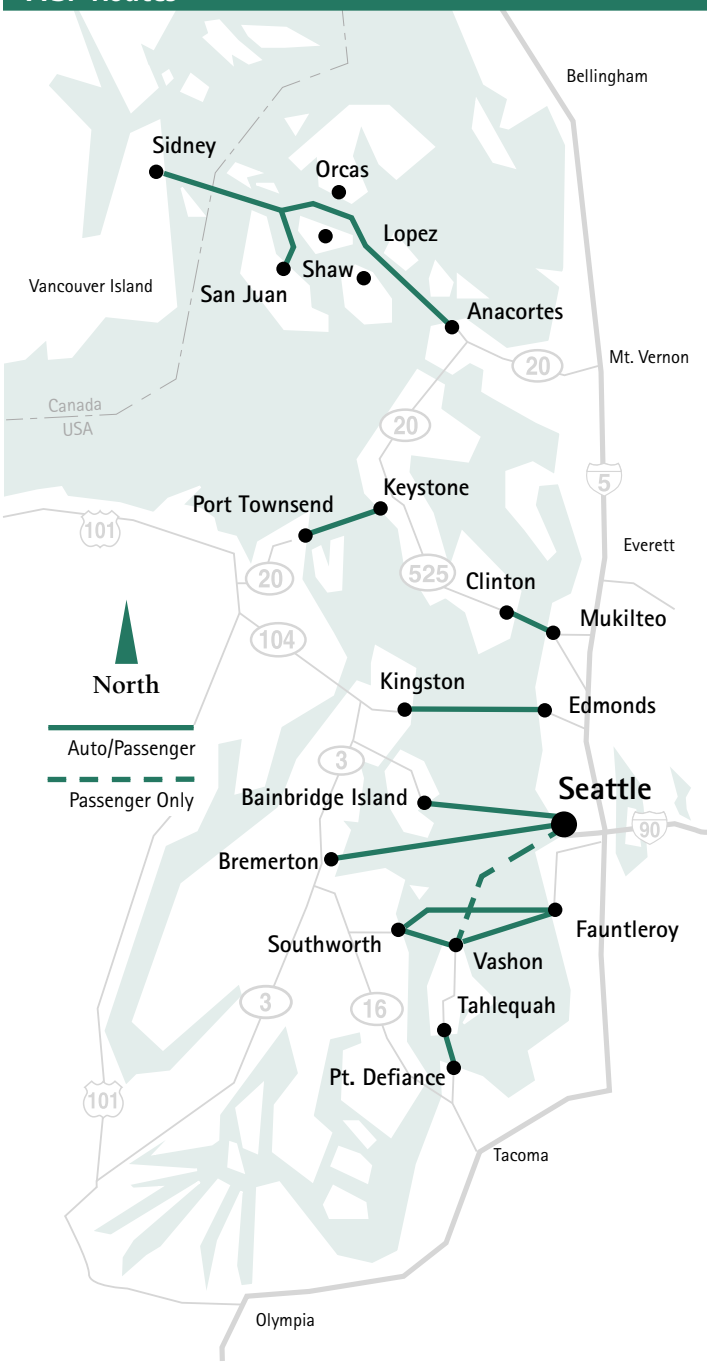
2000 7,626,000 walk-on passengers
7,491,000 vehicle passengers
11,379,000 vehicles/drivers

2001 7,204,000 walk-on passengers
7,936,000 vehicle passengers
11,463,000 vehicles/drivers

2002 7,177,000 walk-on passengers
7,313,000 vehicle passengers
11,141,000 vehicles/drivers

2003 6,776,000 walk-on passengers
6,948,000 vehicle passengers
10,819,864 vehicles/drivers

WSF Routes



Ridership Statistics by Route

FY 2002	Vehicles/Drivers	Vehicle Passengers	Walk-ons
Seattle/Bainbridge	2,204,000	1,622,000	2,982,000
Edmonds/Kingston	2,359,000	1,570,000	659,000
Mukilteo/Clinton	2,259,000	1,396,000	538,000
Fauntleroy/Vashon/Southworth	1,866,000	987,000	409,000
Seattle/Bremerton	724,000	460,000	1,077,000
Anacortes/SanJuans	867,000	641,000	313,000
Seattle/Bremerton PO	N/A	N/A	730,000
Keystone/Port Townsend	367,000	326,000	106,000
Tahlequah/Point Defiance	440,000	223,000	94,000
Seattle/Vashon PO	N/A	N/A	243,000
Anacortes/Sidney, BC	45,000	75,000	20,000
All Routes	11,141,000	7,313,000	7,176,000

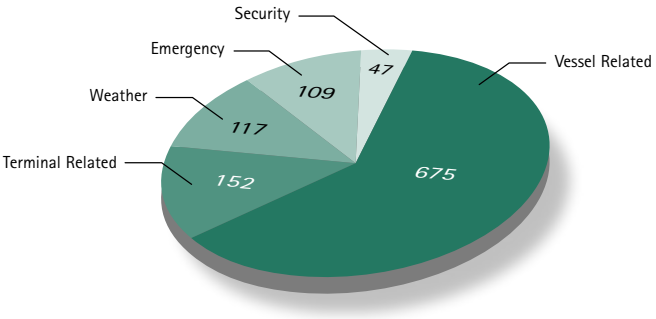
FY 2003	Vehicles/Drivers	Vehicle Passengers	Walk-ons
Seattle/Bainbridge	2,145,000	1,574,000	2,831,000
Edmonds/Kingston	2,312,000	1,495,000	623,000
Mukilteo/Clinton	2,197,000	1,322,000	510,000
Fauntleroy/Vashon/Southworth	1,755,000	860,000	433,000
Seattle/Bremerton	688,000	442,000	988,000
Anacortes/San Juans	870,000	634,000	312,000
Seattle/Bremerton PO	N/A	N/A	637,000
Keystone/Port Townsend	371,000	319,000	101,000
Tahlequah/Point Defiance	431,000	220,000	98,000
Seattle/Vashon PO	N/A	N/A	221,000
Anacortes/Sidney, BC	42,000	68,000	16,000
All Routes	10,820,000	6,948,000	6,776,000

Trip Completion

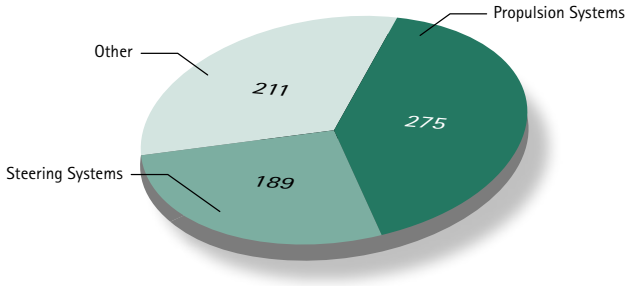
2001–2002

Scheduled Trips	178,737
Cancelled Trips	1597
Replaced Trips	552
Total Completed Trips	**177,692**

2001–2002 Most Common Trip Cancellation Causes



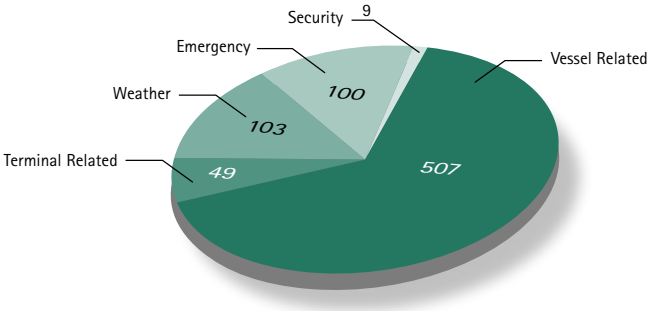
Vessel-Related Missed Trips



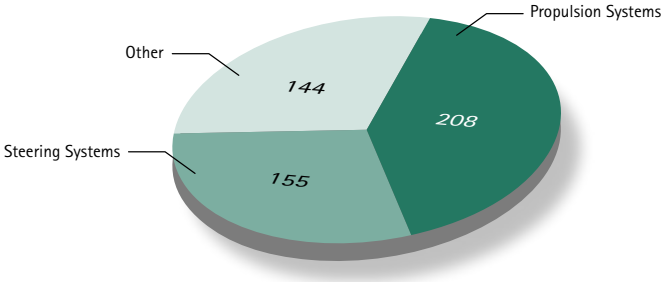
2002–2003

Scheduled Trips	175,652
Cancelled Trips	1,033
Replaced Trips	352
Total Completed Trips	174,971

2002–2003 Most Common Trip Cancellation Causes



Vessel-Related Missed Trips



IV] Strategic Plan

Financially speaking, there has been little good news in recent years for Washington State Ferries. First impacted in 1999 when the voters and the legislature approved Initiative 695, the financial challenges continue.

provides a sustainable future

Financial Challenges

- 1999 Voters Approve Initiative 695
- 2000 The Legislature Adopts the Provisions of Initiative 695. The cost to the ferry system is approximately 25% of the Operating budget ($31 million) and virtually all of the Capital budget ($120 million).
- 2000 The Legislature approves transfers from the Motor Vehicle Account for capital funding. Service changes coupled with a series of fare increases and transfers from the Motor Vehicle Account stabilizes operating budget.
- 2001 Ferry System proposes a plan to produce new revenue with initiatives in advertising and marketing.
- 2002 Voters reject Referendum 51 that would have provided critical funding for capital projects including four new ferries, preservation and maintenance and new ferry terminals.
- 2003 Legislature approves the "Nickel Package," a $4.2 billion package of transportation improvements across the state funded primarily from a 5¢ increase to the gas tax and other license fees. For the ferry system, $300 million was authorized for vessel and terminal construction activities around the Sound.

