ACE Aviation Holdings Inc.

ANNUAL

INFORMATION

FORM

March 28, 2006

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Glossary

Aeroplan — Means Aeroplan Limited Partnership and its predecessor entities;

Aeroplan Miles — Means the currency accumulated by Aeroplan members under the Aeroplan Program;

Aeroplan Program — Means the loyalty marketing program operated by Aeroplan;

Available Seat Miles or ASMs — A measure of passenger capacity calculated by multiplying the total number of seats available for passengers by the miles flown;

Cargo Services — Means the business and operations of the Corporation's air cargo services, including cargo related products, services and ground operations, carried on, for domestic and transborder cargo services, by AC Cargo LP and for international cargo services by Air Canada;

Code-share or Code-sharing — Refers to a commercial agreement between airlines where an air carrier sells air transportation under its own designator code and the actual transportation is provided by the other air carrier;

GAAP — Means generally accepted accounting principles in Canada;

Ground Handling Services — Means the business and operations of the Corporation carried on by ACGHS LP (and its United States subsidiary, ACGHS US Inc.) and Air Canada that provide passenger and aircraft related ground handling services, including check-in, gate management, baggage and cargo handling and ramp services;

Passenger Load Factor — A measure of passenger capacity utilization derived by expressing Revenue Passenger Miles as a percentage of Available Seat Miles;

Jazz – Means for the period up to September 30, 2004, Jazz Air Inc., for the period from September 30, 2004 to February 1, 2006, Jazz Air Limited Partnership, and on or after February 2, 2006, Jazz Air LP;

Passenger Revenue per Available Seat Mile or RASM — Means the average passenger revenue per Available Seat Mile;

Revenue Passenger Miles or RPMs — A measure of passenger traffic calculated by multiplying the total number of revenue passengers carried by the miles they are carried;

Technical Services — Means the heavy maintenance, engine maintenance, component maintenance, engineering and training business and operations carried on by ACTS Limited Partnership; and

Yield — Means average passenger revenue per Revenue Passenger Mile.

Explanatory Notes

The information in this Annual Information Form is stated as at December 31, 2005, unless otherwise indicated.

ACE Aviation Holdings Inc. and the Corporation — References herein to ACE are references to ACE Aviation Holdings Inc. itself and references to the "Corporation" include references, 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.

Currency — All currency amounts used in this document are stated in Canadian dollars, unless otherwise indicated.

Statistical Information — Market data and certain industry forecasts used throughout this Annual Information Form were obtained from internal surveys, market research, publicly available information and industry publications. Industry publications generally state that the information contained therein has been obtained from sources believed to be reliable, but that the accuracy and completeness of such information is not guaranteed. Similarly, internal

surveys industry forecasts and market research, while believed to be reliable, have not been independently verified, and the Corporation does not make any representation as to the accuracy of such information.

Subsidiaries – References to the term "subsidiary" or "subsidiaries" refers, in relation to any entity, to any other entity, including a corporation or a limited partnership, which is controlled, directly or indirectly, by that entity.

Forward-looking statements — ACE's communications often contain written or oral forward-looking statements which are included in this Annual Information Form and may be included in filings with securities regulators in Canada and the United States. These forward-looking statements are identified by the use of terms and phrases such as "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "would", and similar terms and phrases, including references to assumptions. Such statements may involve but are not limited to comments with respect to strategies, expectations, planned operations or future actions. Forward-looking statements, by their nature, are based on assumptions and are subject to important risks and uncertainties. Any forecasts or forward-looking predictions or statements cannot be relied upon due to, among other things, changing external events and general uncertainties of the business. Results indicated in forward-looking statements may differ materially from actual results for a number of reasons, including without limitation, energy prices, general industry, market and economic conditions, war, terrorist attacks, changes in demand due to the seasonal nature of the business, the ability to reduce operating costs and employee counts, employee relations, labour negotiations or disputes, restructuring, pension issues, currency exchange and interest rates, changes in laws, adverse regulatory developments or proceedings, pending litigation and actions by third parties as well as the factors identified throughout this Annual Information Form and, in particular, those referred to under "Risk Factors". The forward-looking statements contained in this Annual Information Form represent ACE's expectations as of the date of this Annual Information Form, and are subject to change after such date. However, ACE disclaims any intention or obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise.

THE CORPORATION

Incorporation

ACE was incorporated on June 29, 2004 under the *Canada Business Corporations Act* ("CBCA") and became the parent holding company of the reorganized Air Canada and its subsidiaries upon the implementation of the consolidated plan of reorganization, compromise and arrangement of Air Canada and certain of its subsidiaries under the CBCA, the *Companies' Creditors Arrangement Act* ("CCAA") and the *Business Corporations Act* (Alberta) which was implemented on September 30, 2004 (referred to herein as the "Plan").

On September 30, 2004, as part of the implementation of the Plan, Air Canada reorganized its corporate structure. Pursuant to such corporate reorganization, APLN Limited Partnership (the predecessor to Aeroplan Limited Partnership), Jazz Air Inc. (the predecessor to Jazz Air Limited Partnership and Jazz Air LP), Touram Inc. (the predecessor to Touram Limited Partnership ("Touram LP")) and Destina.ca Inc. (a predecessor to Destina eCommerce Group LP), which were already established as stand-alone entities under Air Canada, became stand-alone entities under ACE, while ACTS Limited Partnership ("ACTS LP"), AC Cargo Limited Partnership ("AC Cargo LP"), AC Online Limited Partnership (a predecessor to Destina eCommerce Group LP) and ACGHS Limited Partnership ("ACGHS LP") were established as stand-alone limited partnerships under ACE. As a result, ACE operates as a parent holding company of Air Canada, Aeroplan, Jazz, ACTS LP, AC Cargo LP, Destina eCommerce Group LP, ACGHS LP and Touram LP. Prior to 2002, Aeroplan's operations were integrated with those of Air Canada. In 2001, management of Air Canada developed a formal plan to create a separate entity to carry on the operations of the Aeroplan Program. Effective January 1, 2002, Aeroplan has been operated as a separate entity under Air Canada. Jazz Air Inc. had been a stand alone entity under Air Canada and on September 30, 2004 transferred substantially all of its assets and certain of its liabilities to the newly created Jazz Air Limited Partnership, a stand alone limited partnership under ACE. Destina.ca Inc. had been a stand alone entity under Air Canada and on July 31, 2005 transferred substantially all of its assets and certain of its liabilities to Destina eCommerce Group LP, a stand alone limited partnership under ACE. ACE's new corporate structure is designed to facilitate the development of each business unit to its fullest individual potential including, where appropriate, through the pursuit of third party sources of business, and to maximize the value of the subsidiaries.

On June 29, 2005, Aeroplan Income Fund completed its initial public offering of 25 million units at a price of $10 per unit. On June 30, 2005, following the exercise of the over-allotment option by the underwriters, Aeroplan Income Fund issued an additional 3.75 million units at a price of $10. On February 16, 2006, ACE announced a special distribution to its shareholders of units of Aeroplan Income Fund. The distribution of 0.18 units of Aeroplan Income Fund per Variable Voting Share, Voting Share and Preferred Share (on an as converted basis) of ACE is being 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 and the payment date is expected to be on or about March 31, 2006. Following the special distribution, ACE holds a 75.5% ownership interest in Aeroplan Limited Partnership.

