ACE AVIATION

Quarter 2 2006
Interim Unaudited Consolidated Financial Statements and Notes

AUGUST 10, 2006

ACE AVIATION

Consolidated Statement of Operations and Retained Earnings

(in millions except per share figures - Canadian dollars) *(unaudited)*		Three Months Ended June 30		Six Months Ended June 30	
		2006	**2005**	**2006**	**2005**
Operating revenues					
Passenger		**$ 2,288**	$ 2,100	**$ 4,309**	$ 3,839
Cargo		**152**	147	**303**	282
Other		**242**	211	**554**	514
		2,682	2,458	**5,166**	4,635
Operating expenses					
Salaries, wages and benefits		**636**	622	**1,278**	1,235
Aircraft fuel		**631**	530	**1,200**	945
Aircraft rent		**113**	98	**226**	188
Airport and navigation fees		**245**	230	**475**	443
Aircraft maintenance, materials and supplies		**118**	89	**247**	183
Communications and information technology		**69**	78	**147**	155
Food, beverages and supplies		**82**	81	**162**	159
Depreciation, amortization and obsolescence		**140**	119	**274**	239
Commissions		**59**	73	**127**	138
Special charges for labour restructuring	note 5	**-**	-	**33**	-
Other		**408**	360	**878**	782
		2,501	2,280	**5,047**	4,467
Operating income		**181**	178	**119**	168
Non-operating income (expense)					
Interest income		**29**	15	**51**	27
Interest expense		**(91)**	(77)	**(179)**	(152)
Interest capitalized		**13**	3	**22**	6
Gain on sale of US Airways shares	note 2	**100**	-	**100**	-
Gain on sale of assets		**1**	-	**4**	-
Dilution gain	note 7	**-**	190	**220**	190
Other		**-**	(27)	**3**	(30)
		52	104	**221**	41
Income before the following items		**233**	282	**340**	209
Non-controlling interest		**(19)**	(4)	**(34)**	(7)
Foreign exchange gain (loss)		**107**	(53)	**120**	(68)
Provision for income taxes		**(85)**	(56)	**(72)**	(42)
Income for the period		**$ 236**	**$ 169**	**$ 354**	**$ 92**
Retained earnings, beginning of period as originally reported		**533**	80	**415**	157
Adjustment related to change in accounting policy	note 1	**(13)**	(16)	**(13)**	(16)
Retained earnings, beginning of period as restated		**520**	64	**402**	141
Retained earnings, end of period		**$ 756**	**$ 233**	**$ 756**	**$ 233**
Earnings per share					
- Basic		**$ 2.32**	**$ 1.68**	**$ 3.47**	**$ 0.97**
- Diluted		**$ 2.05**	**$ 1.50**	**$ 3.16**	**$ 0.93**

The accompanying notes are an integral part of the consolidated financial statements.

(in millions of Canadian dollars) *(unaudited)*		June 30, 2006	December 31, 2005
ASSETS			
Current			
Cash and cash equivalents		$ **2,055**	$ 1,565
Short-term investments		**767**	616
		2,822	2,181
Restricted cash		**26**	86
Accounts receivable		**778**	637
Spare parts, materials and supplies		**284**	325
Prepaid expenses and other current assets		**112**	125
		4,022	3,354
Property and equipment		**5,753**	5,494
Deferred charges		**126**	145
Intangible assets	note 8	**2,267**	2,462
Investments and other assets		**306**	392
		$ 12,474	**$ 11,847**
LIABILITIES			
Current			
Accounts payable and accrued liabilities		$ **1,425**	$ 1,355
Advance ticket sales		**968**	711
Current portion of Aeroplan deferred revenues		**731**	680
Current portion of long-term debt and capital leases		**280**	265
		3,404	3,011
Long-term debt and capital leases	note 3	**3,584**	3,543
Convertible preferred shares		**157**	148
Future income taxes		**187**	221
Pension and other benefit liabilities		**2,062**	2,154
Non-controlling interest		**221**	203
Aeroplan deferred revenues		**967**	953
Other long-term liabilities		**422**	446
		11,004	10,679
SHAREHOLDERS' EQUITY			
Share capital and other equity	note 6	**691**	747
Contributed surplus	note 1	**23**	19
Retained earnings	note 1	**756**	402
		1,470	1,168
		$ 12,474	**$ 11,847**

The accompanying notes are an integral part of the consolidated financial statements.

Contingencies are described in Note 12.

ACE AVIATION

Consolidated Statement of Cash Flow

(in millions of Canadian dollars) *(unaudited)*		Three Months Ended June 30		Six Months Ended June 30	
		2006	2005	**2006**	2005
Cash flows from (used for)					
Operating					
Income for the period		**$ 236**	$ 169	**$ 354**	$ 92
Adjustments to reconcile to net cash provided by operations					
Depreciation, amortization and obsolescence		**140**	119	**274**	239
Gain on sale of US Airways shares	note 2	**(100)**	-	**(100)**	-
Gain on sale of assets		**(1)**	-	**(4)**	-
Dilution gain	note 7	**-**	(190)	**(220)**	(190)
Foreign exchange (gain) loss		**(134)**	40	**(130)**	55
Future income taxes		**86**	53	**71**	36
Employee future benefit funding more than expense		**(46)**	(6)	**(68)**	(14)
Decrease (increase) in accounts receivable		**(127)**	(108)	**(143)**	(199)
Decrease (increase) in spare parts, materials and supplies		**(25)**	(19)	**35**	(5)
Increase (decrease) in accounts payable and accrued liabilities		**(43)**	(40)	**55**	60
Increase (decrease) in advance ticket sales, net of restricted cash		**184**	219	**389**	438
Other		**40**	102	**54**	141
		210	339	**567**	653
Financing					
Issue of common shares		**1**	443	**3**	443
Issue of convertible notes		**-**	319	**-**	319
Issue of Aeroplan units		**-**	232	**-**	232
Issue of Jazz units	note 7	**-**	-	**218**	-
Credit facility borrowings - Aeroplan		**-**	318	**-**	318
Credit facility borrowings - Jazz	note 3	**-**	-	**113**	-
Aircraft related borrowings	note 3	**98**	-	**222**	-
Reduction of long-term debt and capital lease obligations		**(61)**	(627)	**(149)**	(767)
Distributions paid to non-controlling interests		**(14)**	-	**(22)**	-
Other		**-**	(5)	**-**	(5)
		24	680	**385**	540
Investing					
Short-term investments		**8**	(680)	**(151)**	(1,355)
Additions to capital assets		**(199)**	(57)	**(479)**	(95)
Proceeds from sale of assets		**-**	-	**-**	37
Sale of US Airways shares	note 2	**158**	-	**158**	-
Proceeds from sale of Aeroplan units		**-**	35	**-**	35
Proceeds from sale of Jazz units	note 7	**-**	-	**14**	-
Cash collaterization of letters of credit		**-**	-	**(4)**	(20)
		(33)	(702)	**(462)**	(1,398)
Increase (decrease) in cash and cash equivalents		**201**	317	**490**	(205)
Cash and cash equivalents, beginning of period		**1,854**	959	**1,565**	1,481
Cash and cash equivalents, end of period		**$ 2,055**	**$ 1,276**	**$ 2,055**	**$ 1,276**
Cash payments of interest		**$ 77**	**$ 56**	**$ 140**	**$ 109**
Cash payments of income taxes		**$ 3**	**$ 5**	**$ 6**	**$ 9**