Strategic Plan

In the fall of 2002, Washington State Ferries unveiled a new Strategic Plan comprised of four goals and the Business and Capital Funding Plan to achieve them. Acknowledging that any new resources would be limited, the Strategic Plan provides a sustainable future for the state ferry system through a focus on refining our business practices, broadening our revenue base and investing in our capital infrastructure.

Washington State Ferries Strategic Goals

1. Continually Improve and Refine Our Business Processes
2. Broaden Our Revenue Base and Reduce Costs
3. Promote and Assist in the Planning of Regional Transportation Centers
4. Re-define Who We Are

WSF 5+5+5 Business Plan (Increasing Operating Funds)

In order to achieve the Strategic Goals, WSF developed the 5+5+5 Business Plan. The 5+5+5 Business Plan means that the ferry system is responsible for reducing costs by 5%, capping ferry fare increases at 5%, and generating 5% in new revenues with a comprehensive retail, marketing, and advertising program. Under this new plan, the ferry system will be able to recover 90% of its operating costs by 2008 with revenues generated by the ferry system (currently the ferry system cover approximately 73%).

Capital Funding Plan (Increasing Capital Funds)

The Capital Funding Plan builds on the 5+5+5 Business Plan to address the ferry system's urgent capital needs. The plan provides funding for much-needed major preservation projects and new vessel construction. With aging terminals and four vessels in the fleet that were built when Calvin Coolidge was president, WSF needed to find a way to fund infrastructure improvements without new state revenue.

Without money for new vessels, WSF is faced with the potential of pouring millions of dollars into four of the oldest vessels in the fleet just to keep the current level of service for a few years. If these aging vessels are not replaced and our terminals not maintained properly, we will no longer have a viable ferry system.

The Capital Funding Plan is based on a straightforward formula:

Service reductions + vessel retirements = less preservation work
Less preservation work = funding for critical capital investments

The service reductions were selected to affect the fewest number of riders, leave no one without a transportation alternative and ultimately ensure a viable ferry system. At a time when public agencies must do more with less, Washington State Ferries had to focus on investing in its own capital needs to ensure a sustainable ferry system for years to come.

Phase One of the Capital Funding Plan (2003–2005)

Implementation of the Capital Funding Plan began in Fall 2003. The first step of the plan, discontinuation of passenger-only ferry service from Seattle to Bremerton and Vashon Island, was slated for June 15, 2003. However, the state legislature granted a three-month grace period for the Seattle-Bremerton service; and funded a two-year extension in service to the Vashon-Seattle route. The Legislature will decide the long-term future of WSF's role in passenger only service during the 2005 legislative session.

Phase Two of the Capital Funding Plan (2005–2013)

Phase Two includes building four new boats and upgrading an existing terminal. These capital projects are critical to the ferry system infrastructure. The money the ferry system saves from implementation of Phase One will provide funds for the work scheduled through 2013. Phase Two of the plan spans the period from 2005 – 2013.

During this phase, WSF expects to construct and take delivery of the new vessels, retire four old Steel Electric auto ferries, and begin service at a new terminal in Keystone.

During this eight-year timeframe, WSF plans to implement cost-saving service changes, including discontinuing service to Sidney, B.C. for 12 weeks during the winter season when service demands are low, and eliminating a third vessel during weekend service on the Fauntleroy-Vashon-Southworth route. The possibility of auto ferry service between Vashon and Southworth into Pier 52 (downtown Seattle) will be explored. WSF will also consider a new focused approach to the maintenance facility located at Eagle Harbor, by studying alternative sites for the facility as suggested in a recent legislative oversight committee report.

On the Brink...

New Concessions Model Means More Options

In Fall of 2003, Washington State Ferries issued a Request for Proposals (RFP) for concession services. A key component of the RFP is a totally new approach to concession services.

The new concessions model provides for greater flexibility in the range and type of services for passengers and it allows WSF to be more responsive to change so that the organization can meet customer interests and needs.

In 2004, WSF will begin the review process of bids submitted by interested vendors for onboard and shoreside food, beverage and retail services. Potential vendors will then conduct negotiation discussions with the Inlandboatman's Union (IBU), the union that represents ferry galley workers.

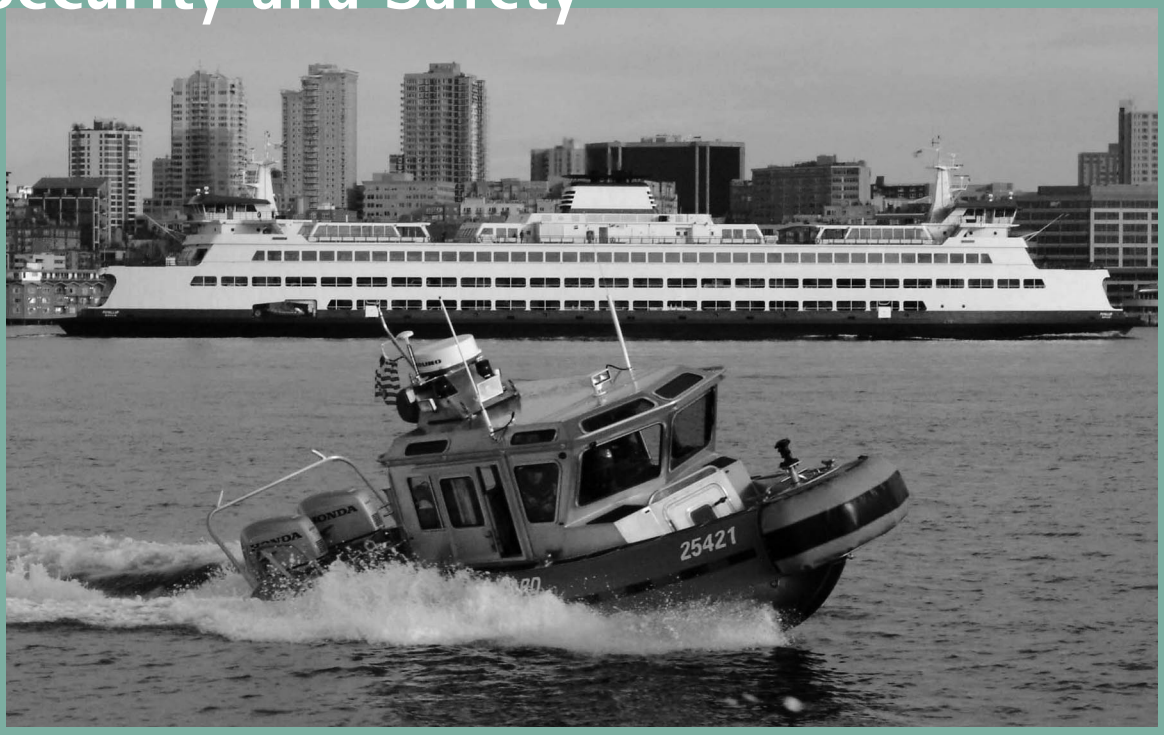
New Seattle Terminal

Colman Dock (Pier 52) is located along the Seattle waterfront and is the heart of the ferry system. It is an inter-modal transportation terminal accommodating pedestrians, autos, trucks, buses, bicycles, and emergency vehicles. Of the approximately 25 million riders who use the ferries annually, 36% or 9 million of those riders come through Pier 52.

Pier 52 is an extension of the highway system allowing Interstate 5 and Interstate 90 to connect across Puget Sound to Bainbridge and Vashon Islands, and Kitsap Peninsula to the west. On the busiest commuter route, Bainbridge to Seattle, WSF carries approximately 18,000 people in an average day, and approximately 700 vehicles per hour during peak travel hours.

Washington State Ferries plans to remodel Colman Dock to include space for vendors and retailers inside the terminal. Construction of the new terminal at Pier 52 in Seattle is slated to begin in 2004.

V] Security and Safety



Following the tragic events of September 11, 2001, WSF tightened overall security and partnered with federal regulators and law enforcement agencies to coordinate threat mitigation and emergency response efforts.

appropriate implementation of security

Security

Background

September 11, 2001

The WSF Security Committee was formed to facilitate appropriate implementation of security measures, accurate/timely communications and reaction to pertinent emerging security issues. In July 2002, WSF's CEO, USCG Captain of the Port, and the Chief of the Washington State Patrol (WSP), signed the charter governing this joint security committee. Formal meetings have been held at least on a monthly basis to develop procedures and contingency plans aimed at ensuring the secure operation of Washington State Ferries during regular and heightened states of security threats.

The Committee agreed to the implementation of a number of new security measures during 2001-2002, all aimed at enhancing security while maintaining system viability.

During the 2001-2002 legislative sessions, the Washington State legislature took steps to fund temporary night watch personnel and a new security coordinator position for WSF. The WSP also received a $1.8 million supplemental budget from the state legislature to enhance security measures dedicated to ferry operations.

2002

First Introduction to Passenger Security Standards from U.S. Coast Guard

In September 2002, the Coast Guard published the *"Guidance on Security Procedures for Ferries Certificated to Carry More than 500 Passengers and the Terminals They Service."* These guidelines included recommended security measures aboard ferries and at terminals.

Ferry officials, along with Congressional and state legislative representatives, met with Coast Guard officials to examine the intent of these guidelines as well as highlight the possible financial, operational, legal and consumer implications of implementation.