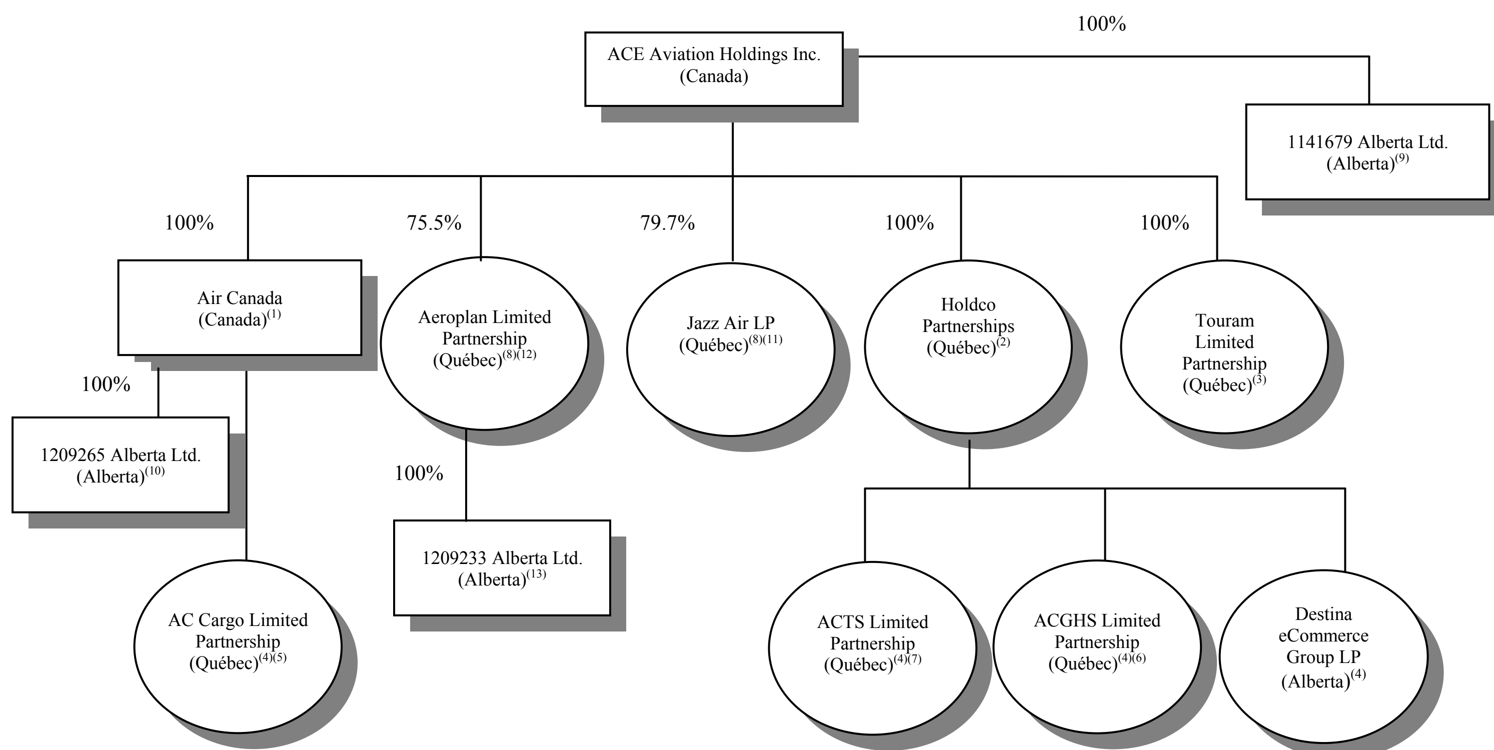
On February 2, 2006, Jazz Air Income Fund completed its initial public offering of 23.5 million units at a price of $10 per unit. On February 27, 2006, Jazz Air Income Fund announced that it had issued an additional 1.5 million units pursuant to the partial exercise of the over-allotment option granted to the underwriters in conjunction with Jazz Air Income Fund's initial public offering at a price of $10 per unit. With the partial exercise of the over-allotment option, ACE currently holds a 79.7% interest in Jazz Air LP.

The Variable Voting Shares and the Voting Shares of ACE are listed on the Toronto Stock Exchange ("TSX"), under the symbols "ACE.RV" and "ACE.B", respectively.

The head office of ACE is located at 5100 de Maisonneuve Boulevard West, Montreal, Québec, H4A 3T2.

Corporate Structure

The following table lists the current ACE principal subsidiaries, including their jurisdictions of constitution and the percentage of equity held or controlled directly or indirectly by ACE:



(1) Air Canada holds all of the issued and outstanding shares of certain subsidiaries, including Air Canada Capital Ltd., which is incorporated under the laws of the Province of Alberta.
(2) The Holdco Partnerships, which are limited partnerships governed by the laws of the Province of Québec, are the limited partners of, and hold 99.99999% of the units in ACGHS LP, ACTS LP and Destina eCommerce Group LP (a successor to AC Online LP). ACE is the limited partner of each Holdco Partnership and holds 99.9% of the limited partner common units of each Holdco Partnership. Wholly-owned subsidiaries of ACE incorporated under the laws of Canada, are the general partners of, and hold 0.1% of the units in, their respective Holdco Partnership. Air Canada holds all of the limited partner preferred units in each Holdco Partnership.
(3) Touram LP provides tour operator services and leisure vacation packages under the trade name Air Canada Vacations and sells surplus seat inventory to travel agents under the trade name Netair. On January 31, 2005, Touram Inc. transferred all of its assets and certain of its liabilities to Touram LP, a limited partnership governed by the laws of the Province of Québec. Prior to its winding-up into ACE on December 29, 2005, Touram Inc., a corporation incorporated under the laws of Canada, was the limited partner of, and held 99.99999% of the units in, Touram LP. Following the winding-up, ACE holds all of the units in Touram LP previously held by Touram Inc. Touram General Partner Inc., a wholly-owned subsidiary of ACE incorporated under the laws of Canada, is the general partner of, and holds 0.00001% of the units in, Touram LP.
(4) The general partners of AC Cargo LP, ACGHS LP, ACTS LP and Destina eCommerce Group LP are wholly-owned subsidiaries of ACE incorporated under the laws of Canada. Such general partners hold 0.00001% of the units in AC Cargo LP, ACGHS LP, ACTS LP and Destina eCommerce Group LP.
(5) AC Cargo LP, together with Air Canada, provides Cargo Services on domestic, transborder and international flights. Air Canada is the limited partner of, and holds 99.99999% of the units in, AC Cargo LP.
(6) ACGHS LP provides passenger and aircraft related ground handling services to Air Canada, Jazz and other airlines with a primary focus on Canadian stations.
(7) ACTS LP provides Technical Services and competes on a global basis as an aircraft maintenance, repair and overhaul service provider.
(8) Following the initial public offering of Aeroplan Income Fund and Jazz Air Income Fund, ACE holds an interest in the general partners of each of Aeroplan and Jazz which is proportional to its interest in their respective partnerships.
(9) 1141679 Alberta Ltd. holds and manages excess cash and investments of ACE on its behalf.
(10) 1209265 Alberta Ltd. holds and manages excess cash and investments of Air Canada on its behalf.
(11) ACE holds a 79.7% ownership interest in Jazz.
(12) ACE holds a 75.5% ownership interest in Aeroplan.
(13) 1209233 Alberta Ltd. holds and manages the investment of a majority of the Aeroplan miles redemption reserve on behalf of Aeroplan.

Certain subsidiaries, each of which represents not more than 10% of the consolidated assets and not more than 10% of the consolidated sales and operating revenues of the Corporation, and all of which, in the aggregate, represent not more than 20% of the total consolidated assets and the total consolidated sales and operating revenues of the Corporation at December 31, 2005, have been omitted.

REGULATORY ENVIRONMENT

In Canada, commercial air transportation, including policy, maintenance standards, operations standards, safety and ground and navigation facilities, falls wholly within the jurisdiction of the federal government and is the responsibility of the Minister of Transport. The Canadian Transportation Agency is responsible for issuing air carrier licenses for both domestic and international services and regulates international air fares as well as terms and conditions of carriage. Since 1996, NAV Canada, a private company, is responsible for providing air navigation services in Canada. In addition, all major Canadian airports are operated by local airport authorities that are also privatized companies.

Domestic Services

The 1987 deregulation of the domestic airline industry allowed carriers to establish fares as well as terms and conditions of carriage without government regulation. The *Canada Transportation Act* ("CTA") provides for free market entry to the extent that a carrier can demonstrate that (i) it is "Canadian", defined in the CTA as being controlled in fact by Canadians and having at least 75% of its voting interest owned and controlled by Canadians; (ii) it can operate safely; (iii) it is suitably insured; and (iv) it meets the minimum financial requirements set out in the *Air Transportation Regulations* (Canada) adopted pursuant to the CTA.

In July 2000, the Government of Canada amended the CTA, the *Competition Act* (Canada) and the *Air Canada Public Participation Act* (Canada) to address the competitive airline environment in Canada and ensure protection for consumers. This legislation increased the powers of the Canadian Transportation Agency with respect to pricing on non-competitive domestic routes, and domestic terms and conditions of carriage. In addition, this legislation included airline-specific provisions concerning "abuse of dominance" under the *Competition Act* (Canada).

In February 2001, the Competition Bureau released, for consultation, draft guidelines outlining the approach it proposed to take in enforcing the airline-specific "abuse of dominance" provisions of the *Competition Act* (Canada) including the establishment of administrative monetary penalties for a breach of the abuse of dominance provisions by a dominant domestic air carrier. The guidelines describe, among other things, how the Competition Bureau would calculate whether a carrier is operating or increasing capacity at fares that do not cover the avoidable costs of providing the services and uses of commissions, incentives, loyalty programs or corporate discounts that would be regarded as anti-competitive. The guidelines were never finalized in light of the letter issued in 2004 by the Commissioner of Competition described below outlining her approach to enforcement of the airline abuse of dominance provision on a going forward basis.

In March 2001, the Commissioner of Competition brought an application under the "abuse of dominance" provisions of the *Competition Act* (Canada), seeking an order prohibiting Air Canada from charging fares on flights on certain routes in eastern Canada where such fares would not cover the avoidable costs of such flights. By agreement of Air Canada and the Commissioner of Competition, the application was divided into two phases. Phase I involved a review of all of Air Canada's costs from April 2000 to March 2001 and a determination of which of those cost items would be considered avoidable costs. The Competition Tribunal released its reasons and findings regarding Phase I on July 22, 2003, and adopted a broadly crafted avoidable cost test. The decision of the Competition Tribunal does not constitute a determination that Air Canada breached the *Competition Act* (Canada) by abusing its dominant position, which is an issue that would have been determined in Phase II of the application. As described below, Phase II of the application will not proceed as the proceeding was terminated by the Commissioner of Competition with the agreement of Air Canada, for the reasons described below.