Cash and cash equivalents exclude Short-term investments of $767 as at June 30, 2006 ($616 as at December 31, 2005)

The accompanying notes are an integral part of the consolidated financial statements.

For the period ended June 30, 2006 (unaudited)
(currencies in millions – Canadian dollars)

1. NATURE OF OPERATIONS AND ACCOUNTING POLICIES

ACE Aviation Holdings Inc. ("ACE") is the parent holding company of various transportation and other service companies and partnerships, which are operated through the following four reporting segments: Transportation Services, Aeroplan Limited Partnership ("Aeroplan"), Jazz Air Limited Partnership ("Jazz") and ACTS Limited Partnership ("ACTS"). The Transportation Services segment includes the following principal operating companies and partnerships: Air Canada, ACGHS Limited Partnership ("ACGHS"), Touram Limited Partnership ("Air Canada Vacations") and AC Cargo Limited Partnership ("Air Canada Cargo"). As at June 30, 2006, ACE holds a 75.3 percent direct ownership interest in Aeroplan and a 79.7 percent direct ownership interest in Jazz.

Reference to "Corporation" in the following notes to the consolidated financial statements refers, as the context may require, to ACE and its subsidiaries collectively, ACE and one or more of its subsidiaries, one or more of ACE's subsidiaries, or ACE itself.

The unaudited interim consolidated financial statements for the Corporation are based on the accounting policies consistent with those disclosed in Note 2 to the 2005 annual consolidated financial statements of ACE, with the exception for the policy on stock-based compensation for employees eligible to retire before the vesting period that is addressed below.

In accordance with Canadian generally accepted accounting principles ("GAAP"), these interim financial statements do not include all of the financial statement disclosures required for annual financial statements and should be read in conjunction with the 2005 annual consolidated financial statements of ACE. In management's opinion, the financial statements reflect all adjustments that are necessary for a fair presentation of the results for the interim periods presented.

The Corporation has historically experienced considerably greater demand for its services in the second and third quarters of the calendar year and significantly lower demand in the first and fourth quarters of the calendar year. This demand pattern is principally a result of the high number of leisure travelers and their preference for travel during the spring and summer months. The Corporation has substantial fixed costs in its cost structure that do not meaningfully fluctuate with passenger demand in the short-term.

EIC-162: Stock-Based Compensation for Employees Eligible to Retire Before the Vesting Date
On July 6, 2006, the Emerging Issues Committee of the Accounting Standards Board of Canada issued EIC-162 – Stock-based compensation for employees eligible to retire before the vesting date. EIC-162 requires that the compensation cost for a stock option award attributable to an employee who is eligible to retire at the grant date be recognized on the grant date, if the employee can retire from the entity at any point and the award's exercisability does not depend on continued service. It further requires that the compensation cost for a stock option award attributable to an employee who will become eligible to retire during the vesting period be recognized over the period from the grant date to the date the employee becomes eligible to retire. This accounting treatment should be applied retroactively, with restatement of prior periods, for financial statements ending on or after December 31, 2006. Earlier adoption is encouraged.

Prior to the adoption of EIC-162, the fair value of stock options granted was recognized as a charge to salaries and wages expense on a straight line basis over the applicable vesting period, without regard to when an employee was eligible to retire. EIC-162 is applicable to the Corporation as the terms of the Corporation's stock option plan specify that upon the retirement of the employee, options granted may be exercised as the rights to exercise accrue.

The Corporation has adopted EIC-162 in the period ended June 30, 2006 with restatement of prior periods. The impact in these interim financial statements of adopting EIC-162 is a charge to retained earnings of $16 and $13 as at January 1, 2005 and January 1, 2006, respectively, a decrease to Salaries, wages and benefits expense of $1 for the period ended June 30, 2005 and an increase of $1 to Salaries, wages and benefits expense for the period ended June 30, 2006 offset against Contributed Surplus. The basic and diluted earnings per share increased by $0.01 for the periods ending June 30, 2005 and decreased by $0.01 for the periods ending June 30, 2006.

Future Accounting Pronouncements

Financial Instruments, Comprehensive Income and Hedges
The Accounting Standards Board has issued three new standards dealing with financial instruments: (i) Financial Instruments – Recognition and Measurement, Disclosure and Presentation, (ii) Hedges and (iii) Comprehensive Income. The key principles under these standards are that all financial instruments, including derivatives, are to be included on a company's balance sheet and measured, initially at their fair values. Subsequent measurement depends on the classification of the instrument and is either at fair value or, in limited circumstances when fair value may not be considered most relevant, at cost or amortized cost. Financial instruments intended to be held-to-maturity should be measured at amortized cost. Existing requirements for hedge accounting are extended to specify how hedge accounting should be performed. Also, a new location for recognizing unrealized gains and losses of certain financial instruments on the balance sheet entitled other comprehensive income has been introduced. The new standards are effective for the Corporation beginning January 1, 2007. The standards do not permit restatement of prior years' financial statements, however, the standards have detailed transition provisions. The Corporation is in the process of evaluating all of the consequences of the new standards; which may have a material impact on the Corporation's financial statements.

2. SALE OF US AIRWAYS SHARES

In Quarter 3 2005 the Corporation made an investment of US$75 in US Airways Group, Inc. ("US Airways") for 5 million shares.