U.S. Legislation

In November 2002, President Bush signed into law the Maritime Transportation Security Act (MTSA) of 2002. The Act contained broad directions to the USCG concerning the establishment of security regulations in the maritime transportation arena. The legislation mandated a very aggressive timeline for regulatory implementation.

International Regulations

In December 2002, the International Maritime Organization (IMO) (of which the United States is a signatory nation) adopted the International Ship and Port Facility Security (ISPS) Code, aimed at enhancing maritime security across the international spectrum. These standards mandate that security measures be put into place by July 1, 2004 and are applicable to ferries on the WSF international route to Sidney, B.C.

2003

In late December 2002, the U.S. Coast Guard issued a notice of its intent to publish new security rules mandated by the MTSA, soliciting industry feedback, and announcing a schedule of public meetings.

In February 2003, the U.S. Coast Guard held a public meeting in Seattle to discuss new requirements for security assessments, plans, and specific measures as they apply to ports, vessels, and waterfront facilities. Discussions focused on how to align domestic maritime requirements mandated by the Maritime Transportation Security Act (MTSA) with the International Ship and Port Facility Security (ISPS) code.

WSF provided detailed comments regarding cost, resources, labor, operational, and legal implications to the Coast Guard docket, which was open through the end of February 2003.

In March 2003, the Federal Transit Administration (FTA) sponsored a safety and security/vulnerability assessment of Washington State Ferries, as one of the 100 key transit systems in the nation, identifying security strengths and weaknesses.

MTSA Interim Final Rules

On July 1, 2003 the U.S. Coast Guard published the MTSA Interim Final Rules.

The comprehensive maritime industry rules required vessel and facility operators to complete security assessments and develop security plans by Dec. 31, 2003, with full implementation of the security measures and procedures contained in the plan by June 30, 2004.

The rules are based on the premise that increased threat equals increased security. Specifically, the rules establish three levels of security, allowing the industry to increase and decrease measures based on threat conditions.

Generally, the rules require the implementation of appropriate security measures. Accounting for varying security levels and other factors, the rules require implementation of measures such as passenger, vehicle, and baggage screening procedures; security patrols; establishing restricted areas; personnel identification procedures; access control measures; installation of surveillance equipment; and designation of security personnel. The rules require designation of, and requirements for, security officers for vessels and/or facilities, and training for security personnel, as well as training for all personnel so that they are ready and able to implement the security plan components.

The rules also provide for Alternative Security Programs, which permit flexibility and encourage innovation by allowing industry to submit, for Coast Guard approval, alternative security programs that provide a level of security equal to that required in the regulations.

July 1, 2003	Publish Interim Final MTSA Security Rules
Oct. 22, 2003	Publish MTSA Final Rules
Dec. 31, 2003	Security Plan and Assessment Submission Deadlines
June 30, 2004	Full Security Plan implementation

Security Grants

As the need for security investments became clearer, more federal grants have been were made available to operators/organizations for use in their security programs.

Washington State Ferries applied for and was awarded a number of grants to help fund its security needs; such as capital costs associated with surveillance and other security equipment, as well as emergency drills and training.

2002

- $50,000 from Federal Transit Administration to fund Emergency Preparedness Drills - one multi-agency terrorist drill and one fire drill aboard our vessels.

- Federal Port Security Grant Program – Round 1 - $110,000 from USDOT Maritime Administration to develop a miti gation and response strategy for a chemical, biological or radiological release aboard a ferry.

2003

- Federal Port Security Grant – Round 2 – Total award of $9.4 million dollars. The grant, although submitted prior to publication of regulations, will support some of the ele ments of WSF's final security plan.

$9.4 Million Divided

$2.5 million from the Office for Domestic Preparedness for terminal monitoring, physical enhancements and access control.

$6.9 million from the Transportation Security Administration for vessel physical security and access control.

The Plan Forward...

In December 2003 Washington State Ferries submitted for approval a comprehensive security plan aimed at addressing applicable provisions of the final rules.

Washington State Ferries' challenge is balancing its number one priority of safe and secure transport of our ferry riders and employees, and commitment to security, against its goal of being an efficient mode of mass transit.

Safety

Background

WSF Addresses New Lifesaving Rules

Security has received considerable attention at Washington State Ferries since the terrorist attacks of September 11, 2001. However, prior to the events of 9/11, WSF had embarked on a comprehensive set of safety enhancements in response to new Coast Guard requirements regarding lifesaving measures.

Title 46, Code of Federal Regulations, Subchapter W stipulates the required lifesaving equipment, arrangements, plans, and training for all vessels, including all WSF vehicle ferries. Subchapter W became effective in 1996 and incorporated a phased-in compliance timeline, with completion of select items by October 1, 1999, and all elements by October 1, 2003.

WSF conducted, and submitted to the Coast Guard, a comprehensive Safety Risk Assessment. In turn, WSF formulated and submitted an Alternative Compliance Strategy to satisfy these new Subchapter W lifesaving rules. In early 2002, WSF gained full Coast Guard approval of its final Subchapter W Safety Risk Assessment and Alternative Compliance Plan.

The compliance plan incorporated a holistic approach to safe ferry operations, identifying those personnel/training elements, organizational components, procedural modifications and/or additions, and equipment upgrades that successfully dovetail together to satisfy the regulatory intent. Collectively, these elements address both the prevention and response aspects of ferry operations, with the goal of providing safety dividends day in and day out, as well as in an emergency.

Key Elements of the Alternative Compliance Plan

Personnel Training

Training of personnel is considered critical to the success of this important safety program. WSF is in full compliance with the minimum personnel training and drilling standards spelled out in the regulations. Furthermore, WSF incorporated training beyond these minimums, which were designed to ensure employees are taught to be proficient in the use of the new/modified equipment.

All Subchapter W specific personnel training elements have been fully completed, with all existing personnel receiving the requisite training, and with set procedures in place for all new employees to receive the appropriate training.

Organization

The creation and maintenance of the organizational elements listed below address in large part the safety management aspects of an effective safety program and are considered essential pieces of WSF's best business practices and a vital part of the Subchapter W compliance strategy.

- Adoption of Safety Management System (SMS) fleet wide (international and domestic routes) to provide a means to enhance the safety culture throughout the organization and systematize the process for continuous improvement;
- A centralized operations center, including automated dispatch support system, to ensure trained and qualified crewmembers;
- A WSF emergency operations center (EOC), to ensure a means to respond in a responsible manner in the event of an incident;
- A safety systems manager/DP position and a Safety Coordination Team that will utilize a matrix management concept to oversee WSF's safety systems.

All organizational elements of the plan have been fully implemented. The vessel engine department automated dispatch process (similar to that process already in use by the vessels Deck Department) is complete and is undergoing final beta testing.

Procedures

The system-wide application of the Safety Management System (SMS), plus publication of Subchapter W related emergency response SMS procedures and the Emergency Operations Center (EOC) Manual were important components of WSF's compliance strategy. The procedural elements incorporate the following topics:

- Modified Muster Lists
- Marine Evacuation Slide Usage
- Operational readiness, maintenance, and inspection
- Shipboard Safety Management and Contingency Plan
- Damage stability capabilities
- Towing procedures

All Subchapter W related emergency response SMS procedures, with the exception of the Emergency Operations Center (EOC) procedures and those for emergency towing, are complete and published. The EOC procedures are currently in final form, have been published, and are being distributed with an effective date of October 15, 2003. The towing procedures are being drafted and will be published to coincide with the equipment deployment discussed below.

Equipment

The main equipment additions/modifications integral to the Subchapter W compliance plan include:

- Four 150-person marine evacuation slides (MES) on each auto ferry
- New rescue boats on all operating vehicle ferries
- Additional 150-person inflatable buoyant apparatus (IBA's) on the Jumbo Mark II vessels (the vessels with the highest passenger capacity)
- Towing equipment, towing bridle for each car/passenger ferry

This equipment forms the basic physical elements of the Subchapter W compliance strategy and was necessarily and appropriately coupled with attendant procedures and training. The fleet wide cornerstones of equipment - MES and rescue boat installations - have been completed on all operating vessels. The IBA installations on the Jumbo Mark II vessels are also complete. All pieces of the towing equipment have been purchased, with all pieces now in WSF possession. Final assembly and full deployment is scheduled to be complete by the end of 2003.
In summary, WSF continues to maintain a commitment to the principles of safety that formed the basis for the Subchapter W compliance plan. This expansive effort is clearly representative of the WSF commitment to being a national leader in the consistently safe and secure transport of passengers. The Coast Guard praised WSF for its comprehensive approach to safe operations, indicating that collectively the elements of the WSF compliance plan met or exceeded the regulatory intent.

VI] Capital/Operating Budgets

WSF's Capital and Operating programs are financed from different sources. The Capital program is financed primarily through state fuel taxes. The Operating program is funded primarily through user fees.

four categories of expenditure

Capital Program

The Legislature accesses WSF's Capital Program to make investments in the Ferry System's infrastructure. During the 2001-2003 Biennium, ferry capital investments were financed through the Motor Vehicle Fund, the Puget Sound Capital Construction Account and the Passenger Ferry Account.

During the 2001-2003 Biennium, State Fuel Taxes provided the largest revenue source for Ferry System investments. This source accounted for $135.1 million or 62.8% of capital sources of funds. State Fuel Tax distributions to the Motor Vehicle Funds accounted for $100.4 million or 74.3% of fuel taxes supporting ferry capital investments.