In September 2004, following extensive discussion with Air Canada, the Competition Bureau terminated the Competition Tribunal application with the agreement of Air Canada and published a letter describing the enforcement approach to be taken by the Competition Bureau to any new complaint made against a dominant domestic carrier in light of the changes in the airline industry that have occurred since 2000. In addition, on November 2, 2004, the Minister of Industry tabled amendments to the *Competition Act* (Canada) in Bill C-19 which, if enacted, would have removed the airline-specific "abuse of dominance" provisions from the *Competition Act* (Canada). However, on November 29, 2005, the 38th Parliament of Canada was dissolved. As a result, the legislative

process relating to the adoption of Bill C-19 was terminated. Management cannot predict if or when such proposed legislation will be re-introduced in the House of Commons.

In light of these developments, and as part of the agreement to terminate the March 2001 application to the Competition Tribunal, Air Canada determined that it would not appeal the Competition Tribunal's decision in Phase I of the application. The Competition Bureau has expressed its view that the principles established by the Competition Tribunal in Phase I of the application regarding the application of the avoidable cost test would be relevant for any future cases which may arise in similar circumstances.

On April 27, 2004, the Government of Canada amended the *Canadian Computer Reservation Systems (CRS) Regulations* adopted under the *Aeronautics Act* (Canada) to lessen the regulatory requirements and place greater reliance on market forces in the distribution system that will result in market efficiencies and reduced costs for airlines. With the amendments, airlines with at least 10% market share are no longer required to participate in all CRSs operating in Canada and have the freedom to select the levels of participation that best serve their operations. Also, all airlines and CRS vendors are now permitted to freely negotiate fees on strictly commercial terms.

Transborder Services

In February 1995, a new air services agreement (the "1995 Canada-US Air Services Agreement") was implemented between Canada and the United States, replacing the previous bilateral agreement, which had imposed greater restrictions on market access and fares. This agreement gave Canadian air carriers unlimited route rights to provide "own aircraft" services between points in Canada and points in the United States. The carriage of local traffic between points within one country by carriers of the other country, commonly known as cabotage, continued to be prohibited.

Under the 1995 Canada-US Air Services Agreement, rules governing fare levels and the requirement to file tariffs (excluding rules tariffs) with government authorities were eliminated. Carriers of both countries are free to set their own prices for transborder services according to market forces. Prices may only be disallowed under special circumstances if the authorities of both countries agree, for example in response to predatory or monopolistic pricing behaviour on specific routes. In November 1997, Canada and the United States concluded an agreement that allows Canadian and United States carriers to Code-share to, from and via each other's territory, with carriers from other countries provided the other country allows Code-sharing and the carriers hold the underlying rights to serve that country. As a result, Air Canada increased its Code-sharing with certain Star Alliance® partners via Canada and the United States and these Star Alliance® partners' codes appear on some Jazz operated transborder flights.

On November 11, 2005, Transport Canada announced that the governments of Canada and the United States had negotiated an open skies agreement (the "Open Skies Agreement") which further liberalized air transportation services and which is scheduled to come into effect on September 1, 2006. This Open Skies Agreement will allow air carriers of both countries to (i) pick up passenger and/or cargo traffic in the other country and carry that traffic to a third country as part of a service to or from the carrier's home country, (ii) operate stand-alone all-cargo services between the other country's territory and third countries, and (iii) offer the lowest prices for services between the other country and a third country. Cabotage remains prohibited.

International Services

Scheduled international air services are regulated by the Canadian and foreign governments involved. The Minister of Transport has the authority to designate which Canadian air carriers may serve scheduled international routes. International route rights are obtained through bilateral negotiations between Canada and foreign countries. Bilateral agreements provide for the rights which may be exercised over agreed routings and the conditions under which the carriers may operate, including, among others, the number of carriers which may operate, the capacity and/or flight frequencies that may be provided and the controls over tariffs to be charged. Most bilateral agreements to which Canada is a party provide for the designation of more than one Canadian carrier, while some provide for the designation of only one Canadian carrier. In general, bilateral agreements between Canada and European countries are more liberal in terms of controls on capacity and flight frequencies than those between Canada and Asian countries.

In February 2001, the Minister of Transport launched an international air services policy review to address competition in the international market with the objective of liberalizing Canada's policy for scheduled international air services, including how Canada approaches the negotiation and management of air traffic rights with other countries.

In May 2002, the Minister of Transport introduced a liberalized multiple designation policy applicable to scheduled international air services by Canadian carriers (excluding services to the United States). Any Canadian carrier may apply to be designated to serve any foreign country, regardless of the size of the air travel market. If the number of Canadian carriers permitted is restricted under existing bilateral agreements, the Canadian government has indicated that it will pursue negotiations with the appropriate countries to seek the necessary rights for Canadian carriers. In addition, an incumbent carrier's designation in a particular market will be subject to reallocation only in circumstances where the bilateral agreement limits designation and the carrier is not operating its own aircraft or Code-share services.

Charter Services

Charter operations are generally not covered by bilateral agreements, although charter services are covered under the 1995 Canada-US Air Services Agreement. Canadian government policy permits any Canadian carrier to operate charter services between Canada and any point in the world subject to prior approval of the Canadian and other appropriate regulatory authorities. Charter services are operated by Air Canada to provide service to foreign points where it is not the designated airline or to generate additional revenues from aircraft that would otherwise be idle.

In April 2000, the Minister of Transport announced a new policy governing international passenger charter air services. This policy removed restrictions such as advance booking, minimum stay requirements and prohibitions on one way travel. To preserve a distinction between charter and scheduled international services, this policy retains the requirements that the entire seating capacity of an aircraft be chartered and that charter carriers be prohibited from selling seats directly to the public.

Official Languages Act

Air Canada is subject to the *Official Languages Act* (Canada) (the "OLA"). The OLA compels Air Canada to, among other things, ensure that any member of the traveling public can communicate with and obtain services in either official language where there is significant demand for those services in that language (Part IV of the OLA) and to allow employees to work in either official language (Part V of the OLA). In 2000, Parliament passed amendments to the *Air Canada Public Participation Act* (Canada) (the "ACPP") to impose on Air Canada the obligation to ensure any of its subsidiaries' customers can communicate with the subsidiary in respect of air services and incidental services, and obtain those services, in either official language, where the number of customers warrants such services.

In September 2004, as a result of the emergence of Air Canada from protection under the CCAA, several internal divisions and former subsidiaries of Air Canada were spun off into limited partnerships under the direct or indirect control of ACE. While the linguistic obligations stated above continue to apply to Air Canada itself, ACE and the successor entities it owns are not currently subject to official language obligations, except that pursuant to the OLA, where services are performed on behalf of Air Canada by another party, any member of the public can communicate with and obtain those services in either official language in any case where those services, if provided by Air Canada, would be required under the OLA to be provided in either official language.

On May 2, 2005, Bill C-47, An Act to amend the Air Canada Public Participation Act (Canada) (the "Bill C-47") was tabled in the House of Commons. On November 3, 2005, Bill C-47 passed second reading and referred to the Standing Committee on Transport. Bill C-47 sought to amend existing legislation to ensure that Air Canada's successor entities are subject to official language requirements. However, on November 29, 2005, the 38th Parliament of Canada was dissolved. As a result, the legislative process relating to the adoption of Bill C-47 was terminated. Although Management cannot predict if or when such proposed legislation will be re-introduced in the House of Commons, ACE and the relevant successor entities it owns do comply, or have already taken steps toward compliance with, Part IV of the OLA.

Security Initiatives

Following the September 11, 2001 terrorist attacks, the Minister of Transport issued new air security measures, including increased passenger and baggage screening and enhanced security procedures at check-in gates and on-board the aircraft. Other countries such as the United States and the United Kingdom have similarly imposed additional security requirements. The Corporation's priority has been to ensure the safety and security of all passengers and crew members on all flights. In response to these new measures, the Corporation has reinforced the cockpit doors on all of its mainline operating aircraft and has required passengers to produce valid identification prior to boarding all flights. In December 2001, the Minister of Transport announced several security initiatives including a new Canadian Air Transport Security Authority responsible for the provision of key air security services, an expanded program of armed police on aircraft to cover selected domestic and international flights, and an air traveler's security charge. The air traveler's security charge was introduced on April 1, 2002. The charges have been revised in subsequent federal budgets. Since April 1, 2005, the maximum charge is $10 for domestic travel and $17 for transborder and international travel.

In October 2002, the Canadian government implemented its Advance Passenger Information initiative to identify potentially high risk individuals and address other border security issues. In March 2003, it also established a Passenger Name Record program. Canadian and foreign carriers are now required by regulation to provide the Canada Border Services Agency with specific personal information on all passengers and crew members on board international flights destined to Canada at the time of departure, as well as to provide access to passenger name records in the carriers' internal reservation systems. Foreign countries such as the United States, the United Kingdom, Australia, Mexico and South Korea have enacted similar information requirements with respect to flights operating into and/or from their territory.