On April 10, 2006, the Corporation disposed of 1.75 million shares of its holdings in US Airways to PAR Investment Partners LP. The proceeds from the sale transaction amounted to $78 (US$68). ACE has recorded a pre-tax gain of $46 ($38 after tax) in Quarter 2 2006 as a result of this transaction.

Over the period from June 7, 2006 to July 6, 2006, the Corporation disposed of 2.75 million shares of its holdings in US Airways through a series of transactions on the open stock market at an average price of over US$50 per share. Prior to June 30, 2006, 1.5 million shares were sold at an average price of over US$47 per share for net proceeds of $80 (US$72). The Corporation has recorded a pre-tax gain of $54 ($45 after tax) in Quarter 2 2006 as a result of these transactions.

In July the Corporation sold an additional 1.25 million shares at an average price of over US$53 per share for net proceeds of $74 (US$66). The Corporation has recorded a pre-tax gain of $52 ($43 after tax) in Quarter 3 2006 as a result of these transactions.

As of August 10, 2006, ACE continues to hold 0.5 million shares in US Airways with a market value of US$20.

3. LONG-TERM DEBT AND CAPITAL LEASES

Embraer Aircraft Financing

In Quarter 2 2006, Air Canada drew loans to finance the acquisition of four Embraer aircraft totalling $98 (US$88). The loans, secured by the Embraer aircraft, are to be repaid in quarterly instalments and mature in 2021. Quarterly principal repayment requirements through 2010 are approximately US$1. The borrowings bear interest at a weighted average fixed interest rate of 8.37%.

In Quarter 1 2006, Air Canada drew loans to finance the acquisition of five Embraer aircraft totalling $124 (US$107). The loans, secured by the Embraer aircraft, are to be repaid in quarterly instalments and mature between 2018 and 2021. Quarterly principal repayment requirements through 2010 are approximately US$1. The majority of the borrowings bear interest at a weighted average fixed interest rate of 7.80% and the remainder bear interest at a floating interest rate equal to the three month US LIBOR plus 3.25% (8.75% as at June 30, 2006).

Revolving Credit Facilities

Air Canada

On March 31, 2006, Air Canada finalized amendments to its existing senior secured syndicated revolving credit facility, including reductions in interest rates and standby fees. The aggregate amount available was also amended to $250 (or the US dollar equivalent) from $300 (or the US dollar equivalent). Specifically, the interest rate margin has been adjusted downwards by 0.25% to rates ranging from LIBOR plus 2.25% to 3.25% or prime plus 1.25% to 2.25% (based on Air Canada's earnings before interest, taxes, depreciation, amortization and obsolescence and aircraft rent). As at June 30, 2006, no amount was drawn under this facility.

Jazz

In connection with the initial public offering of the Jazz Air Income Fund (refer to Note 7), Jazz arranged for a senior secured syndicated credit facility in the amount of $150. On closing of the offering, $115 was drawn under the credit facility ($113 net of fees). The facility bears interest at floating rates and has a three year term. The outstanding credit facility is secured by substantially all the present and future assets of Jazz. Jazz entered into swap agreements with third parties with a nominal value of $115 to receive floating rates and pay fixed rates of 7.09% (Note 11). Jazz has repaid term loans and credit facilities of $14 that were outstanding as at December 31, 2005.

ACE Convertible Senior Notes

In connection with the special distribution of units of Aeroplan Income Fund to the shareholders of ACE (refer to Note 8), the conversion rate of the 4.25% Convertible Senior Notes due 2035 ("Convertible Notes") has been adjusted from 20.8333 to 22.2838 Class A variable voting shares (if the holder is not a Canadian) or Class B voting shares (if the holder is Canadian) per $1,000 principal amount of Convertible Notes. This adjustment was effective on March 22, 2006 and has been determined in accordance with the terms of indenture governing the Convertible Notes.

4. POST-EMPLOYMENT EXPENSES

The Corporation has recorded pension and other employee future benefits expense as follows:

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
Pension benefit expense	**$ 46**	$ 47	**$ 91**	$ 78
Other employee future benefit expense	**27**	26	**55**	65
Total	**$ 73**	$ 73	**$ 146**	$ 143

5. LABOUR RELATED PROVISIONS

The following table outlines the changes to labour related provisions:

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
Beginning of period	**$ 177**	**$ 185**	**$ 157**	**$ 192**
Charges recorded	**2**	**3**	**35**	**4**
Amounts disbursed	**(15)**	**(10)**	**(28)**	**(18)**
End of period	**164**	**178**	**164**	**178**
Current portion	**(72)**	**(50)**	**(72)**	**(50)**
Long-term employee liabilities	**$ 92**	**$ 128**	**$ 92**	**$ 128**

The current portion of labour related provisions are included in Accounts payable and accrued liabilities. The long-term portion is included in Other long-term liabilities.

In February, 2006, the Corporation announced that certain ACE companies would proceed with the reduction of non-unionized staffing levels by 20%. The non-unionized staff reductions are primarily at Air Canada, ACTS, ACGHS and Air Canada Cargo. A special charge of $33 was recorded during Quarter 1 2006 relating to staff reductions, with $28 recorded in Transportation Services and $5 in ACTS.

6. SHARE INFORMATION

As at June 30, 2006, the issued and outstanding common shares of ACE, along with common shares potentially issuable, pursuant to convertible preferred shares, convertible notes and stock options were as follows:

	Authorized	Number of shares (000) At June 30, 2006	Number of shares (000) At December 31, 2005
Issued and outstanding common shares			
Class A variable voting shares	unlimited	**79,600**	76,735
Class B voting shares	unlimited	**22,360**	25,059
Shares held in escrow		**-**	28
Total issued and outstanding common shares		**101,960**	101,822
Potential common shares			
Convertible preferred shares		**10,483**	10,228
Convertible notes		**7,354**	6,875
Stock options		**3,869**	3,187
Total potential common shares		**21,706**	20,290

The information presented in the table above reflects the changes in connection with the special distribution of Aeroplan units (refer to Note 8).

7. DISPOSAL OF INTERESTS IN JAZZ

ACE completed an initial public offering of the Jazz Air Income Fund ("Jazz Fund") on February 2, 2006. The Jazz Fund subscribed for 23.5 million units of Jazz at a price of $10.00 per unit for net proceeds of $218, net of offering costs of $17 that were paid during Quarter 1 2006. Concurrent with the closing of the initial public offering, Jazz received proceeds of $113, net of fees of $2, representing the drawing under a new term credit facility (refer to Note 3).