State Fuel Tax distributions to the Puget Sound Capital Construction Account accounted for $34.7 million or 25.7% of fuel taxes supporting investments. In contrast to the 1999-2001 Biennium, Motor Vehicle Excise Taxes did not support ferry investments, as this source of revenue was abolished by Initiative 695. Bond sales accounted for $50 million or 23.2% of capital sources of funds. In contrast to preceding biennia, the bonds sold in the 2001-2003 Biennium were authorized by Referendum 49. They are not ferry bonds. As a result ferry capital sources of funds are not responsible for their debt service.

Federal grants accounted for $24.1 million or 11.2% of capital revenues. Funds carried forward from the prior biennium into the 2001-2003 Biennium accounted for 2.6% of capital sources of funds. Miscellaneous revenues, local funds and transfers accounted for $0.5 million or 0.2% of capital sources of funds. Taken together, all of these sources of funds amounted to $215.2 million.

Capital Funds Spent on Key Activities

Spending for Vessel Construction

Total amounted to $84.1 million or 39.8% of total expenditures. Almost two-thirds of Vessel Construction spending went to projects that had biennial expenditures greater than $5 million. These investments involved eight of WSF's 28 vessels. They included the *MV Walla Walla* ($9.3 million), the *MV Tillikum* ($7.9 million), the *MV Cathlamet* ($7.9 million), the *MV Spokane* ($6.7 million), the *MV Sealth* ($6.5 million), the *MV Hyak* ($5.9 million), the *MV Klahowya* ($5.9 million), and the *MV Issaquah* ($5.3 million).

Spending for Terminal Construction

Total amounted to $68.2 million or 32.3%. Over 50% of Terminal Construction spending went to projects that had biennial expenditures greater than $5 million. These projects involved four of WSF's 20 major shoreside facilities. They included the Clinton Ferry Terminal ($15 million), the Anacortes Ferry Terminal ($7.8 million), the Southworth Ferry Terminal ($7.5 million) and the Fauntleroy Ferry Terminal ($5.9 million).

Spending for Ferry Debt Service and WSDOT/Other Agency support

Total amounted to $52.1 million or 24.7%

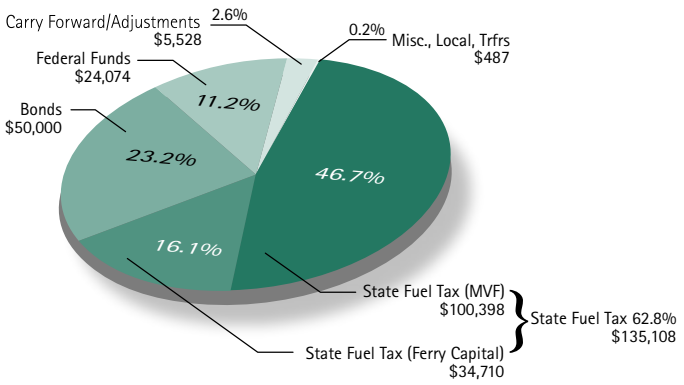
Spending for Emergency Repairs of Terminals and Vessels

Total amounted to $6.7 million or 3.2%

Taken together, these biennial expenditures totaled $211.1 million. $4.1 million was carried forward to support capital investments in the 2003-2005 Biennium.

WSF's Capital Program Revenue

IN THOUSANDS OF DOLLARS



Capital Program

	1999/01 Biennium (1000s)	2001/03 Biennium (1000s)
Revenue		
State Fuel Tax Distribution to the Motor Vehicle Fund*	3,339	100,398
State Fuel Tax Distribution For Ferry Capital	34,151	34,710
State Motor Vehicle Excise Tax Distribution For Ferry Capital	29,172	(14)
Bond Proceeds**	27,183	50,000
Federal Funds	40,472	24,074
Private/Local Funds	0	110
Transfers	79,756	(77)
Miscellaneous Revenues***	1,056	454
Capital Program Revenue	$215,129	$209,655
Previous Biennium Cash Carryforward	1,744	5,527
Fund Balance Adjustments****	3,042	1
Total Biennium Capital Funds Available	$219,915	$215,184
Capital Program Expenditures***		
Emergency Repair	6,955	6,694
Terminals	48,045	68,198
Vessels	104,192	84,101
Ferry Debt Service Withholding and WSDOT/Treasurer Support Programs	55,196	52,094
Total Biennium Capital Expenditures	$214,387	$211,087
Cash Carryforward	$5,527	$4,097

* The 1999-01 Operations Report did not show State Fuel Tax Distributions to the Motor Vehicle Fund used to support ferry debt service.
** 2001-2003 Biennium bond proceeds are derived from the sale of Referendum 49 bonds not ferry bonds.
**** The 1999-2001 Biennium fund balance adjustment was not reported in the 1999-2001 Operations Report.
***** The Motor Vehicle Fund supported emergency repairs, terminal construction, vessel construction in the amount of $159,192,000 in the 2001-2003 Biennium; ferry debt service withholding in the amounts of $3,338,500 in the 1999-2001 Biennium and $12,618,000 in the 2001-2003 Biennium, and WSDOT/other agency support in the amount of $2,971,000 (estimated) in the 2001-2003 Biennium.

Executive and Administrative Support

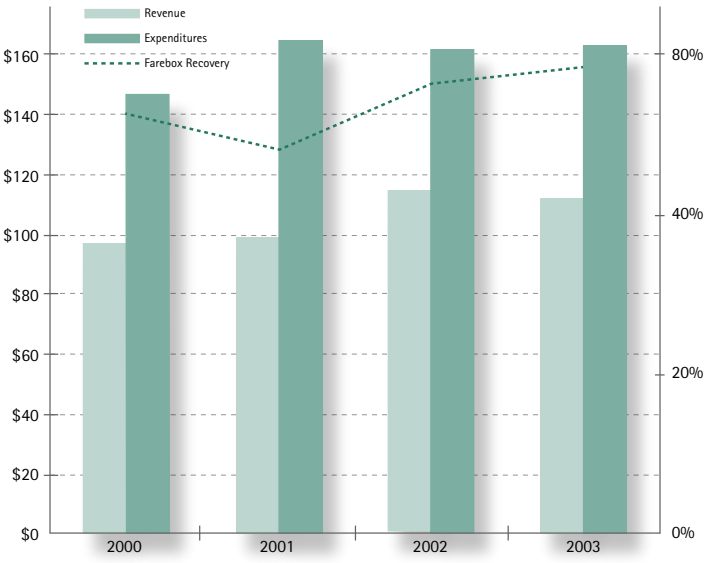
(Total Amounted to $40.8 million)
This activity includes executive and administrative support such as program oversight, accounting, human resources, contract administration, public relations, and audit functions. Also included are rents, leases, insurance and other costs of business.

Other State Support

(Total Amounted to $16.3 million)
Includes charges from other state agencies in support of WSF, including charges from the Attorney General, self insurance premiums, information technology costs and other support activities.

Following the passage of Initiative 695, the Governor's Blue Ribbon Panel on Transportation and the legislatively created Joint Task Force on Ferries directed WSF to take actions to increase farebox recovery to 80%. Acting on the recommendations, WSF embarked on a series of tariff increases in the spring of 2001. WSF's Strategic Plan, however, concentrates on removing the burden of these increasing fare increases, by capping them at just 5% annually, and plans to increase revenue though alternative sources, such as concessions and amenities.

Expenses and Farebox Recovery for 2000 – 2003



Operating Program

WSF's operating program is funded primarily through user fees. Tariffs, concession fees, and other revenues generated from customers covered 73% of operating and maintenance costs for fiscal year 2003.

Operating Funds Spent on Key Activities

Daily Operations of Terminals and Vessels

Total Amounted to $226.5 million. This activity directly supports the legislatively approved service schedule and service hours. It includes labor, fuel and materials for deck and engine operations of the fleet. Daily operations also include revenue collection costs, traffic control costs, operations training, and vessel and terminal operations management and support.

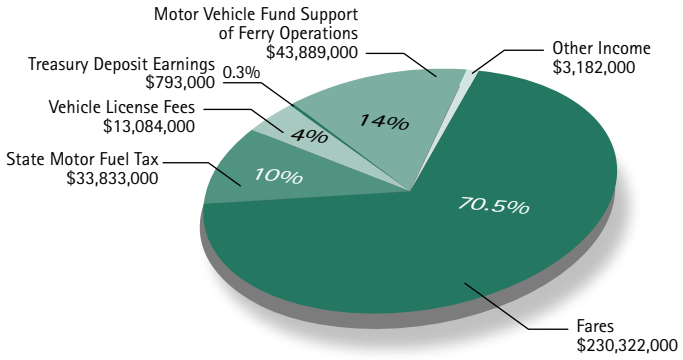
Maintenance of Terminals and Vessels

Total Amounted to $44 million. Maintenance includes labor, materials, repair contracts and miscellaneous costs associated with terminal and vessel maintenance. Vessel maintenance is accomplished by WSF at its dedicated maintenance facility at Eagle Harbor. Larger vessel maintenance contracts and drydockings are performed at commercial shipyards around Puget Sound. Terminal maintenance includes routine asset maintenance and inspection performed by Eagle Harbor staff and contracted maintenance for major maintenance needs.