On May 6, 2004, Bill C-7, an *Act to amend certain Acts of Canada in order to enhance public safety* (known as the *Public Safety Act*, 2002) received royal assent. The legislation amends certain provisions of the *Aeronautics Act* (Canada) so as to further develop the scope and objectives of the existing national aviation security regime. The amendments include requirements for Canadian carriers and foreign carriers operating into Canada to provide, upon request, information concerning specified flights or persons to the Minister of Transport, Royal Canadian Mounted Police and Canadian Security Intelligence Service for transportation security or national security purposes. These amendments came into force on May 11, 2004.

Safety Initiatives

On June 15, 2005, the Minister of Transport announced regulatory amendments to further improve the safety performance of Canadian air operators and increase accountability in the aviation sector through the implementation of safety management systems. The goals of safety management systems are to increase industry accountability, to instill a consistent and positive safety culture, and to help improve the safety performance of air operators. Amendments to the Canadian Aviation Regulations require air operators to implement safety management systems in their organizations and appoint executives who are accountable for safety. These amendments came into force on May 31, 2005. On May 16, 2005, Bill S-33, *An Act to amend the Aeronautics Act and to make consequential amendments to other acts* (Canada) ("Bill S-33") was tabled for first reading in the Senate. Bill S-33 sought, among other things, to address integrated management systems and to authorize the establishment of voluntary reporting programs under which information relating to aviation safety and security may be reported. On June 14, 2005, Bill S-33 was withdrawn. Management cannot predict if or when such proposed legislation will be re-introduced.

Air Canada, Jazz, and ACTS LP are all in the process of implementing their respective safety management systems in accordance with the recent amendments to the Canadian Aviation Regulations. The President and Chief Executive Officer of Air Canada, Montie Brewer has been appointed as the executive currently accountable for Air Canada's safety management system. The President and Chief Executive Officer of Jazz, Joseph D. Randell has been appointed as the executive currently accountable for Jazz's safety management system. The President and Chief Executive Officer of ACTS LP, Chahram Bolouri has been appointed as the executive currently accountable for ACTS LP's safety management system. In addition, the Senior Director Corporate Safety & Environment, ACE is facilitating the implementation of the Air Canada safety management system, the Director of Corporate Safety, Jazz

is facilitating the implementation of the Jazz safety management system, and the Senior Director, Regulatory Compliance, ACTS is facilitating the implementation of the ACTS LP safety management system.

Privacy

The Corporation is subject to Canadian, United States and foreign privacy laws regarding the collection, use, disclosure and protection of passenger and employee data. Among other things, Canada's federal private sector privacy legislation, the *Personal Information Protection and Electronic Documents Act* (Canada) (the "PIPEDA"), governs the collection, use and disclosure of personal information in the course of commercial activities by a federally regulated business. In addition, the PIPEDA regulates the handling of employee personal information by federally regulated employers. The PIPEDA also applies to the collection or disclosure of personal information across provincial or Canadian international borders and within provinces without substantially similar private sector privacy legislation. The PIPEDA requires informed consent by the individuals whose personal information is collected and used. The personal information may then only be used for the purposes for which it was originally collected or for other specific purposes specified in the PIPEDA. The Corporation has a privacy policy which is designed to meet or exceed the requirements of such privacy legislation. Management believes that its privacy policy and practices comply with applicable law in Canada and elsewhere.

In addition to the Corporation's privacy policy, specific privacy measures and policies to protect the information of customers and employees are applied by each subsidiary of the Corporation.

INDUSTRY OVERVIEW AND COMPETITIVE ENVIRONMENT

Airline Transportation Industry

General

The airline industry is highly competitive. Over the past two decades, governments have gradually removed economic regulation of commercial aviation, resulting in a more open and competitive environment for domestic, transborder and international airline services, for both scheduled and leisure charter operations.

Deregulation has transformed the global airline industry and allowed the emergence of low-cost carriers. Following in the footsteps of Southwest Airlines in the United States and easyJet and Ryanair in Europe, the entry in the Canadian market of low-cost carriers marked the beginning of a rapid shift in the domestic competitive environment. With their relatively low unit costs, which result largely from lower labour costs and a simpler product, low-cost carriers are able to operate profitably while offering substantially lower fares. By offering such fares to business passengers in particular, these carriers have succeeded in expanding and taking demand away from the larger, more established carriers, commonly referred to as "legacy carriers".

In response to these changes, many legacy carriers have adopted similar strategies for dealing with competition from low-cost carriers in their respective domestic markets. A common strategy has been to reduce costs and capacity by negotiating substantial labour concessions, rationalizing domestic capacity, and focusing on long-haul premium business routes. These measures enable the legacy carriers to exploit their competitive advantages in the global marketplace while also drawing on a much larger customer base.

The terrorist attacks of September 11, 2001 materially affected the airline industry, and the airport security procedures that were subsequently introduced caused air travel to become comparatively more time consuming and less convenient for passengers. In 2003, the war in Iraq and the outbreak of SARS (which most dramatically affected Asia and Canada), also adversely impacted the airline industry.

In order to realign their business models, many legacy carriers have restructured or are currently restructuring either through court-supervised or consensual processes. The degree of restructuring and the changes being implemented vary from carrier to carrier. The U.S. industry comprises several legacy carriers in a highly fragmented market, characterized by significant overcapacity, deep price discounting and increasing competition

from low-cost carriers (such as Southwest Airlines and JetBlue Airways). The Canadian airline industry is less fragmented than the U.S. airline industry.

Domestic Market

Air Canada is Canada's largest domestic full service airline. Jazz is the largest regional airline in Canada and the second largest airline in Canada after Air Canada based on fleet size and number of routes operated. The Canadian airline industry is characterized by a limited number of high density markets, which account for the majority of passenger traffic and revenue. Domestic low-cost carriers have achieved a material presence in all major domestic markets and they continue to expand. The Corporation has redefined its business strategy in order to compete effectively.

Based on Official Airline Guide ("OAG") data, the Corporation estimates that in March 2006, it will provide approximately 61% of the Canadian airline industry's overall domestic scheduled capacity, as measured by ASMs, while WestJet will provide approximately 29%.

Transborder Market

With the most non-stop destinations and flights to the United States, Air Canada and Jazz carry more passengers between Canada and the United States than any other airline. Competition in the transborder market is primarily from the U.S. legacy carriers, which tend to operate flights between the United States and Canada via their hubs for connecting flights. U.S. legacy carriers with transborder operations include, without limitation, American Airlines, Delta Airlines, Continental Airlines, United Airlines and Northwest Airlines.

Canadian low-cost carriers operate transborder services and are expanding their operations in the transborder market. WestJet currently provides transborder services to Orlando, Tampa, Fort Myers, Fort Lauderdale, Los Angeles, Palm Springs, Phoenix, Las Vegas, Honolulu and Maui. CanJet currently provides transborder services to New York and Orlando, Florida, year-round, and seasonally to other destinations in Florida including, St Petersburg, West Palm Beach, Fort Lauderdale and Sarasota. In addition, a United States low cost carrier, Frontier Airlines, announced that it will begin transborder services between Calgary and Denver towards the end of May, 2006.

Based on OAG data, the Corporation estimates that in March 2006, it will provide approximately 42% of the overall transborder scheduled capacity as measured by ASMs.

International Market

Air Canada has a broad portfolio of international route rights and is Canada's largest scheduled international carrier. In the trans-Atlantic and trans-Pacific markets, Air Canada primarily competes with foreign legacy carriers and, to a lesser extent, with charter and low-cost carriers on higher density routes, primarily during peak travel seasons. U.S. legacy carriers also provide indirect competition by flying Canadian passengers through their hubs to international markets. However, management believes that the U.S. government policy requiring a visa from residents of certain countries for transit through the United States has provided an advantage to Air Canada since there is currently no equivalent requirement that applies to transit through Canada.

The expansion of major airline alliances, such as Star Alliance®, oneworld and SkyTeam has consolidated operations in the trans-Atlantic and trans-Pacific markets. In the trans-Pacific market, the emergence of polar routes has provided opportunities for new non-stop services from eastern North American cities to Asia. Air Canada is pursuing these opportunities by introducing non-stop services from Toronto to Tokyo, Hong Kong, Beijing, Shanghai and Seoul, and one-stop service from Toronto to Delhi. The South American market also represents an area of growth for Air Canada, since no South American carrier currently flies to Canada.

Based on OAG data, the Corporation estimates that in March 2006, it will provide approximately 46% of the overall international scheduled capacity between Canada and Europe and Canada and Asia, as measured by ASMs.

Air Canada is currently the only Canadian scheduled carrier on Asian routes from Canada, although many Asian countries have their own carriers serving Canada.

Regional Airline Industry

The Canadian regional airline industry is composed of Jazz, and a number of other smaller operators of turboprop aircraft, most of which operate aircraft in the 19 to 50 seats range. Other than Jazz, these carriers are primarily stand-alone operations, operating in niche markets. Few other regional airlines in Canada operate under capacity purchase agreements, and those who do have relationships with Air Canada to operate turboprop aircraft with 19 seats or less. All of these carriers, excluding Jazz, are privately held or family-run companies. None of these carriers approach the size and scope of Jazz's operation as their fleets range from one to 12 aircraft.