On February 27, 2006, following the exercise of the over-allotment option by the underwriters, the Jazz Fund issued an additional 1.5 million units at a price of $10.00 per unit for additional net proceeds of approximately $14. The Jazz Fund is an unincorporated, open-ended trust that indirectly holds 20.3% of the outstanding limited partnership units of Jazz. ACE holds the remaining 79.7% of the outstanding limited partnership units of Jazz.

Certain of the units held by the Corporation (the "Subordinated Units") representing 20% of the units issued and outstanding at the closing are subordinated. Distributions on the Subordinated Units will be subordinated in favour of the non-subordinated units. Distributions (including in respect of accrued deficiencies in distributions) will only be paid by Jazz on the Subordinated Units at the end of the fiscal quarter.

Under the terms of an investor liquidity agreement, the units held by ACE in Jazz, to the extent not subordinated, are exchangeable for Jazz Fund units on a one-to-one basis. The subordinated units of Jazz held by ACE will become exchangeable after December 31, 2006. The exchange right expires once all units of Jazz held by ACE have been exchanged. The investor liquidity agreement also provides for registration and other liquidity rights that enable it to require the Jazz Fund to file a prospectus and otherwise assist with a public offering subject to certain restrictions.

ACE has recorded a dilution gain of $220 in Quarter 1 2006 and a non-controlling interest on the statement of financial position of $10 as a result of the dilution of its interests in Jazz. The dilution gain is the net proceeds of the offering in excess of ACE's proportionate carrying value of its investment in Jazz. In addition, a future income tax expense of $10 was recorded in Quarter 1 2006.

8. SPECIAL DISTRIBUTION OF AEROPLAN UNITS

On February 16, 2006, ACE's Board of Directors declared a special distribution of units of the Aeroplan Income Fund to ACE's shareholders. The distribution of 0.18 Aeroplan unit per Class A variable voting share, Class B voting share, and preferred share (on an as converted basis) of ACE was made as a return of capital and represents in the aggregate approximately 10.1% of the units of Aeroplan Income Fund on a fully diluted basis. The record date for the purpose of the special distribution was March 3, 2006. Based on the closing price of the units of Aeroplan Income Fund on March 3, 2006, the fair value of the units distributed amounted to $251.

Units of Aeroplan cannot be distributed to shareholders of ACE that are resident in the United States. A total of 7,085,111 units of Aeroplan Income Fund, representing those Aeroplan units that would have otherwise been delivered to shareholders of ACE that are resident in the United States, as well as those units of Aeroplan that would have otherwise been delivered to the registered shareholders of ACE holding less than 200 shares in the capital of ACE and any fractional interests in units of Aeroplan, were sold through an orderly sale process on the Toronto Stock Exchange and the net cash proceeds of such sale of units were remitted to shareholders. A total of 20,204,165 Aeroplan units were distributed as part of the special distribution to ACE shareholders, of which 13,119,054 units were delivered to ACE shareholders and the remaining 7,085,111 units were sold on the Toronto Stock Exchange. Following the completion of the distribution, and the funding of Aeroplan's Initial Long Term Incentive Plan as described below, ACE's direct interest in Aeroplan is 75.3% and Aeroplan Income Fund's interest is 24.7%.

The special distribution to Class A and Class B shareholders totaling 18,347,309 Aeroplan units is a non-monetary non-reciprocal transfer to owners. Non-monetary non-reciprocal transfers to owners are recorded at the carrying amount of the net assets transferred and do not give rise to a gain or loss. As Aeroplan is in a deficit position, in these consolidated financial statements, no amounts have been reflected for this element of the distribution, other than accounting entries relating to future income taxes described below.

The special distribution to preferred shareholders of ACE totaled 1,856,856 Aeroplan units. This transaction is considered a non-reciprocal transfer to non-owners since the holders of the Convertible Preferred Shares are not considered owners of the Corporation for accounting purposes. The transfer is measured at fair value at the date of distribution and results in net interest expense of $4 recorded in Quarter 1 2006 and a reduction to intangible assets of $4. The net interest expense of $4 is the fair value of the distribution of $23 less a gain recorded of $19, which is the fair value of the distribution in excess of the Corporation's proportionate carrying value of its investment in Aeroplan of $4 (including fair value adjustments recorded on consolidation).

The special distribution has no cash tax consequences. However, the distribution involves a use of loss carry forwards in ACE giving rise to a reduction in future income tax assets of $65. $59 relates to the distribution to the Class A and Class B shareholders which is recorded as a reduction in Share capital and Intangible assets in accordance with the Corporation's accounting policy on income taxes. The remaining $6 relating to the distribution to preferred shareholders is recorded as a future income tax expense in the statement of operations in Quarter 1 2006.

In accordance with the terms of the ACE Convertible Senior Notes, the special distribution and return of capital triggers a conversion rate adjustment (refer to Note 3). This change in the conversion rate did not have any accounting consequences. Similarly, the Corporation's stock option plan provides for amendments to the option exercise price and the number of common shares to which participants are entitled to exercise. Effective March 22, 2006 the adjustment was applied to all unexercised ACE stock options as of March 1, 2006, whether vested or not. As at the adjustment date, the weighted average exercise price and number of options outstanding had been amended from $25.54 and 3,131,946 options to $23.87 and 3,350,193 options.

Initial Long Term Incentive Plan – Aeroplan
On March 31, 2006 ACE exchanged on a 1:1 basis 500,000 of its Aeroplan Limited Partnership units into Aeroplan Income Fund units. The Aeroplan Income Fund units were transferred to a trust for the purpose of funding the Initial Long Term Incentive Plan of Aeroplan. The transfer is recorded at the carrying amount of the net assets transferred and does not give rise to a gain or loss. Under the terms of the plan 50% of the Units granted are subject to vesting conditions based on performance and the remaining 50% based on time. Performance based Units vest at the end of each performance period if distributable income targets established by Aeroplan's board of directors for each of the periods ended December 31, 2005, 2006 and 2007 are met, or

on a cumulative basis at the end of the following performance period if such targets are met in that following performance period. Time based Units vest at the end of the three year period ending on June 29, 2008. Forfeited units that do meet the vesting conditions and accumulated distributions thereon accrue back to ACE.