Breakdown of Operating Program

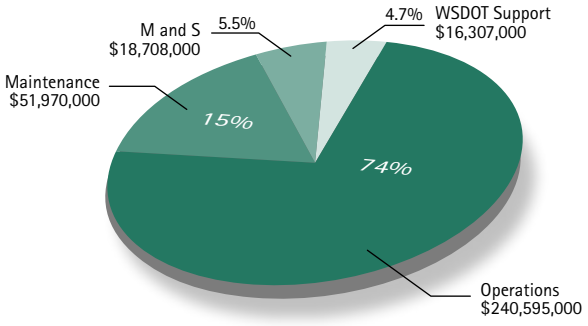
Revenue 2001-2003

Fares	230,322,000
State Motor Fuel Tax	33,833,000
Vehicle License Fees	13,084,000
Treasury Deposit Earnings	793,000
Motor Vehicle Fund Support of Ferry Operations	43,889,000
Other Income	3,182,000
Total	**325,103,000**



Expenses 2001-2003

Operations	240,595,000
Maintenance	51,970,000
M and S	18,708,000
WSDOT Support	16,307,000
Total	**327,580,000**



VII] Maintaining and Preserving Vessels

WSF's vessel and terminals are the foundation of the ferry system. Securing funding for important maintenance, structural improvements and preservation will ensure the lifespan of these assets. Capital investments ensure that the ferry system remains viable for years to come. WSF makes capital investments in its fleet to protect existing vessels through scheduled maintenance, emergency repairs, preservation activities, and improvement projects. Vessel maintenance and preservation are critical to the ferry system's infrastructure.

detailed and complex maintenance

The ferry system operates its ten routes using 24 vessels. WSF owns 28 vessels; four of which are on a deactivated status. Deactivated vessels are boats that are used only in an extreme emergency and therefore have less maintenance and preservation money dedicated to them.

Maintenance

Vessel maintenance is a combined effort of the vessel's engine crew and machinists at the Eagle Harbor maintenance facility as well as larger maintenance contracts performed at local shipyards.. Engine crews monitor the ferry's propulsion system and auxiliary machinery, performing planned maintenance procedures and maintaining virtually every piece of equipment onboard the ferry. Many of these tasks are performed while the vessel is underway. Crews use nighttime hours to perform heavier repair and maintenance functions.

Vessel maintenance is grouped into two categories: basic and intermediate. Basic vessel maintenance is also referred to as shipboard preventative maintenance, and includes activities that can be accomplished by the ship's operating crew while the vessel is in service or moored for the night. Examples of this maintenance include oil changes, tune-ups, and systems adjustments.

Intermediate vessel maintenance includes activities that require removing the vessel from service. Most intermediate maintenance activities are accomplished at the Eagle Harbor Maintenance Facility and by specialty vendors. Often this work requires a shore-based infrastructure that is not available aboard ship. Examples of this maintenance include rebuilding engines, hydraulic component overhauls and upholstery repair.

Washington State Ferries employs a detailed and complex maintenance schedule to address maintenance issues that can be anticipated and scheduled.

Washington State Ferries' begins scheduling routine maintenance and annual inspections two years in advance. Using a highly detailed and scheduled maintenance program allows the ferry system to meet Coast Guard regulations for required maintenance, and minimize the impact on our operations and ultimately our customers.

Once a vessel is scheduled to undergo maintenance, steps are taken to assure appropriate service remains on the route where the vessel is being pulled from. With a schedule set in advance, WSF is able to plan which vessels will need to be reassigned. Many times, several vessel changes will be necessary in order to meet the demand on all routes.

Vessel maintenance for 2001-2003 totaled $19.0 million in FY 2002 and $14.8 million in FY 2003.

Improvements to Maintenance Program

The ferry system's Maintenance Productivity Enhancement Tool (MPET) system helps WSF track vessel maintenance by transferring data from ship to shore via a wireless computer system.

Over the 2001-2003 biennium, the ferry system worked to complete installation of the system on every active vessel. This system will make the maintenance department more consistent, more efficient, and will allow WSF to reduce paperwork and inventory.

The tool provides WSF employees the ability to review planned maintenance schedules, the maintenance history of each piece of machinery, preventative maintenance processes, and total costs of maintenance including labor, travel time, and materials.

Emergency Expenditures

Washington State Ferries allots funds for emergency repair of its vessels. Emergency repair activities include unexpected damage to vessels, such as occurs when a ferry makes a hard landing at a dock. Emergency repairs differ from other capital investments because they are governed by statutes that streamline the contracting process. This allows WSF to expedite repairs and get the vessel back in service as soon as possible. In the 2001-2003 biennium WSF used $1.8 million in capital funds for emergency repairs to vessels. Once that money is spent, WSF draws from either the Operating budget for maintenance work, or regular capital funding.

Preservation

In general, auto ferries have a useful lifespan of about 60 years. Vessels require preservation investments throughout their lives but needs peak as they approach 30 and 60 years of operation. WSF has four vessels that are that are over 75 years old, and over half of its auto vessels were constructed prior to 1975.

Vessel preservation includes the activities that require the services and facilities of a commercial shipyard. Examples of this maintenance include dry dock inspections, exterior painting, structural repairs, and replacing complete systems, such as electrical or propulsion systems. Preservation such as this can give new life to an aging vessel that is still under its initial lifespan. Capital investments in preservation are essential to ensure that Washington State's ferry system is using equipment that is safe and reliable to transport its customers.

WSF uses the life cycle model preservation program. Vessel parts are classified into a category - either vital or other. Vital parts are those designated by the US Coast Guard as vital to the protection of people, the environment and the vessel. Other parts of the vessel may be important but not vital as defined by the US Coast Guard.

Each part has a life cycle, and each is tracked, and either replaced or preserved according to its lifecycle. By doing this, the ferry system can allot its resources in a way that makes sense for the entire system. In the absence of investments to protect these assets, the overall life cycle rating for the fleet declines.

Ferry Vessels

In 2001-2003, WSDOT spent $86 million to preserve the ferry system's vessels, including emergency repairs.

Investments focused on ferries in the Issaquah Class ($32 million), Jumbo Class ($16 million), Evergreen State Class ($14 million) and Super Class ($10 million)

Washington State Ferries measures the performance of its preservation program in terms of the number of vessel systems and structures refurbished or replaced. Systems and structures may consist of multiple components. For example, the engine system on a ferry may consist of four engines. Overall, investments in ferries replaced 137 systems and structures on 24 of the 28 vessels owned by the ferry system during this time period. 111 vital systems and structures, and 26 other systems and structures were preserved.

Project Facts

- The average age of a WSF vessel is over 30 years. Four were built in 1927.
- WSF will invest $576 million over ten years toward ensuring existing vessels are safe, sound, comfortable and efficient.
- WSF rehabilitates or replaces 717 vessel systems and structures annually.

Vessel Classes of WSF

Steel Electric 1927

Nisqually, Illahee, Quinault, Klickitat - 1927

Miscellaneous 1947

Rhododendron - 1947

Evergreen Class 1954 –1959

Evergreen State - 1954, Klahowya - 1958, Tillikum - 1959

Miscellaneous 1967

Hiyu - 1967

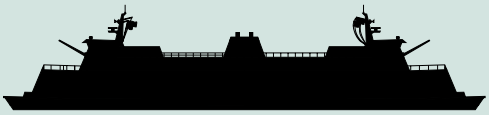
Super Class 1967

Hyak, Kaleetan, Yakima, Elwha - 1967

Jumbo Class 1972

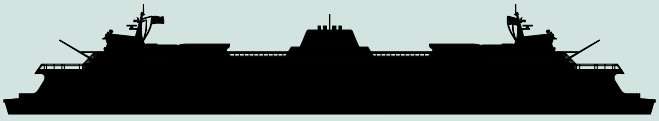
Spokane, Walla Walla - 1972

Issaquah Class 1979 – 1982



Issaquah - 1979, Kittitas - 1980, Kitsap - 1980,
Cathlamet - 1981, CHelan - 1981, Sealth - 1982