Jazz is the only regional carrier which offers service in more than one region of the country as well as transborder service. In addition, it is the only regional carrier in Canada operating regional jets.

The Canadian domestic market is characterized by a large geographic territory with a concentration of routes in Western and Eastern Canada around four major hubs, Toronto, Vancouver, Montreal and Calgary. This market is served by Jazz, Air Canada, domestic low-cost carriers such as WestJet and Canjet, and smaller regional airlines.

In the transborder market, Air Canada and Jazz compete against a variety of U.S. network airlines and their regional carriers, the majority of which operate under capacity purchase agreements. These regional carriers operate under their respective capacity purchase agreement partner brands including United Express, America West Express, US Airways Express, Continental Express, Northwest Airlink, Delta Connection, American Eagle and Horizon Airlines.

The Canadian Loyalty Marketing Industry

Loyalty marketing encompasses a wide range of tools and practices designed to give loyal customers collectible incentives which, when converted into rewards, form part of a compelling value proposition to continue purchasing a company's products or services. Loyalty marketing has successfully been used by companies to attract new customers, enable customer retention and increase the purchase levels of targeted consumers. It has become a key element in many companies' marketing mix. Several companies have shifted large portions of their marketing budgets from mass-market advertising to direct marketing generally, and loyalty marketing programs in particular. Strong loyalty management systems allow for the identification and segmentation of customers based on purchasing behaviour. Unlike other traditional marketing practices generally using mass media, loyalty marketing creates a direct link between individuals, their specific demographics and transactional data. Combined with the latest database management tools and technologies, loyalty marketing is one of the most sophisticated and measurable forms of marketing.

There are two main forms of loyalty programs in Canada, coalition programs and proprietary programs. Coalition programs unite many different participating organizations under the same program and currency structure, such as the Aeroplan Program and the Air Miles™ program. Proprietary programs only have a single organization/ currency and generally have a narrower scope of accumulation opportunities, rewards and benefits. Operators of such programs are required to support the full infrastructure cost. In Canada, the vast majority of loyalty programs are proprietary.

According to The Loyalty Guide — 2004 published by Wise Research Limited, a research and publishing company based in the United Kingdom, loyalty marketing provides consumers with a practical reason for being attracted to and continuing to buy a partner's products and services: the accumulation of points or miles toward a valued reward or benefit. Loyalty marketing competes with other forms of marketing, including direct mail, telephone marketing, mass media advertising, sales promotions and incentives.

Increasing competitive pressure for the attention and engagement of consumers combined with the rapid evolution of technology have created an environment conducive to the growth of the Canadian loyalty marketing

industry. Loyalty programs have become prevalent in multiple consumer sectors, including mass merchandise, retail pharmacies, financial services and the travel services sector.

Maintenance, Repair and Overhaul Industry

While aircraft maintenance, repair and overhaul ("MRO") services stem from three primary customer sources (airlines, original equipment manufacturers, and other MRO providers), the MRO industry's performance is most dependent on the airline industry's economic performance. Although airline profit margins have suffered in recent years as a result of rising fuel prices and a very competitive market, the industry is showing signs of recovery. As airlines add capacity and increase traffic, the MRO market is expected to grow in parallel. According to Overhaul & Maintenance, a magazine devoted to the overhaul and maintenance industry, the world fleet is forecasted to grow from over 15,000 planes in 2005 to over 25,000 planes in 2015, with regional jets showing the largest percentage increase.

Similarly, as airline cost pressures continue to mount, global MRO outsourcing is expected to continue. According to Overhaul & Maintenance, the global commercial MRO market is expected to grow to approximately US$55 billion by 2015, a 45% increase from US$38 billion in 2005. Also, according to Mercer Management Consulting, almost half of United States carriers' maintenance work is currently outsourced. This growth is expected in all sectors, including airframe, engine, components and line maintenance.

Going forward, successful full-service MRO providers will be ones that can provide ‘one-stop' solutions for their customers. Increasingly, airlines and leasing companies already prefer to deal with a single MRO provider that has the expertise required to manage all of their MRO work, including airframe, component, and engine repairs as well as specialized services. However, MRO operators will continue to be under industry pressure to maintain effective cost controls to bid competitively in a cost-sensitive marketplace.

THREE-YEAR SUMMARY: EVOLUTION OF BUSINESS

Economic Environment

In early 2003, Air Canada's revenues began to be severely impacted by: (i) the advent of the Iraq war; (ii) the SARS outbreak; and (iii) the rapid expansion of WestJet and other low-cost carriers. In combination, these factors caused Air Canada's passenger revenues to decline significantly in 2003 versus 2002. The operating losses of 2001 and 2002 had already significantly diminished the liquidity of Air Canada and alternative sources of funding were not available.

On March 21, 2003, the Office of the Superintendent of Financial Institutions ("OSFI") issued directions requiring Air Canada to file new actuarial valuations of its ten registered pension plans and to make retroactive current service contributions to eight of those plans in respect of 2002. The impact of these directions would have been to place a great burden on Air Canada's liquidity over the ensuing five years in order to fund the pension plans' solvency deficit in the time required by existing regulations.

Consequently, with the advice of their financial and legal advisors, the Applicants (as defined below) elected to restructure their operations, debt and capitalization under the protection of the *Companies' Creditors Arrangement Act* ("CCAA").

Air Canada's Consolidated Plan of Reorganization, Compromise and Arrangement

On April 1, 2003 Air Canada obtained an initial order from the Ontario Superior Court of Justice (the "Court") providing creditor protection under the CCAA. The initial order was further amended by the Court throughout the CCAA proceedings based on motions from Air Canada, its creditors and other interested parties. On April 1, 2003, Air Canada, through Ernst &Young Inc., its Court-appointed monitor ("Monitor"), also made a concurrent petition for recognition and ancillary relief under Section 304 of the U.S. Bankruptcy Code. The CCAA and U.S. proceedings covered Air Canada and the following of its wholly-owned subsidiaries: Jazz Air Inc., ZIP Air Inc., 3838722 Canada Inc., Air Canada Capital Ltd., Manoir International Finance Inc., Simco Leasing Ltd., and

Wingco Leasing Inc. (collectively, the "Applicants"). Aeroplan, Touram Inc. and Destina.ca were not included in the CCAA filing. These three subsidiaries continued to deal with their creditors on a normal basis, unaffected by the CCAA and U.S. proceedings.

The initial order and U.S. proceedings contained a general stay of proceedings against the Applicants. This stay generally precluded parties from taking any action against the Applicants for breach of contractual or other obligations. The purpose of the stay period order was to provide the Applicants with relief designed to stabilize their operations and business relationships with customers, vendors, employees and creditors and to allow Air Canada to develop a process for soliciting new equity or other post emergence financing. During the stay period, Air Canada developed its revised business plan and concluded new arrangements with creditors (including aircraft lessors) and labour unions.

On September 30, 2004, ACE's predecessor corporation and now its wholly-owned subsidiary, Air Canada, and the other Applicants, emerged from creditor protection under the CCAA and implemented the Plan. The purpose of the Plan, together with Air Canada's new business strategy, was to restructure the capitalization, operations and cost structure of Air Canada. The Plan and the new business strategy were designed to:

(i) reduce Air Canada's operating costs to a competitive level through the renegotiation of collective bargaining agreements, aircraft leases, real property leases and various other commercial agreements;

(ii) implement a fleet renewal program to achieve the appropriate number, size and mix of aircraft for Air Canada's route network;

(iii) complete a restructuring of Air Canada's debt and lease obligations;

(iv) redefine Air Canada's core product offerings to enable it to compete effectively in the current and future airline industry environment; and

(v) reorganize Air Canada's corporate structure to enable certain key businesses to better compete for third party business and generate value for their stakeholders.

The implementation of the Plan reduced Air Canada's debt (net of cash and cash equivalents) and lease obligations (on a present value basis) to approximately $4 billion as at December 31, 2004 compared to $12 billion as at December 31, 2002, prior to Air Canada's filing for protection under the CCAA. Also, as part of the implementation of the Plan, all the preferred shares of Air Canada were cancelled and all of the holders of common shares and Class A non-voting shares of Air Canada exchanged their shares for Voting Shares and Variable Voting Shares. Pursuant to such exchange, the former holders of common shares and Class A non-voting shares of Air Canada received 0.01% of the fully diluted equity of ACE upon emergence from the CCAA proceedings.

On September 30, 2004, as part of the implementation of the Plan, Air Canada reorganized its corporate structure. Pursuant to such corporate reorganization, APLN Limited Partnership (a predecessor to Aeroplan), Jazz Air Inc. (the predecessor to Jazz Air Limited Partnership and Jazz Air LP), Touram Inc. (the predecessor to Touram Limited Partnership) and Destina.ca Inc. (a predecessor to Destina eCommerce Group LP), which were already established as stand-alone entities under Air Canada, became stand-alone entities under ACE, while ACTS LP, AC Cargo LP, AC Online Limited Partnership (a predecessor to Destina eCommerce Group LP) and ACGHS LP were established as stand-alone limited partnerships under ACE. Jazz Air Inc. had been a stand alone entity under Air Canada and on September 30, 2004 transferred substantially all of its assets and certain of its liabilities to the newly created Jazz Air Limited Partnership, a stand alone limited partnership under ACE. Destina.ca Inc. had been a stand alone entity under Air Canada and on July 31, 2005 transferred substantially all of its assets and certain of its liabilities to Destina eCommerce Group LP, a stand alone limited partnership under ACE.