9. SEGMENT INFORMATION

The Corporation has four reportable segments: Transportation Services, Aeroplan, Jazz, and ACTS. The accounting policies for each of these segments are the same as those disclosed in Note 2 to the 2005 annual consolidated financial statements of ACE, with the exception of the policy on stock-based compensation for employees eligible to retire before the vesting period which is described in Note 1 to these interim financial statements. Segment financial information has been prepared consistent with how financial information is produced internally for the purposes of making operating decisions. Segments negotiate transactions between each other as if they were unrelated parties. A reconciliation of the total amounts reported by each segment to the applicable amounts in the consolidated financial statements follows:

	Three months ended June 30, 2006					
	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
Passenger revenue	$ 2,288	$ -	$ -	$ -	$ -	$ 2,288
Cargo revenue	152	-	-	-	-	152
Other revenue	4	181	2	55	-	242
External revenue	2,444	181	2	55	-	2,682
Inter-segment revenue	31	2	338	171	(542)	-
Total revenue	**2,475**	**183**	**340**	**226**	**(542)**	**2,682**
Aircraft rent	82	-	33	-	(2)	113
Depr, amortization and obsolescence	122	4	7	7	-	140
Other operating expenses	2,158	148	264	218	(540)	2,248
Total operating expenses	**2,362**	**152**	**304**	**225**	**(542)**	**2,501**
Operating income	**113**	**31**	**36**	**1**	**-**	**181**
Non-operating (a)	59	1	-	(5)	-	55
Segment results	**$ 172**	**$ 32**	**$ 36**	**$ (4)**	**$ -**	**$ 236**

	Three months ended June 30, 2005					
	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
Passenger revenue	$ 2,100	$ -	$ -	$ -	$ -	$ 2,100
Cargo revenue	147	-	-	-	-	147
Other revenue	6	155	3	47	-	211
External revenue	2,253	155	3	47	-	2,458
Inter-segment revenue	52	2	228	142	(424)	-
Total revenue	**2,305**	**157**	**231**	**189**	**(424)**	**2,458**
Aircraft rent	85	-	15	-	(2)	98
Depr, amortization & obsolescence	104	2	5	8	-	119
Other operating expenses	2,010	130	184	161	(422)	2,063
Total operating expenses	**2,199**	**132**	**204**	**169**	**(424)**	**2,280**
Operating income	**106**	**25**	**27**	**20**	**-**	**178**
Non-operating (a)	(2)	-	(3)	(4)	-	(9)
Segment results	**$ 104**	**$ 25**	**$ 24**	**$ 16**	**$ -**	**$ 169**

	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
	Six months ended June 30, 2006					
Passenger revenue	$ 4,309	$ -	$ -	$ -	$ -	$ 4,309
Cargo revenue	303	-	-	-	-	303
Other revenue	71	378	4	101	-	554
External revenue	4,683	378	4	101	-	5,166
Inter-segment revenue	84	5	656	325	(1,070)	-
Total revenue	**4,767**	**383**	**660**	**426**	**(1,070)**	**5,166**
Aircraft rent	165	-	65	-	(4)	226
Depr, amortization and obsolescence	240	8	11	15	-	274
Other operating expenses	4,367	305	512	429	(1,066)	4,547
Total operating expenses	**4,772**	**313**	**588**	**444**	**(1,070)**	**5,047**
Operating income	**(5)**	**70**	**72**	**(18)**	**-**	**119**
Non-operating (a)	246	1	(3)	(9)	-	235
Segment results	**$ 241**	**$ 71**	**$ 69**	**$ (27)**	**$ -**	**$ 354**

	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
	Six months ended June 30, 2005					
Passenger revenue	$ 3,839	$ -	$ -	$ -	$ -	$ 3,839
Cargo revenue	282	-	-	-	-	282
Other revenue	98	325	5	86	-	514
External revenue	4,219	325	5	86	-	4,635
Inter-segment revenue	101	5	440	278	(824)	-
Total revenue	**4,320**	**330**	**445**	**364**	**(824)**	**4,635**
Aircraft rent	161	-	30	-	(3)	188
Depr, amortization and obsolescence	210	3	10	16	-	239
Other operating expenses	3,929	276	348	308	(821)	4,040
Total operating expenses	**4,300**	**279**	**388**	**324**	**(824)**	**4,467**
Operating income	**20**	**51**	**57**	**40**	**-**	**168**
Non-operating (a)	(62)	-	(7)	(7)	-	(76)
Segment results	**$ (42)**	**$ 51**	**$ 50**	**$ 33**	**$ -**	**$ 92**

Depreciation, amortization and obsolescence included amortization expense related to intangible assets of $23 ($46 for the six months ended June 30, 2006; $24 for the three months ended June 30, 2005 and $50 for the six months ended June 30, 2005).

(a) Non-operating refers to the combination of Non-operating income (expense), Non-controlling interest, Foreign exchange gain (loss), and Provision for income taxes.

Geographic Information

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
Passenger revenue				
Canada	**$ 969**	**$ 916**	**$ 1,755**	**$ 1,593**
US Transborder	**474**	**399**	**948**	**778**
Atlantic	**479**	**437**	**818**	**730**
Pacific	**228**	**224**	**426**	**413**
Other	**138**	**124**	**362**	**325**
Total passenger revenue	**$ 2,288**	**$ 2,100**	**$ 4,309**	**$ 3,839**

Passenger revenues for Canada are based on the actual flown revenue for flights with an origin and destination in Canada. Passenger revenues for US Transborder and other international destinations are based on the actual flown revenue for flights with an origin or destination outside of Canada.

Balance Sheet Information

	As at June 30, 2006					
	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
Cash resources (b)	**2,214**	**498**	**110**	**-**	**-**	**2,822**
Total assets	**11,648**	**734**	**457**	**428**	**(793)**	**12,474**

	As at December 31, 2005					
	Transportation Services	Aeroplan	Jazz	ACTS	Inter-segment Elimination	Consolidated Total
Cash resources (b)	1,682	465	34	-	-	2,181
Total assets	11,001	674	504	381	(713)	11,847

(b) Cash resources refer to Cash and cash equivalents, and Short-term investments.

10. RECONCILIATION OF CANADIAN GAAP TO UNITED STATES GAAP

The consolidated financial statements of the Corporation have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"), which differ in certain respects from accounting principles generally accepted in the United States ("US GAAP"). The following table represents the significant reconciling items between US GAAP and Canadian GAAP. For a complete discussion of US and Canadian GAAP differences, refer to Note 23 to the 2005 annual consolidated financial statements of ACE and Sub-Note 3 below.