Jumbo Mark II Class 1997 – 1999



Tacoma - 1997, Wenatchee - 1998, Puyallup - 1999

Passenger-Only Class – 1989

Skagit, Kalama - 1989

Issaquah Class Biennium Work

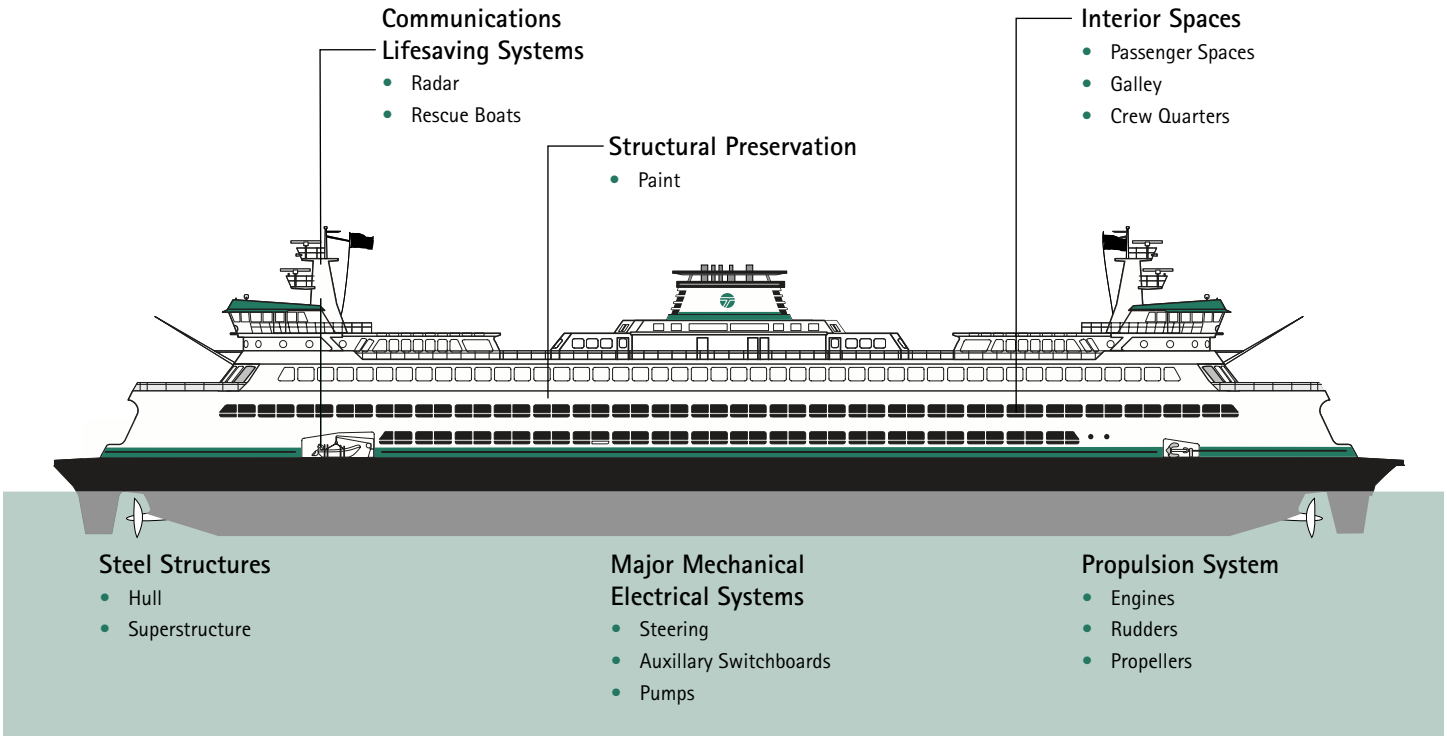
The six vessels in the Issaquah Class were built between 1979 and 1982. They are just past the 30-year midpoint of their expected lives (when preservation costs peak). During the 2001-2003 biennium, WSF spent $32 million to replace or refurbish 75 of the systems and structures on these vessels. The US Coast Guard classified 59 of these systems and structures as vital. Sixteen other systems and structures were also preserved.

The work accomplished renewed the life cycles of 24 propulsion systems, 15 major mechanical systems, 14 communication-navigation-life saving systems, 10 steel structures, nine structural protection systems, two interior spaces, and one piping system.

Examples of equipment and parts that were installed during the 2001-2003 Biennium:

- Old engines were replaced with engines of more fuel efficient design and reduced emissions
- New controllable pitch propeller hubs
- Matthews Marine steering gear controls
- New ships service diesel generators
- A vital service diesel generator
- New pilothouse control consoles
- A remodeled passenger deck interior
- Two new main propulsion General Electric EFI diesel engines
- New rescue boats and davits
- Marine Evacuation Systems
- Vital service diesel generator
- Passenger deck interior package
- SSOG Switchboards with paralleling capabilities
- Carlisle & Finch Zenon Searchlights
- Started the design for Data-cogging capabilities

Vessel Systems and Structures



Jumbo Class Biennium Work

The two vessels in the Jumbo Class were built in 1972. They are also just past the 30-year midpoint of their expected lives. During the 2001-2003 Biennium, WSF spent $16 million to replace or refurbish 14 of the systems and structures on these vessels. The US Coast Guard classified 11 of these systems and structures as vital. Three other systems and structures were also preserved.

The work accomplished renewed the life cycles of five communication-navigation-life saving systems, four steel structures, two propulsion systems, two structural protection systems, and one major mechanical system.

Replaced or refurbished items include rescue boats, the general alarm system, interior communications and temporary emergency power, generators, rudders, steel on the hull, auto deck and superstructure, and protective systems for the hull and sewage tanks.

Evergreen State Class Biennium Work

The three vessels in the Evergreen State Class were built in the 1950's and refurbished in the late 1980's and mid-1990's. They are in the second half of their expected lives. During the 2001-2003 Biennium, WSF spent $14 million to replace or refurbish 11 of the systems and structures on these vessels. The US Coast Guard classified eight of these systems and structures as vital. Three other systems and structures were also preserved.

The work accomplished renewed the life cycles of six propulsion systems, three structural protection systems and two life saving systems.

Replaced or refurbished items include rescue boats, propulsion controls, switchboards, and motors.

Super Class Biennium Work

The four vessels in the Super Class were built in the 1967. Three were refurbished in 1991, 1999 and 2000. One vessel has not yet received major refurbishment. They are in the second half of their expected lives. During the 2001-2003 Biennium, WSF spent $10 million to replace or refurbish 17 of the systems and structures on these vessels. The US Coast Guard classified 13 of these systems and structures as vital. Four other systems and structures were also preserved.

The work accomplished renewed the life cycles of eight communication-navigation-life saving systems, three propulsion systems, three steel structures, two structural protection systems and one piping system.

Types of items replaced or refurbished include

- Rescue boats
- A sprinkler system
- Generators
- Rudders
- Auto deck and tank steel
- Protective systems for potable water and sewage tanks.

Other Vessel Class Biennium Work

WSF spent $5 million to replace or refurbish 20 of the systems and structures on the remaining vessels of the fleet. The US Coast Guard classified all of these systems and structures as vital.

The work accomplished renewed the life cycles of 14 communication-navigation-life saving systems, four propulsion systems, one major mechanical system and one steel structures.

Types of items replaced or refurbished include

- Rescue boats
- Radars
- Diesel engines
- Rudders
- Hull steel
- CO2 system and controls

Environmental Protection

WSF's vessel preservation program provides the following environmental protection:

- Replacing or refurbishing navigation systems allow ferry captains to use state-of-the-art equipment and up-to-date information to safely navigate vessels to avoid potentially hazardous situations (such as shoals or other vessels) in all weather conditions. Installation of these new systems will help to minimize any risk of vessel groundings or collisions and the potential for an oil spill that may result from those types of incidents.

- Replacing or refurbishing propulsion systems allows captains and crew to expertly control vessel speed and direction. Upgrades to these systems also work to minimize any risk of vessel groundings or collision and the potential for resultant spills.

- Replacing or refurbishing mechanical and electrical systems allows WSF to improve the energy efficiency of its vessels. Increased energy efficiency promotes environmental protection in many ways, from reducing the natural resources that are needed to power the vessels, to minimizing the wastes and/or emissions that are generated. WSF is installing new engines in its Jumbo Class vessels. These new engines contain electronic fuel injection systems that will reduce air emissions by up to 50 percent.

- Replacing or refurbishing piping systems ensures that the fluids that are necessary for ships operations (such as fuel, lubricants, fresh water and bilge water) are safely contained and managed inside the vessel. Fluids handled in this way pose little risk of release into the sensitive aquatic environment of Puget Sound.

On the Brink...

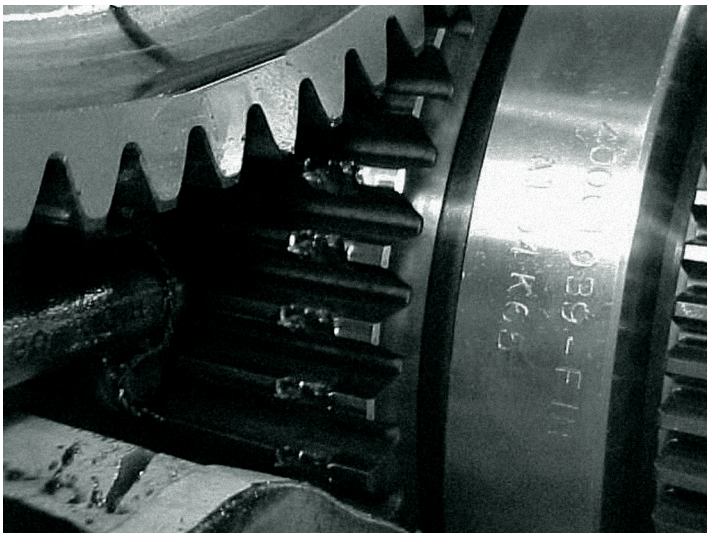
After a vessel's engine reaches its averaged 60-year lifespan, preservation is no longer a viable option. At this point, continuing to funnel money into maintenance and preservation of the vessel becomes irresponsible and ineffective.

With a class of vessels that is over 75 years old, the Steel Electric Class, Washington State Ferries is looking for alternatives to the preservation process. WSF hopes to retire the four Steel Electric Class vessels in the fleet (the *MV Quinalt, MV Nisqually, MV Klickitat* and the *MV Illahee*).

In late 2003, WSF issued the first in a series of Requests For Proposals for a contract to design and build four auto ferries capable of carrying 130 vehicles and over 1,200 passengers and crew per vessel. WSF estimates the contract will be worth $285 million.

The vessels will be passenger friendly, complying with standards under the Americans with Disabilities Act, and safe, conforming to Federal Regulation standards for operations on lakes, bays and sounds.

The plan approved by the legislature schedules the first vessel delivery in 2008. The project will bring new levels of efficiency, reliability and flexibility to the system's ferry fleet.