As a result, ACE operates as a holding company for Air Canada and ACE's other subsidiaries. ACE's new corporate structure is designed to facilitate the development of each business unit to its fullest individual potential including, where appropriate, through the pursuit of third party sources of business, and to maximize the value of the subsidiaries.

Rights Offering

As part of the Plan, ACE offered rights to Air Canada's creditors with proven claims to subscribe for up to $850 million of Voting Shares and/or Variable Voting Shares ("Shares"). Pursuant to its standby purchase agreement with Air Canada, Deutsche Bank Securities Inc. ("Deutsche Bank") agreed to act as the exclusive standby purchaser in respect of the rights offering. As standby purchaser, Deutsche Bank had the right to syndicate out its rights to purchase Shares. Deutsche Bank and the participants in its syndicate subscribed for all the Shares not otherwise subscribed for by the creditors at a subscription price per Share of $21.50, which represented the subscription price of $20.00 paid by creditors, plus a premium of $1.50. On September 30, 2004, ACE completed the issuance of Shares under such rights offering for total gross proceeds of $865 million, including the amount of the premium paid by Deutsche Bank and the participants of its syndicate pursuant to the standby purchase agreement.

In accordance with the terms of the standby purchase agreement, ACE entered into a registration rights agreement with Deutsche Bank, dated as of September 30, 2004 (the "Registration Rights Agreement"). Under the Registration Rights Agreement, ACE agreed to use its reasonable best efforts to prepare and file with the United States Securities and Exchange Commission ("SEC") a registration statement covering the resale, from time to time, of Registrable Securities (as defined below) by the Selling Shareholders (as defined below), and to use its reasonable best efforts to maintain the effectiveness of the registration statement for a period of two years from the date of effectiveness. "Registrable Securities" means any Shares purchased by Deutsche Bank or the participants in its syndicate pursuant to the Plan, including Shares purchased pursuant to the standby purchase agreement, as well as any securities issued upon conversion of, in exchange for, or in substitution for such securities. Such Shares will cease to be Registrable Securities if: (i) they are sold pursuant to the Resale Prospectus (as defined below); (ii) they are sold pursuant to an exemption from registration under the 1933 Act and, following such sale, are freely tradable in the United States and Canada; or (iii) such Shares cease to be outstanding. "Selling Shareholders" means Deutsche Bank and each participant of its syndicate for so long as such person is the registered owner of any Registrable Securities, and such person's heirs, successors and permitted assigns so long as such heir, successor or permitted assign is the registered owner of Registrable Securities with a fair market value of at least $100,000 as of the date of the Resale Prospectus.

On November 30, 2004, a resale registration statement containing a resale prospectus (the "Resale Prospectus") was filed with the SEC in accordance with the terms of the Registration Rights Agreement in order to cover resales of Registrable Securities by the Selling Shareholders. Based upon information provided to ACE by the Selling Shareholders, the Selling Shareholders held, as of November 12, 2004, a total of 26,774,011 Variable Voting Shares and 58,805 Voting Shares. ACE cannot estimate the amount of Shares that will be held by the Selling Shareholders upon the termination of the two-year period during which the Resale Prospectus remains valid.

Investment Agreement

On September 30, 2004, Promontoria Holding III B.V. ("Cerberus Affiliate") invested $250 million in ACE in consideration for the issuance to it of 12,500,000 Preferred Shares initially convertible into 9.16% of the fully diluted equity of ACE upon emergence from the CCAA proceedings. The Cerberus Affiliate holds all of the issued and outstanding Preferred Shares. For a summary of the terms of the Preferred Shares, see "*Description of Capital Structure — Preferred Shares*".

Pursuant to the investment agreement with the Cerberus Affiliate dated June 23, 2004 ("Investment Agreement"), three of the 11 members of the board of directors of ACE appointed pursuant to the Plan were designated by the Cerberus Affiliate. The Cerberus Affiliate has the right to designate three of the 11 members of the board of directors of ACE for a minimum of two years after September 30, 2004. After September 30, 2006, for as long as the Cerberus Affiliate and its affiliates hold at least 75% of the Preferred Shares (or Shares into which they are converted or convertible) originally purchased under the Investment Agreement, the Cerberus Affiliate will continue to have the right to designate three individuals to the board of directors of ACE. After September 30, 2006, for as long as the Cerberus Affiliate and its affiliates hold at least 50% but less than 75% of the Preferred Shares (or Shares into which they are converted or convertible) originally purchased under the Investment Agreement, the Cerberus Affiliate will have the right to designate two individuals to the board of directors of ACE. For as long as the Cerberus Affiliate and its affiliates hold at least 25% but less than 50% of the Preferred Shares (or Shares into

which they are converted or convertible) originally purchased under the Investment Agreement, the Cerberus Affiliate will have the right to designate one member of the board of directors of ACE. For as long as the Cerberus Affiliate and its affiliates hold at least 2.5% of the economic equity interests of ACE, the Cerberus Affiliate will have the right, at reasonable times and upon reasonable notice, to have access to the management of ACE and to all reasonable financial and operating information of ACE, including business plans, budgets and quarterly results, in order to consult with management and express its views on the business and affairs of ACE and its subsidiaries.

The Preferred Shares (including the Shares into which they are converted or convertible) may not be sold, assigned or in any way transferred by the Cerberus Affiliate (other than to its affiliates) including pursuant to hedging transactions, swaps or other arrangements transferring any of the economic consequences of the ownership of the Preferred Shares acquired by the Cerberus Affiliate for a period of 24 months after September 30, 2004; provided that, if at any time during such 24-month period the Cerberus Affiliate is required to convert the Preferred Shares, then the restrictions on transfer with respect to 50% of the Preferred Shares (and any Shares into which they are converted or convertible) will be of no force and effect and the restrictions on transfer with respect to the remaining 50% of the Preferred Shares (and any Shares into which they are converted or convertible) will be limited only to sales of beneficial ownership of the Preferred Shares (and any Shares into which they are converted or convertible) to third parties. Notwithstanding the foregoing, the transfer restrictions will cease to be in effect as to all Preferred Shares (and any Shares into which they are converted or convertible) in the event of a tender offer or take-over bid for any of the Shares, any change in control transaction, any liquidation, dissolution, bankruptcy or other similar proceedings of ACE.

The terms attached to the Preferred Shares provide the Cerberus Affiliate with preemptive rights on any issuance or sale by ACE of Variable Voting Shares or Voting Shares or other equity securities, rights, options, warrants or other convertible securities which represent rights to purchase Variable Voting Shares or Voting Shares. For further details, see " *Description of Capital Structure — Preferred Shares — Preemptive Rights*".

GECC Lease Restructuring and Financing

In 2003 and 2004, agreements were signed between General Electric Capital Corporation ("GECC") and Air Canada (the "GECC Agreements") which provided for:

(i) the restructuring of existing arrangements for 106 aircraft which included lease rate reductions on 47 aircraft, termination of obligations with respect to 20 parked aircraft, the cancellation of four future aircraft lease commitments and the restructuring of the overall obligations of six aircraft;

(ii) exit financing totalling approximately US$681 million in three tranches for use upon emergence from the CCAA proceedings. The loan was repaid in full prior to maturity on April 6, 2005;

(iii) a financing commitment of up to US$950 million to be used for acquisitions of new regional jet aircraft (the "RJ Financing"). On exit from CCAA the parties agreed to reduce the commitment to US$500 million; and

(iv) the purchase from GECC by Air Canada on September 30, 2004 of two Boeing 747-400 Combi aircraft (which Air Canada was leasing at the time) for an aggregate amount of $353 million. The purchase price was paid for with $290 million in cash and the issuance of a limited-recourse loan in the amount of US$50 million. The two Boeing 747-400 Combi aircraft were sold in December 2004 and January 2005 and the proceeds from such sale were used to repay the US$50 million loan from GECC.

Pension Plan Arrangements

Air Canada sponsors 10 defined benefit registered pension plans for its employees and retirees in Canada. Canadian federal pension legislation requires that the funded status of registered pension plans be determined periodically on both a going concern basis (*i.e.*, essentially assuming indefinite plan continuation) and a solvency basis (*i.e.*, essentially assuming immediate plan termination). The solvency position of the pension plans deteriorated significantly in 2002 as a result of various macroeconomic developments, triggering a series of valuation and funding directions to Air Canada by OSFI, the federal pension regulator, in March 2003.