(Canadian dollars – millions except per share data)

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
Income for the period in accordance with Canadian GAAP	**$ 236**	$ 169	**$ 354**	$ 92
Convertible securities	**15**	(24)	**53**	(42)
Derivative instruments	**44**	-	**86**	-
Jazz dilution gain reduction (1)	**-**	-	**(41)**	-
Interest expense (2)	-	-	**4**	-
Stock-based compensation (3)	**(3)**	(1)	**(3)**	(1)
Aircraft lease expense (4)	**(1)**	-	**(1)**	-
Aeroplan dilution gain reduction (5)	**-**	(82)	**-**	(82)
Amortization of intangible assets	**(2)**	(1)	**(4)**	(1)
Income adjustments for the period before the following	**53**	(108)	**94**	(126)
Income tax adjustment	**(12)**	21	**(20)**	20
Respective period income adjustments	**41**	(87)	**74**	(106)
Income for the period in accordance with US GAAP	**$ 277**	$ 82	**$ 428**	$ (14)
Minimum pension liability adjustment (a)	**35**	(335)	**140**	(359)
Available-for-sale securities (a), (6)	**(66)**	-	**(52)**	-
Comprehensive income (loss) for the period in accordance with US GAAP	**$ 246**	$ (253)	**$ 516**	$ (373)
Earnings (loss) per share - US GAAP (7)				
- Basic	**$ 2.68**	$ 0.78	**$ 4.11**	$ (0.22)
- Diluted	**$ 2.35**	$ 0.74	**$ 3.65**	$ (0.22)

(a) All items in Other Comprehensive Income are shown net of tax.

		At June 30, 2006		At December 31, 2005
Deferred charges				
Balance under Canadian GAAP	$	126	$	145
Deferred finance charges (4)		(4)		(2)
Balance under US GAAP	$	122	$	143
Goodwill				
Balance under Canadian GAAP	$	-	$	-
Goodwill (1,2)		1,174		1,452
Balance under US GAAP	$	1,174	$	1,452
Intangible assets				
Balance under Canadian GAAP	$	2,267	$	2,462
Convertible preferred shares (2)		4		
Goodwill		307		146
Balance under US GAAP	$	2,578	$	2,608
Other assets				
Balance under Canadian GAAP	$	306	$	392
Derivative instruments		75		(11)
Available-for-sale securities (6)		68		130
Balance under US GAAP	$	449	$	511
Long-term debt and capital leases				
Balance under Canadian GAAP	$	3,584	$	3,543
Convertible securities		20		22
Balance under US GAAP	$	3,604	$	3,565
Convertible preferred shares				
Balance under Canadian GAAP	$	157	$	148
Reclassification of preferred shares		(157)		(148)
Balance under US GAAP	$	-	$	-
Pension and other benefit liabilities				
Balance under Canadian GAAP	$	2,062	$	2,154
Minimum pension liability adjustment		35		246
Balance under US GAAP	$	2,097	$	2,400
Future income taxes				
Balance under Canadian GAAP	$	187	$	221
Goodwill		37		22
Balance under US GAAP	$	224	$	243
Other long-term liabilities				
Balance under Canadian GAAP	$	422	$	446
Convertible preferred shares - embedded derivative		128		165
Convertible notes - embedded derivative		58		64
Balance under US GAAP	$	608	$	675
Temporary equity				
Balance under Canadian GAAP	$	-	$	-
Reclassification of convertible preferred shares		191		182
Balance under US GAAP	$	191	$	182

	At June 30, 2006	At December 31, 2005
Shareholders' equity		
Share capital and other equity		
Balance under Canadian GAAP	**$ 691**	$ 747
Reclassification of convertible preferred shares and convertible notes	**(209)**	(209)
Future income tax (2)	**(6)**	-
Goodwill recorded at fresh-start	**1,596**	1,596
Balance under US GAAP	**$ 2,072**	$ 2,134
Contributed Surplus		
Balance under Canadian GAAP	**$ 23**	$ 19
Stock-based compensation (3)	**(10)**	(13)
Balance under US GAAP	**$ 13**	$ 6
Retained Earnings		
Balance under Canadian GAAP	**$ 756**	$ 402
Convertible securities	**(9)**	(17)
Current year income adjustments	**74**	(51)
Cumulative prior year adjustments:		
Stock-based compensation (3)	**13**	16
Future income tax	**17**	(2)
Goodwill	**(94)**	-
Intangible asset amortization	**(3)**	-
Deriviative instruments	**(11)**	-
Convertible securities	**(78)**	(102)
Balance under US GAAP	**$ 665**	$ 246
Accumulated Other Comprehensive Income		
Balance under Canadian GAAP	**$ -**	$ -
Current year adjustments to comprehensive income:		
Minimum pension liability adjustment	**140**	(162)
Available-for-sale securities	**(52)**	108
Cumulative prior year adjustments to comprehensive income:		
Minimum pension liability adjustment	**(164)**	(2)
Available-for-sale securities	**108**	-
Balance under US GAAP	**$ 32**	$ (56)
Balance under US GAAP	**$ 2,782**	$ 2,330

1. Jazz dilution gain adjustment

As described in Note 7, under Canadian GAAP, ACE has recorded a dilution gain of $220 as a result of the dilution of its interest in Jazz. Under US GAAP, the dilution gain is reduced by $41 due to the impact of the disposal of goodwill.

2. Special distribution of Aeroplan units

Under Canadian GAAP, as described in Note 8, ACE's Board of Directors declared a special distribution of units of the Aeroplan Income Fund to ACE's shareholders. The special distribution to Class A and Class B shareholders is a non-monetary non-reciprocal transfer to owners, which is recorded at the carrying amount of the net assets transferred and does not give rise to a gain or loss. As Aeroplan LP is in a deficit position, in these consolidated financial statements, no amounts have been reflected for this element of the distribution, other than accounting entries relating to future income taxes described below.

Under Canadian GAAP, the special distribution to preferred shareholders of ACE is considered a non-reciprocal transfer to non-owners since the host instrument is classified as debt for accounting purposes. This results in net interest expense of $4 recorded in Quarter 1 2006 and a reduction to intangible assets of $4. Under US GAAP, the special distribution to preferred shareholders of ACE is considered a non-monetary non-reciprocal transfer to owners since the host instrument is classified as temporary equity for accounting purposes. Consistent with the accounting treatment of the special distribution for Class A and Class B shareholders, a non-monetary non-reciprocal transfer to owners is recorded at the carrying amount of the net assets transferred and does not give rise to a gain or loss. The adjustment under US GAAP is a reduction to net interest expense of $4 in Quarter 1 2006 and an increase to intangible assets of $4.