Vessel Construction Activities

2001-2003 Biennium Investments and Performance Measures

DOLLARS IN MILLIONS

Vessel Investments	Total	Preservation	Improvements
Jumbo Mark II Class Ferries	**$2.1**	**$2.0**	**$0.1**
MV Puyallup	$0.7	$0.7	$0.0
MV Tacoma	$0.5	$0.5	$0.0
MV Wenatchee	$0.8	$0.7	$0.1
Jumbo Class Ferries	**$16.0**	**$16.0**	**$0.0**
MV Spokane	$6.7	$6.7	$0.0
MV Walla Walla	$9.3	$9.3	$0.0
Super Class Ferries	**$10.4**	**$10.4**	**$0.0**
MV Elwha	$3.2	$3.2	$0.0
MV Hyak	$5.9	$5.9	$0.0
MV Kaleetan	$0.9	$0.9	$0.0
MV Yakima	$0.4	$0.4	$0.0
Issaquah Class Ferries	**$31.7**	**$31.7**	**$0.0**
MV Cathlamet	$7.9	$7.9	$0.0
MV Chelan	$3.5	$3.5	$0.0
MV Issaquah	$5.3	$5.3	$0.0
MV Kitsap	$5.1	$5.1	$0.0
MV Kittitas	$3.4	$3.4	$0.0
MV Sealth	$6.5	$6.5	$0.0
Evergreen State Class Ferries	**$14.2**	**$14.2**	**$0.0**
MV Evergreen State	$0.5	$0.5	$0.0
MV Klahowya	$5.9	$5.9	$0.0
MV Tillikum	$7.9	$7.9	$0.0
Steel Electric Class Ferries	**$1.4**	**$1.4**	**$0.0**
MV Illahee	$0.4	$0.4	$0.0
MV Klickitat	$0.5	$0.5	$0.0
MV Nisqually	$0.2	$0.2	$0.0
MV Quinault	$0.4	$0.4	$0.0
Miscellaneous Class Ferries	**$0.3**	**$0.3**	**$0.0**
MV Hiyu	$0.0	$0.0	$0.0
MV Rhododendron	$0.3	$0.3	$0.0
Passenger-only Class Ferries	**$0.2**	**$0.2**	**$0.0**
MV Kalama	$0.2	$0.2	$0.0
MV Skagit	$0.0	$0.0	$0.0
MV Tyee Law	$0.0	$0.0	$0.0
Kalama/Skagit Replacement	$0.0	$0.0	$0.0
Passenger-only Fast Class Ferries	**$0.1**	**$0.1**	**$0.0**
MV Chinook	$0.0	$0.0	$0.0
MV Snohomish	$0.0	$0.0	$0.0
Replacement Auto-passenger Ferries	**$0.2**	**$0.2**	**$0.0**
Emergency Repairs	$1.8	$1.8	$0.0
System-wide Vessel Project	$7.4	$7.4	$0.0
Total Vessel Investments	**$85.9**	**$85.8**	**$0.1**

VIII] Maintaining and Preserving Terminals

Washington State Ferries operates 19 terminals and a major maintenance facility on Bainbridge Island. More than half of WSF's terminals are 50 years old. Aging terminals require preservation and improvement investments to ensure the safety, efficiency, and viability of the facilities for landing, loading, and unloading vessels.

detailed and complex maintenance

Maintenance

Just like vessels, terminal structures have a life expectancy. At any point in time a percentage of these parts are within their life cycle. Each part must be replaced periodically to ensure the entire terminal structure operates safely, soundly, and efficiently.

The ferry system's terminals and maintenance facilities consist of hundreds of systems and structures, many of which are designated as vital to the protection of people and the environment. Generally, they are the systems and structures needed to land, unload and load a vessel.

Terminal Maintenance Program

Similar to the vessel maintenance program, terminal maintenance is accomplished in steps. The one primary difference between the terminal maintenance and vessel maintenance programs is that terminals do not have an equivalent to the vessel engine crew, which is available to the vessel 24 hours a day, seven days a week.

The elements of WSF's Terminal Maintenance Program are as follows:

- On-Site Maintenance & Management: The Facilities Manager performs minor adjustments of building and other engineering system components, provides support to on-site vendor services, and reports observed discrepancies or concern regarding the terminal infrastructures for further evaluation and repair.

- Scheduled Preventative Maintenance Program: Personnel from Washington State Ferries Maintenance Facility perform scheduled preventative maintenance work to the terminal infrastructure and various components as assigned by Terminal Engineering.

- Corrective Maintenance Program: Personnel from the Maintenance Facility are responsible for minor to complex corrective work on site. Crews are dispatched from the Maintenance Facility with the necessary tools, equipment and supplies to complete the work. The availability of Maintenance Facility personnel is particularly important when prompt response is required to restore service after breakdown or damage.

- Vendor Services: Certain work is assigned and designated to outside vendors and contractors for routine maintenance. Examples of this work are tasks such as elevator service, automatic door services and fire sprinkler system services.

- Construction Support: During a construction project, personnel from the Maintenance Facility are often tasked with performing certain work to complete the project.

Preservation

WSDOT used $60.9 million of its 2001-2003 Biennium capital spending authority (excluding emergency repairs) to preserve the ferry system's terminals and maintenance facilities. The major investment during the biennium was the reconstruction of the Clinton Terminal trestle and north vessel slip.

Additional investments replaced or refurbished vessel slips at Anacortes, Bainbridge Island, Fauntleroy, Kingston, Southworth and Tahlequah. Overall, the two-year investment program affected 13 terminals and maintenance facilities by replacing or refurbishing 75 terminal systems and structures, including 37 dolphins and wingwalls; 17 towers, bridge seats, transfer spans and aprons; 9 utility systems; five trestle sections; and seven other structures. This effort increased the life cycle rating for vital assets from 70% to 71%. However, the life cycle rating for other assets dropped from 66% to 62%. The results reflect WSF's emphasis on preserving terminal systems and structures that are vital to the protection of people and the environment.

Clinton Phase 2 Terminal Reconstruction

Phase 2 of the Clinton Terminal Reconstruction project was the final phase of an important terminal construction project that started in the 1990's. The Mukilteo/Clinton route is historically the third largest route in the system, carrying over 4 million riders per year.

Preservation spending at this terminal was the largest single terminal investment made during the 2001-2003 Biennium, amounting to $10.8 million. This project replaced and expanded the remaining timber trestle (part of the timber trestle was replaced in Phase 1 during the 99-01 biennium) with a concrete trestle on steel piling. Other work included the reconstruction (and realignment) of Slip 2; replacing the remaining timber bulkhead with a steel sheet pile and concrete bulkhead; and additional architectural upgrades, including a new agent's office and terminal building.

Environmental Concerns

In Phase One of this project, Washington State Ferries worked with marine scientists to ensure appropriate techniques were used during the dock expansion so that the nearby eelgrass population was not damaged. Eelgrass is a habitat for salmon, which can be harmed by prop-wash from boats and restriction of natural light. The final permitted design impacted only 3,444 square feet of eelgrass habitat, a significant reduction from the 10,280 square feet contemplated in the original design.

To minimize the impact of the new dock on the eelgrass beds, WSF installed glass blocks in the passenger walkway to allow light to penetrate through the deck to the eelgrass below, narrowed the trestle and moved the slips further offshore to minimize the effects of propeller wash scour on eelgrass beds, and relocated an existing private fishing pier and float offshore to reduce shading.

Fauntleroy-Southworth Terminal Preservation

In Fall 2002, WSF closed the Fauntleroy and Southworth Ferry Terminals to repair and improve the docks. The projects were scheduled at the same time to minimize impacts to customers. The projects were designed to make much-needed repairs and replace worn out parts at both terminals.

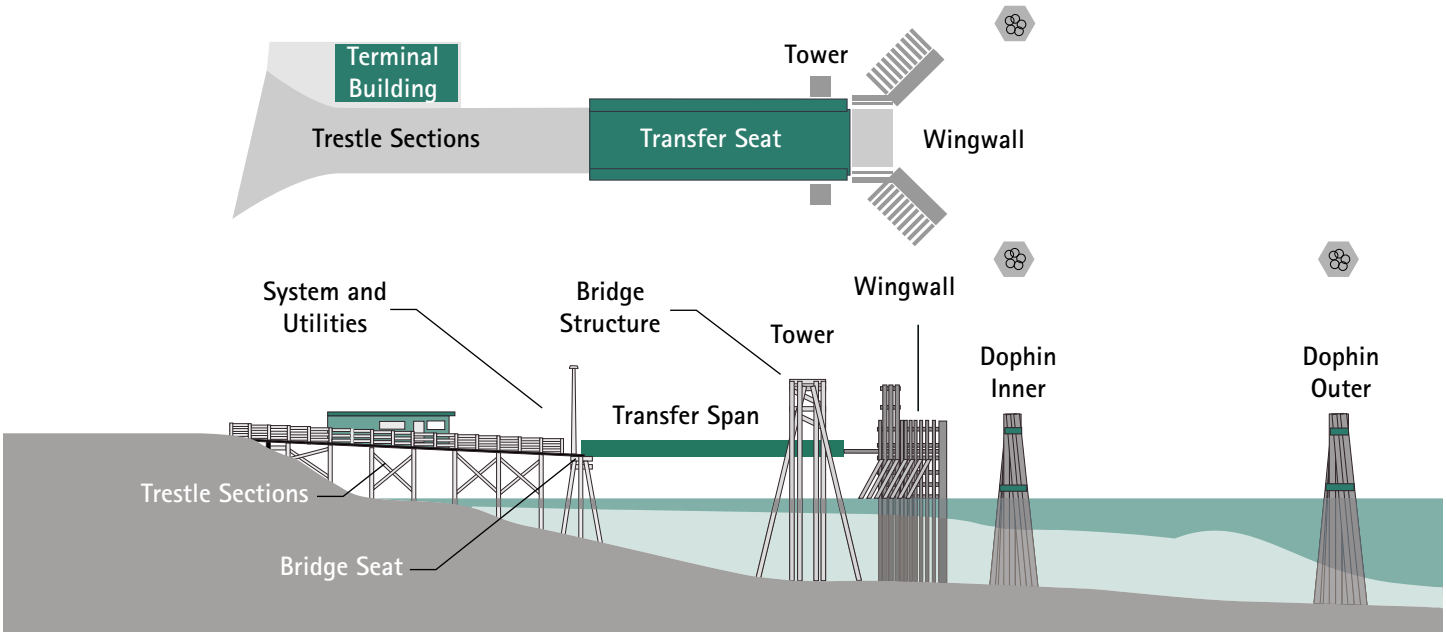
The Southworth and Fauntleroy terminals have been the backbone of the main water link for people and their cars between West Seattle, Vashon Island, and Kitsap County since 1958. It was only a matter of time before everyday wear and tear required WSF to do repairs and replacements.