On September 30, 2004, after negotiations with OSFI and representatives of the pension plan stakeholders, the *Air Canada Pension Plan Solvency Deficiency Funding Regulations* came into effect. The Regulations extended the usual five-year amortization period for solvency deficits to ten years, and provided for the making of variable annual amortization payments according to an agreed schedule rather than the usual equal annual payments. Air Canada also issued a series of subordinated secured promissory notes in the aggregate amount of $346.6 million in favour of the pension plan trustees. The promissory notes are secured by a second priority charge over assets of Air Canada and certain of its affiliates and will be reduced by the capital portion of the solvency deficit amortization payments made by Air Canada to the pension plans in accordance with the agreed schedule.

Arrangements with Unions

Following its filing for protection under the CCAA, Air Canada concluded in 2003 and amended in 2004 long-term collective agreements with the International Association of Machinists and Aerospace Workers (IAMAW), the Air Canada Pilots Association (ACPA), the Canadian Union of Public Employees (CUPE), the Canadian Air Line Dispatchers Association (CALDA), the National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW) and the International Brotherhood of Teamsters (IBT), which expire in 2009. Air Canada also concluded agreements with the Transport and General Workers Union (TGWU) and Amicus, both in the United Kingdom. All these labour agreements were ratified by the members of their respective bargaining units. The agreements provided for a combination of productivity improvements and wage reductions. All unconditional employment security provisions in the collective agreements were also eliminated. All scheduled bonus payments and wage increases were cancelled and all overtime is now paid at one and a half times the applicable pay rate. Air Canada also entered into "clean slate" agreements with all of its North American unions where the parties agreed to resolve, waive or compromise outstanding grievances.

These collective agreements provide that, in 2006, the parties may negotiate the wage provisions for the balance of the collective agreement and, failing agreement of the parties to adjust wages as circumstances may warrant, the matter shall be resolved by mediation or binding arbitration without resort to strike or lock-out.

The Unions in the United Kingdom, TGWU and Amicus, had a wage re-opener as part of their extended collective agreements which was effective October 1, 2004. Although there was no general increase to the wage rates provided to either of the groups, targeted adjustments were made as part of a retention strategy. The agreements concluded in 2004 expire in 2009 and contain a provision to reopen negotiations for wages, effective April 1, 2006. Another component of the agreement between Air Canada and Amicus was the introduction of a defined contribution pension plan for newly hired employees, to be implemented following the implementation of a defined contribution plan for non-unionized employees.

All of Air Canada's North American unions, have agreements entitling them to participate in a profit-sharing program under which (i) 7.5% of adjusted pre-tax profits up to 7% of revenues, and (ii) 25% of adjusted pre-tax profits above 7% of revenues, will be distributed to eligible employees. Payments under the profit-sharing program were distributed based on the results of the year 2005.

Jazz also concluded new collective agreements with its unions following its filing for protection under the CCAA in 2003. All of Jazz's collective agreements expire on June 30, 2009 and the unions are not allowed to strike until the end of the term of the collective agreements. These collective agreements, except for the collective agreement with the pilot union group of Jazz, provide for a process to revise the wage levels in mid-2006 by negotiation or, failing negotiation, by mediation or arbitration. Jazz also entered into "clean state" agreements with its unions where the parties agreed to resolve, waive or compromise outstanding grievances.

Contract Renegotiation/Repudiation during CCAA

During the restructuring period, the Corporation reviewed all of its real estate facilities, resulting in the elimination of unused or under-utilized facilities and the consolidation of its operations to further reduce operating costs. In addition, the Corporation evaluated all of its contracts for goods and services to identify opportunities to consolidate its supply base, to better leverage its buying power, and to take advantage of the opportunity represented by the restructuring process to repudiate contracts that were unfavourable.

In addition, the Corporation conducted extensive negotiations with its aircraft lessors and financiers to restructure its aircraft ownership and leasing costs. Through these efforts, Air Canada and Jazz achieved: (i) reduced ownership and leasing costs more consistent with then current market conditions, (ii) modified lease expiry dates based on planned new aircraft acquisitions and scheduled heavy maintenance requirements, and (iii) satisfactory aircraft return conditions consistent with modified lease expiry dates.

Public Offering of Voting Shares, Variable Voting Shares and Convertible Senior Notes due 2035

On April 6, 2005, ACE completed the public offering of an aggregate of 11,350,000 Voting Shares and Variable Voting Shares at a price of $37.00 per share for gross proceeds of approximately $420 million, and $300 million of 4.25% convertible senior notes due 2035 (the "Notes"). ACE used approximately $553 million of the aggregate net cash proceeds of the offerings to repay all of its outstanding debt under the exit credit facility with GECC. The repayment of the GE exit facility has reduced net annual interest costs by an estimated $27 million and has provided ACE with greater strategic and financial flexibility. On April 13, 2005, following the exercise of the over-allotment option by the underwriters, ACE issued an additional 1,135,000 Variable Voting Shares at a price of $37.00 per share and $30 million of Notes for additional aggregate gross proceeds of approximately $72 million. ACE used the additional proceeds for general corporate purposes.

Initial Public Offering of Aeroplan Income Fund

On June 29, 2005, Aeroplan Income Fund completed its initial public offering of 25 million units at a price of $10 per unit for gross proceeds of $250 million. On June 30, 2005, following the exercise of the over-allotment option by the underwriters, Aeroplan Income Fund issued an additional 3.75 million units at a price of $10 per unit for additional gross proceeds of $37.5 million, bringing the aggregate gross proceeds of the initial public offering to $287.5 million. Aeroplan Income Fund's units trade on the Toronto Stock Exchange under the symbol AER.UN. Aeroplan Income Fund has acquired a 14.4% ownership interest in Aeroplan. Following the initial public offering and the exercise of the over-allotment option by the underwriters, ACE held a 85.6% ownership interest in Aeroplan.

US Airways Group Inc.

On September 27, 2005, the Corporation invested $87 million (US$75 million) in US Airways Group Inc. (US Airways) in conjunction with the carrier's exit from US bankruptcy proceedings. The Corporation's investment represented approximately 6 percent of the equity of US Airways at December 31, 2005. The equity investment is subject to a six-month holding period from the closing date. In connection with the equity investment, ACE also received options to purchase additional common stock in US Airways. On closing of the transaction, ACE sold these options for proceeds of $1 million.

Aircraft Purchase Agreement between The Boeing Company and Air Canada

On November 4, 2005, Air Canada concluded agreements with The Boeing Company ("Boeing") for the acquisition of up to 36 Boeing 777 aircraft and up to 60 Boeing 787 Dreamliners. The agreements include firm orders for 18 Boeing 777 aircraft, plus purchase rights for an additional 18 aircraft, in a yet-to-be determined mix of the 777 family's newest models. Deliveries of the Boeing 777 aircraft are scheduled to commence in March 2007. Seven Boeing 777 aircraft are expected to be delivered in 2007, nine aircraft in 2008, and two aircraft in 2009. The agreements also include firm orders for 14 Boeing 787 Dreamliners, plus options and purchase rights for an additional 46 aircraft. Air Canada's first Boeing 787 aircraft is scheduled for delivery in 2010.

Initial Public Offering of Jazz Air Income Fund

On February 2, 2006, Jazz Air Income Fund completed its initial public offering of 23.5 million units at a price of $10 per unit for gross proceeds of $235 million. On February 27, 2006, following the partial exercise of the over-allotment option by the underwriters, Jazz Air Income Fund issued an additional 1.5 million units at a price of $10 per unit for additional gross proceeds of $15 million, bringing the aggregate gross proceeds of the initial public offering to $250 million. Jazz Air Income Fund's units trade on the Toronto Stock Exchange under the symbol

JAZ.UN. Jazz Air Income Fund has acquired a 20.3% ownership interest in Jazz. Following the initial public offering and the partial exercise of the over-allotment option by the underwriters, ACE holds a 79.7% ownership interest in Jazz.

Distribution by ACE of Units of Aeroplan Income Fund

On February 16, 2006, ACE announced a special distribution to its shareholders of units of Aeroplan Income Fund. The distribution of 0.18 units of Aeroplan Income Fund per Variable Voting Share, Voting Share and Preferred Share (on an as converted basis) of ACE is being 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 and the payment date is expected to be on or about March 31, 2006. Following this distribution, ACE holds a 75.5% ownership interest in Aeroplan.

OVERVIEW OF THE BUSINESS

ACE is the parent holding company of the following subsidiaries:

Air Canada is Canada's largest domestic and international full-service airline and the largest provider of scheduled passenger services in the domestic market, the Canada-US transborder market and each of the Canada Europe, Canada Pacific, Canada Caribbean/Central America and Canada South America markets. Passenger transportation is the principal business of the Corporation and, in 2005, represented 84 per cent of its total operating revenues.

Air Canada and Jazz, the Corporation's regional carrier, operate an extensive domestic, US transborder and international network. During 2005, Air Canada and Jazz operated, on average, approximately 1,200 scheduled flights each day and carried over 30 million passengers. In 2005, Air Canada and Jazz provided direct passenger air transportation to 159 destinations and, through commercial agreements with other unaffiliated regional airlines referred to as Tier III carriers, to an additional 11 destinations, for a total of 170 direct destinations on five continents. Air Canada's primary hub is located in Toronto, and its other hubs are located in Montreal, Vancouver and Calgary. Toronto's Pearson International Airport is Canada's largest airport and Air Canada's largest hub overall. Montreal's Pierre-Elliott Trudeau International Airport is a hub for domestic, transborder and international (primarily trans-Atlantic) traffic. Vancouver International Airport and Calgary International Airport are hubs for domestic, transborder and international (primarily trans-Pacific in the case of Vancouver) traffic.