Under Canadian GAAP, a $65 reduction in future income tax assets was recorded in Quarter 1 2006, consisting of a $59 reduction in Share capital and Intangible assets for the portion related to the distribution to the Class A and Class B shareholders and $6 future income tax expense and reduction to Intangible assets for the portion related to the distribution to preferred shareholders. Under US GAAP, the $65 reduction in future income tax assets results in a $65 reduction of Share capital and Goodwill. The adjustment for US GAAP is a $65 increase in Intangible assets, a $65 decrease in Goodwill; a $6 decrease in future income tax expense and a $6 decrease in Share capital.

3. Stock-based compensation

Under Canadian GAAP, as described in Note 1, the Corporation has adopted EIC-162 in the period ended June 30, 2006 with restatement of prior periods. EIC-162 requires that the compensation cost for a stock option award attributable to an employee who is eligible to retire at the grant date be recognized on the grant date or for an employee who will become eligible to retire during the vesting period be recognized over the period from the grant date to the date the employee becomes eligible to retire (the "non-substantive vesting period approach").

Under US GAAP, the Corporation adopted Statement of Financial Accounting Standards ("FAS") No. 123 (revised 2004), "Share-Based Payment" ("FAS 123R") on January 1, 2006, which has the same requirements as EIC-162 under Canadian GAAP except FAS 123R is to be applied prospectively from January 1, 2006 to new option awards that have retirement eligibility provisions. The nominal vesting period approach is continued for any option awards granted prior to adopting FAS 123R and for the remaining portion of unvested outstanding options. Under US GAAP, the adjustment reflects the reversal of the charge to retained earnings of $16 as at January 1, 2005 ($13 as at January 1, 2006) an increase to Salaries, wage and benefits expense of $1 for the period ended June 30, 2005 and an increase of Salaries, wage and benefits expense of $3 for the period ended June 30, 2006, all with an offset to contributed surplus.

Under US GAAP, the impact of applying the non-substantive vesting period approach for awards granted after January 1, 2006 compared to the nominal vesting period approach is an increase to Salaries, wage and benefits expense of $3 for the three month period ended June 30, 2006 ($3 for the six month period ended June 30, 2006). The Salaries, wage and benefits expense for the six month period ended June 30, 2005 would decrease by $1 had the non-substantive vesting period approach been applied retroactively.

4. Aircraft leases

Under Canadian GAAP, when a lease is extended and the payment terms are modified, the lessee should continue to account for the lease in accordance with the terms of the original lease contract until the original lease term expires. The difference between the modified payment and the payment under the terms of the original lease is deferred. Under US GAAP, any straight-line rent accruals and other deferred amounts should be amortized over the combined period of the remaining original lease term and the new lease term. Under US GAAP, additional aircraft lease expense of $1 has been recorded with the offset to deferred charges.

5. Aeroplan dilution gain adjustment

During the course of preparing the annual 2005 consolidated financial statements, it was noted that the Aeroplan gain calculation, as reported in the three month period ended June 30, 2005, did not take into account the goodwill that is allocated to Aeroplan. As a result the dilution gain for US GAAP purposes, previously reported at $190 less tax of $28, has been decreased by $60 to $108 less tax of $6.

As a result of this adjustment the interim periods in 2005 have been adjusted. The income for the three month period ended June 30, 2005, previously reported at $142, has been restated to $82. The income for the six month period ended June 30, 2005, previously reported at $46, has been restated to a loss of $14. This adjustment does not impact the amounts reported under Canadian GAAP.

6. Available-for-sale securities

Under Canadian GAAP, portfolio investments are accounted for using the cost method. Under US GAAP, portfolio investments classified as available-for-sale securities are carried at market value with unrealized gains or losses reflected as a separate component of shareholders' equity and included in comprehensive income. Under US GAAP, an unrealized gain of $16 less tax of $3 ($33 less tax of $6 for the six month period ended

June 30, 2006) has been recorded as a separate component of shareholders' equity and included in other comprehensive income, to reflect the fair value of the remaining US Airways investment of $99 ($217 at December 31, 2005). This adjustment is offset by a decrease of $95 less tax of $16, as the gain for the disposal of 3.25 million shares in Quarter 2 2006 is realized under Canadian GAAP.

7. Earnings per share

	Three months ended June 30		Six months ended June 30	
	2006	2005	**2006**	2005
Numerator				
Numerator for basic earnings per share:				
Income (loss)	**$ 277**	$ 82	**$ 428**	$ (14)
Accretion of convertible preference shares	**(4)**	(4)	**(9)**	(7)
Adjusted numerator for income (loss) per share	**273**	78	**419**	(21)
Effect of potential dilutive securities:				
Convertible preferred shares	**4**	4	**9**	7
Convertible notes	**6**	5	**12**	5
Add back anti-dilutive impact	**-**	(5)	**-**	(12)
Adjusted income (loss) for diluted earnings per share	**283**	82	**440**	(21)
Denominator				
Denominator for basic earnings per share:				
Weighted-average shares	**102**	101	**102**	95
Effect of potential dilutive securities:				
Convertible preferred shares	**10**	9	**10**	9
Convertible notes	**7**	6	**7**	3
Stock options	**1**	1	**1**	1
Add back anti-dilutive impact	**-**	(6)	**-**	(14)
Denominator for diluted earnings per share:				
Adjusted weighted-average shares	**120**	111	**120**	95
Basic earnings (loss) per share	**$ 2.68**	$ 0.78	**$ 4.11**	$ (0.22)
Diluted earnings (loss) per share	**$ 2.35**	$ 0.74	**$ 3.65**	$ (0.22)

The calculation of earnings per share is based on whole dollars and not on rounded millions. As a result, the above amounts may not be recalculated to the per share amount disclosed above.