Preservation spending at the Southworth and Fauntleroy Ferry Terminals amounted to $13.4 million during the 2001-2003 Biennium. At Southworth, preservation investments were made in dolphins, towers, the transfer span, apron, and the foundation. At Fauntleroy preservation investments were made in the wingwalls, transfer span and apron, the north half of the bulkhead or seawall, the south timber trestle and pavement, and the vessel backfeed and cathodic protection systems.

In order to accommodate some of the work, temporary terminal closures were necessary. WSF worked with local transit providers to develop updated bus service and commute options to accommodate customers during the terminal closures. A year prior to construction, the ferry system surveyed customers and asked for their preference regarding possible construction service scenarios. The ferry system took cues from the responses received to formulate a construction plan. With the plan in place, management staged public outreaches on the vessels to inform customers of their options during the construction.

Both the Southworth and Fauntleroy Terminals were closed for three weeks in the fall of 2002. WSF altered its schedule based on discussion with a local watershed group, to protect returning adult salmon in Fauntleroy Creek.

Typical Terminal Structure



Other Terminal Reconstruction and Preservation Projects

Preservation spending at the Anacortes Ferry Terminal amounted to $7.8 million during the biennium. The Slip 2 and Phase 1 Dolphin Replacement project preserved the Auxiliary South Slip 2 towers, bridge seat, transfer span and apron; three dolphins of the Main North Slip 1;three dolphins of the Auxiliary South Slip 2 and the vessel backfeed, backup generator and signage systems.

Preservation spending at the Bainbridge Island Ferry Terminal amounted to $3.4 million during the biennium. The Dolphin Replacement project preserved four dolphins of the Main North Slip, two dolphins of the Center Auxiliary Slip, one dolphin of the Tie-up Slip, and pavement on the timber trestle and the upland holding area.

Preservation spending at the Kingston Ferry Terminal amounted to $3.4 million during the biennium. The Dolphin Replacement Phase 2 project constructed three dolphins, towers, the transfer span and apron at the Auxiliary North Slip 2 and two dolphins at Main Center Slip 2. The Sewer Outfall project compensated Kitsap County for the costs to replace an effluent outfall line damaged during ferry terminal construction activity.

Preservation spending at the Tahlequah Ferry Terminal amounted to $1.5 million during the biennium. The Dolphin Replacement Phase I project preserved two dolphins.

Preservation spending noted above for Anacortes and Bainbridge Island Ferry Terminals plus the Seattle Ferry Terminal included the repair of passenger overhead loading facilities. The work involved modifying the hoist cable system, improving operator visibility, increasing operator control of passenger access, installing emergency lighting, and increasing live load pin monitoring at each terminal.

Emergency Expenditures

When a ferry terminal is damaged, WSF works hard to correct the problem immediately, as it affects the viability of the entire route.

In the 2001-2003 Biennium, Ferry System terminals required expenditures of $4.8 million for emergency repairs. This constituted 72% of all emergency spending. Ten of the 19 terminals operated by WSF required this type of investment. They included the terminals at Anacortes, Bremerton, Clinton, Fauntleroy, Friday Harbor, Keystone, Point Defiance, Seattle, Southworth and Vashon.

Improvement Expenditures

WSF allocated $7.7 million or 10.5% of the funds invested in its terminals for improvements. Improvement projects increase the capacity of a terminal to move riders and vehicles through the facility; provide mobility options, such as access to transit and commuter rail; or generate revenue to support the ferry system. Improvement spending took place at five WSF shore-side facilities. In order of magnitude of investment, these facilities are Clinton, Seattle, Mukilteo, Eagle Harbor, and Bainbridge Island. Other small investments were made system-wide.

Improvement spending at the Clinton Ferry Terminal amounted to $4.3 million. Most of the expenditures were made to expand the trestle in conjunction with the preservation project. Less than $100,000 went to close the prior biennium project to widen the trestle.

Improvement spending at the Seattle Ferry Terminal amounted to $1.9 million. Three-quarters of expenditures were used to complete the Slip 1 Overhead Loading project started prior to the 2001-2003 Biennium. Remaining funds were used for planning future improvements to the terminal, preparing the SR 10—Pier 52 Access Study and designing retail space at the terminal for revenue generation.

Improvement spending at the Mukilteo Ferry Terminal amounted to $1.3 million. These funds were used to plan the relocation of the terminal to a more favorable site and to design a multimodal transportation facility.

Improvement spending at the Eagle Harbor Maintenance Facility amounted to $100,000. The funds were used to prepare a master plan for future development of the facility.

Investment spending at the Bainbridge Island Ferry Terminal consisted of a negligible amount expended to close out the project to widen the lower vehicle holding area that was substantially completed in the prior biennium.

Finally, WSF spent a minor amount for system-wide planning of business initiatives that have the potential of generating revenue for the ferry system.

The table on page 51 summarizes terminal investments in the 2001-2003 Biennium in terms of the three categories: preservation, improvements and emergency repairs.

Environmental Protection

Preservation of terminal structures protects the environment by:

- Reducing the risk of damage to the environment caused by failure of terminal systems and structures;
- Eliminating marine contamination by replacing creosote-treated timber terminal structures with concrete and steel structures;
- Employing environmental mitigation, such as replanting eel-grass; and
- Controlling and removing hazardous materials at terminal and maintenance sites.

Terminal Construction Activities

2001-2003 Biennium Investments and Performance Measures

DOLLARS IN MILLIONS

Terminal Investments	Total	Preservation	Improvements
Anacortes Terminal	$7.8	$7.8	$0.0
Bainbridge Island Terminal	$3.4	$3.4	$0.0
Bremerton Terminal	$0.6	$0.6	$0.0
Clinton Terminal	$15.0	$10.8	$4.3
Eagle Harbor Maintenance Facility	$3.7	$3.6	$0.1
Edmonds Terminal	$0.0	$0.0	$0.0
Fauntleroy Terminal	$5.9	$5.9	$0.0
Friday Harbor Terminal	$1.1	$1.1	$0.0
Keystone Terminal	$0.0	$0.0	$0.0
Kingston Terminal	$3.4	$3.4	$0.0
Lopez Terminal	$0.0	$0.0	$0.0
Mukilteo Terminal	$2.2	$0.9	$1.3
Orcas Terminal	$0.0	$0.0	$0.0
Point Defiance Terminal	$0.0	$0.0	$0.0
Port Townsend Terminal	$1.8	$1.8	$0.0
Seattle Terminal	$3.1	$1.1	$1.9
Shaw Terminal	$1.9	$1.9	$0.0
Southworth Terminal	$7.5	$7.5	$0.0
Tahlequah Terminal	$1.5	$1.5	$0.0
Vashon Terminal	$0.1	$0.1	$0.0
Emergency Repairs	$4.9	$4.9	$0.0
System-wide Terminal Projects	$9.1	$9.1	$0.0
Total Terminal Investments	**$73.1**	**$65.4**	**$7.7**

IX] Looking Forward

Washington State Ferries has experienced many paradigm shifts over the past two years; some were prompted internally, while others were a matter of course.

there will be challenges

The ferry system is tackling the funding and viability of our organization in a whole new way, going from relying on the Motor Vehicle Excise Tax to recovering up to 90% of our operating costs through efficiencies and non-farebox revenues. Not wanting to rely soley on the farebox for this revenue, the ferry system is seeking creative ways of attaining the money, exploring business and profit opportunities from previously untapped sources.

WSF believes that the Business and Capital Funding Plans will allow us to generate new revenue to stabilize ferry system financing and build four new ferry vessels. The ultimate goal is to begin expanding ferry services once again; thereby increasing service for our customers and providing new jobs.

WSF has responded to the national call to tighten security. Over the past two years, WSF addressed Coast Guard regulations, State and Federal legislation on both domestic and international security requirements and new immigration laws. WSF formed a Security Committee (consisting of WSF, USCG, and WSP) to assess risks, flesh out security requirements, and formulate a compliance plan. In 2003, the Security Committee's work coalesced in a cohesive and comprehensive Security Plan that the ferry system will implement by 2004.

With this work behind us, we look forward to the days ahead, knowing that we are capable of rising to the challenges of a time when funding is seemingly ever dwindling, and security is more necessary than ever.

We know there will be challenges. And, we are ready to face them. With every challenge – either financial, safety, or operational – Washington State Ferries continues to take the opportunity to show our customers and stakeholders our ability to manage and operate the country's largest ferry system in good times and bad.

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