1-FRR as method of funding replacement Ferry

The Ferry Replacement Reserve (FRR) is not fit for the purpose of funding the ferry replacement. It would require the current, rather than future users, of the ferry to fund the purchase of a new vessel that would not come into service until 2032. …………. Now hold that thought……………………………

- The Accounts and Balance Sheet of the Applicant: Bournemouth – Swanage Motor Road and Ferry Company - aka Sandbanks Ferry Company (SFC) - include Other Reserves which in the notes to the Balance Sheet are described as the Ferry Replacement Reserve (FRR). This is an arcane method of accounting and can be likened to a Sinking Fund which is rarely seen other that in exam papers of the Institute of Chartered Accountants back in the 1960's.
- The idea was to put aside Net Profit after Taxation to facilitate the purchase of a new ferry. Regrettably SFC have seen fit in past years to prioritise the payment of an ever increasing dividend at the expense of the FRR. It was therefore the FRR that suffered when there were not sufficient profits for the required divided and the FRR was raided to maintain the ever-increasing dividends. The effect of this is highlighted by the fact that in 2008 the FRR stood at £2.496M and 10 years later in 2018 the balance was £2.491M. (Please see appendix MT1 for the historical movements).
- The estimated replacement cost of a new ferry in 2032 is £12.8M and appendix MT 2 shows the projected future movement in the FRR. This information is taken from Applicant's appendix 2.2 .Following criticism from the 2018 Inspector, SFC have volunteered to make transfers to the FRR before payment of the dividend.
- There are no other Revenue Reserves of SFC as the company pursues a policy of total distribution. Consequently no fall back funds to cover unforeseen eventualities.
- The use of an FRR for replacing the Ferry is an extremely inefficient method of replacing the ferry. It pre-supposed that all funds are raised from existing users in advance of the event. These funds are treated by HMRC as revenue and are subject to tax in advance of the purchase. With current Corporation Tax (CT) rates at 19% SFC need to raise £15.8M gross to have £12.8M net of tax. In the event that the CT rate were to increase it would be necessary for the fares to increase pro rata.

- Commercial practice would be to match the purchase of the fixed asset with loan and equity using revenue streams and tax relief to fund the purchase. That way would ensure future users of the ferry would be paying for a new ferry that will operate from 2032. SFC would have the benefit of substantial tax reliefs which would equate to £2.43M in cash terms at current CT rates. In the 2020 Application the parent company have volunteered a £5M loan that was not included in the previous unsuccessful application and partially recognises that they cannot hope to put all the purchase cost onto the users by way of the FR
- If the Applicants were to be successful in the fare increase for the next 12 years, it would amount to enrichment of the SFC to the detriment of the existing users. SFC would have the ability to pay dividends to Fairacres Group Ltd in excess of £9M, transfer £5.3M to the FRR and have a shiny new ferry. They would benefit from lower running and maintenance costs, substantial tax reliefs and the ability to pay dividends in excess of £1M pa already projected.

Now back to the beginning -

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Malcolm Tice

11th November 2020