8. Pension and other benefit plans

The components of US GAAP net periodic cost of defined benefit plans include the following:

	Three months ended June 30			
	Pension Benefits		Other Benefits	
	2006	2005	**2006**	2005
Service cost	**$ 64**	$ 56	**$ 19**	$ 14
Interest cost	**160**	165	**12**	13
Expected return on plan assets	**(184)**	(174)	**-**	-
Amortization of prior service cost	**-**	-	**-**	-
Amortization of net transition obligation	**-**	-	**-**	-
Amortization of experience (gains) losses	**4**	-	**(4)**	(1)
Total	**$ 44**	$ 47	**$ 27**	$ 26

	Six months ended June 30			
	Pension Benefits		Other Benefits	
	2006	2005	**2006**	2005
Service cost	**$ 128**	$ 99	**$ 40**	$ 42
Interest cost	**320**	326	**24**	25
Expected return on plan assets	**(369)**	(347)	**-**	-
Amortization of prior service cost	**-**	-	**-**	-
Amortization of net transition obligation	**-**	-	**-**	-
Amortization of experience (gains) losses	**9**	-	**(9)**	(2)
Total	**$ 88**	$ 78	**$ 55**	$ 65

As of June 30, 2006 the Corporation had contributed $178 to its defined benefit pension plans. The Corporation expects to contribute an additional $253 during the remainder of 2006.

9. New accounting policies

Guidance on application of Variable Interest Entity standard

In April 2006, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) No. FIN 46(R)-6, “Determining the Variability to Be Considered in Applying FASB Interpretation No. 46(R)”, which provides additional clarification on how to determine the variability to be considered in applying FASB Interpretation No.46 (revised December 2003), “Consolidation of Variable Interest Entities.” FSP FIN46(R)-6 is effective prospectively beginning the first day of the first reporting period beginning after June 15, 2006. The Corporation will adopt this standard as of Quarter 3 2006 and is currently assessing the impact of adopting this statement on the consolidated financial position and results of operations.

Accounting for certain hybrid financial instruments

In February 2006, the FASB issued FASB Statement 155, “Accounting for Certain Hybrid Financial Instruments – an amendment of FASB Statement No. 133 and 140” (FAS155), which permits fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, with changes in fair value recognized in earnings. The fair-value election will eliminate the need to separately recognize certain derivatives embedded in hybrid financial instruments under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities. FAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity’s first fiscal year that begins after September 15, 2006. The Corporation will adopt this standard as of Quarter 1 2007 and is in the process of assessing the impact of adopting this standard on the consolidated financial position and results of operations.

Accounting for uncertainty in income taxes

In June 2006, the FASB issued FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109” (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB Statement No. 109, “Accounting for Income Taxes.” The interpretation prescribes a recognition threshold and measurement attribute for the financial statement accounting guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Corporation will adopt this standard as of Quarter 1 2007 and is in the process of assessing the impact of adopting this standard on the consolidated financial position and results of operations.

11. FINANCIAL INSTRUMENTS

Fuel Price Risk Management

The Corporation enters into contracts with financial intermediaries to manage its exposure to jet fuel price volatility. During Quarter 2 2006, the Corporation entered into two three-way collar option structures that have two call strike prices within each option, which puts a ceiling on the potential benefit to be realized by the Corporation if commodity prices increase above the threshold of the second call strike price. Due to the ceiling in these derivative instruments, this type of derivative does not qualify as a hedging instrument under GAAP. As at June 30, 2006, the fair value of these derivative instruments was $1 and is recorded in Investments and other assets on the consolidated statement of financial position. The Corporation recognized a net gain of $1 in non-operating expense.

Interest Rate Risk Management

Air Canada

Air Canada enters into interest rate swaps to manage the risks associated with interest rate movement on US and Canadian floating rate debt and investments. During Quarter 2 2006, Air Canada entered into 19 interest rate swaps with a nominal value of US$414 to receive floating rates and pay a weighted average fixed rate of 5.81% for the debt to be arranged in relation to the financing of Embraer 190 aircraft between June 2006 and November 2007. The swaps have 15 year terms from the expected delivery date of the aircraft and their maturities range from June 2021 to December 2022. The Corporation did not apply hedge accounting to these derivative instruments.

Before June 30, 2006, one of these swaps was settled at a nominal value. As at June 30, 2006, the fair value of the remaining 18 swaps was $2 and is recorded in Other long-term liabilities on the consolidated statement of financial position. The Corporation recognized a net loss of $2 in non-operating expense.

Jazz

During Quarter 1 2006, Jazz entered into interest rate swaps to hedge its exposure to changes in interest rates (Note 3). Effective February 2, 2006, the Corporation is applying hedge accounting to these financial instruments and no amount is recorded in these financial statements. As at June 30, 2006, the fair value of these swaps was $1 in favour of the Corporation.

12. CONTINGENCIES

U.S. DoJ Cargo Investigation

The European Commission, the United States Department of Justice (the "U.S. DoJ") and the Competition Commission in Canada, among other competition authorities, are investigating alleged anti-competitive Cargo pricing activities, including certain fuel surcharges levied by a number of airlines and other Cargo operators. The U.S. DoJ has recently sought information from Air Canada as part of its investigation. Air Canada is cooperating fully with this investigation.

In addition, Air Canada is named as a defendant in a number of class action lawsuits that have been filed before the United States District Court and in Canada in connection with these allegations. It is not possible to predict, with any degree of certainty, the outcome of these actions. Air Canada intends to defend these law suits vigorously.

It is Air Canada's policy to conduct its business in full compliance with all applicable laws, including competition laws.

WestJet

In the 2005 annual consolidated financial statements, the Corporation disclosed a potential contingency related to claims and counterclaims between Air Canada and WestJet Airlines Limited.

During Quarter 2 2006 and as further discussed in a joint press release dated May 29, 2006, a resolution was reached by which WestJet, among other things, has agreed to pay Air Canada's investigation and litigation costs of $5.5, which has been recorded as a recovery of Other operating expenses during Q2 2006. Air Canada has withdrawn its claims in light of this settlement. All legal proceedings between the parties have been terminated.

13. SUBSEQUENT EVENT - STRATEGIC INITIATIVES

On August 11, 2006, the Board of Directors of ACE announced the following strategic initiatives, market conditions permitting, to create further value for ACE shareholders:

- Launching of an initial public offering (IPO) of a minority stake in Air Canada in late 2006;
- Commencing a process in late 2006 to monetize ACTS; and
- Pursuing opportunities that realize the value of its investment in Aeroplan and Jazz.

In connection with these plans, ACE intends, subject to shareholder and Court approval under the Canada Business Corporations Act, to enter into a plan of arrangement. The plan would provide the Board of ACE with the authority to reduce the capital of the Corporation up to an aggregate amount of approximately $2 billion over time, but without any maximum time limit. A special meeting of shareholders will be convened in October 2006 to review the proposed plan of arrangement.