Air Canada also operates an extensive global network in conjunction with its international partners. Air Canada is a founding member of the Star Alliance® network, the world's largest airline alliance group. The Star Alliance® network has grown, since its inception, to include 16 members and three regional members. Through its strategic and commercial arrangements with Star Alliance® members and several other airlines, Air Canada offers service to over 795 destinations in 139 countries, with reciprocal participation in frequent flyer programs and use of airport lounges.

In addition to scheduled passenger service, both Air Canada and Jazz also operate charter services in the domestic, transborder and international markets. Air Canada has four of its Airbus A320 aircraft configured in all business class seating and these aircraft are dedicated to executive style charter services operated through a division

of Air Canada called Air Canada Jetz. Air Canada Jetz provides these executive charter services to customers such as professional sports teams, rock bands and corporations.

The Corporation has a controlling interest in Aeroplan which operates Canada's premier loyalty program. Aeroplan provides its commercial partners with loyalty marketing services designed to attract and retain customers and stimulate demand for such partners' products and services. Aeroplan's objective is to offer its commercial partners superior value relative to other marketing alternatives through access to Aeroplan's base of members and the design and execution of marketing programs aimed at increasing revenue, market share, and customer loyalty. The Aeroplan program is one of Canada's longest standing loyalty programs. It was founded in 1984 by Air Canada to manage the airline's frequent flyer program. Aeroplan benefits from its unique strategic relationship with Air Canada in addition to its contractual arrangements with leading commercial partners including AMEX, Bell Canada, CIBC, Future Shop, Imperial Oil (Esso), Star Alliance® member airlines and numerous hotel chains and car rental companies.

Aeroplan offers its approximately five million active members the ability to accumulate Aeroplan Miles throughout its partner network through purchases of products and services. Aeroplan sells Aeroplan Miles to its extensive network of over 60 commercial partners, representing over 100 brands in the financial services, travel services and consumer products and services industries. Today, financial services partners generate the majority of Aeroplan's revenues.

Jazz and Air Canada entered into a capacity purchase agreement (the "Initial CPA") effective September 30, 2004, pursuant to which Air Canada purchased substantially all of Jazz's fleet capacity based on predetermined rates. The Initial CPA was replaced by an amended and restated capacity purchase agreement effective January 1, 2006 (the "CPA") pursuant to which Air Canada continued to purchase substantially all of Jazz's fleet capacity based on predetermined rates. Under the CPA with Air Canada, Jazz provides service to and from lower density markets as well as higher density markets at off-peak times throughout Canada and to and from certain destinations in the United States. As of March 1, 2006, Jazz operated scheduled passenger service on behalf of Air Canada with approximately 730 departures per weekday to 55 destinations in Canada and 22 destinations in the United States with a fleet of 131 aircraft made up of 129 operating aircraft and 2 newly delivered aircraft that were not yet in active service. Jazz and Air Canada have linked their regional and mainline networks in order to serve connecting passengers more efficiently and to provide valuable traffic feed to Air Canada’s mainline routes.

The Corporation also provides Technical Services through ACTS LP. ACTS LP is a full-service Maintenance, Repair and Overhaul (MRO) organization that provides airframe, engine and component maintenance and various ancillary services to a wide range of more than 100 global customers. ACTS LP operates maintenance centers across Canada, with principal centers located in Montréal, Toronto, Winnipeg and Vancouver.

The Corporation also provides cargo services through AC Cargo LP; ground handling services through ACGHS LP; and tour operator services and leisure vacation packages through Air Canada Vacations.

New Business Strategy

In order to respond to a rapidly changing landscape, the Corporation has fundamentally changed its business strategy and has been redesigning its business processes since emergence from CCAA. ACE designed and embarked on a new business plan to: (i) consolidate the domestic market position of Air Canada and Jazz through a superior product offering at a competitive cost; (ii) provide a sustainable foundation for Air Canada's growing international markets; and (iii) highlight the value inherent in ACE's subsidiaries. The Corporation's new business strategy is based on the following four major components:

(i) a competitive cost structure;

(ii) a redesigned network to maximize efficiency and leverage international growth opportunities;

(iii) a new revenue model for passenger services; and

(iv) a new corporate structure to facilitate the implementation of strategic initiatives and to surface the value of its subsidiaries.

Competitive Cost Structure

The Corporation's new business strategy is built on a significantly improved competitive cost structure. During the CCAA restructuring process and since emerging from the process, the following three main focus areas have contributed significantly to the Corporation's benefit:

(i) Through the CCAA restructuring process, the Corporation dramatically reduced its operating costs;

(ii) Following this, the Corporation embarked on a substantial re-engineering process to simplify its internal processes and reduce its costs even further by eliminating non-value adding tasks and procedures. This is an ongoing process of continuous improvement; and

(iii) Additionally, the Corporation has created a new business model whereby its customers can be served directly using web-enabled technology which is envisaged to further eliminate substantial external non-value adding processes between the Corporation and its customers. This too is an ongoing process of continuous improvement.

Stemming from the above focus areas, the Corporation has realized and envisages continuing to benefit from substantial cost reductions in the following areas:

(i) substantially reduced supplier obligations, including aircraft and real estate;

(ii) significantly improved labour productivity due to a rationalized work force and lower average salaries;

(iii) lower trip costs due to better matching of capacity with demand;

(iv) higher operating efficiencies through its fleet modernization program;

(v) lower pilot training, inventory carrying and maintenance costs;

(vi) significantly lower sales and distribution costs by improved and easy to use web-enabled technology for its customers; and

(vii) dramatically lower internal costs by eliminating business processes which do not fit the new revenue model.

Unlike its low-cost competitors, the Corporation incurs costs related to the offer of value-added transportation services, such as Executive Class services and other non-air services. The Corporation believes that these costs are offset by a revenue premium, driven primarily by higher Yield and Passenger Load Factor, increased international connecting traffic and increased Aeroplan and cargo revenues. The Corporation expects to maintain this revenue premium by continuing to leverage its key competitive advantages, including:

(i) a more extensive route network, greater flight frequency and greater market presence;

(ii) value-added services, for which customers are willing to pay a premium, including unlimited schedule changes, same day stand by, advance seat selection, full Aeroplan mileage, concierge service and Executive Class service; and

(iii) higher yielding international (including Canada-US transborder) connections.

Redesigned Network to Maximize Efficiency and Leverage International Growth Opportunities

The Corporation's objective is to become the customer's clear choice in all the markets in which it competes by offering a better scheduled product at a competitive price. To this end, the Corporation's redesigned network focuses on offering better flight frequencies on key domestic and Canada-US transborder routes, while maintaining competitive frequency on other domestic and Canada-US transborder routes, and reducing the average seating capacity per departure.

The Corporation expects to achieve its objectives through the increased use of large regional jet aircraft which have lower trip costs. This initiative, for which deliveries commenced in October 2004, will see Air Canada and Jazz add 90 new regional jet aircraft to their fleet by the end of 2007. As of the date hereof, the Corporation had received fifteen 50-seat Bombardier CRJ-200 aircraft, fifteen 75-seat Bombardier CRJ-705 aircraft and fifteen 73-seat Embraer ERJ 175 aircraft under firm order as well as six 93-seat ERJ 190 aircraft. Thirty-nine additional Embraer ERJ 190 aircraft under firm order are scheduled for delivery during the remainder of 2006 and during 2007. In addition, as a result of agreements reached with Air Canada's and Jazz's unions during Air Canada's restructuring under the CCAA, all of the Corporation's Bombardier CRJ aircraft will be operated out of Jazz's regional operations. The Corporation expects that the lower trip costs of these regional jet aircraft will enable the Corporation to compete more effectively with low-cost carriers. This strategy should allow the Corporation to operate its network more efficiently by better matching capacity with demand and by facilitating connections in a timely fashion.

Since international services generally produce higher margins than domestic and transborder services, the Corporation also intends to expand its existing services to currently served international destinations as well as adding new international destinations. The Corporation believes that it is well positioned to grow its international services and increase its current market share by leveraging the following competitive advantages:

(i) its superior international network;

(ii) its widely recognized brand and its strong position in the market for trans-Atlantic and trans-Pacific travel to and from Canada and more recently the Canada-South America market; and

(iii) its ability to capitalize on the relative speed and convenience associated with having its hubs located in Canada which, unlike the United States, does not currently require a visa from residents of certain countries transiting through the country.

For domestic, Canada-US transborder and international services, the Corporation will continue to leverage the strengths of its Aeroplan program.

Customer Driven Revenue Model for Passenger Services

The Corporation's new revenue model for passenger services is aimed at improving customer satisfaction and retention by focusing on simplicity, value, choice, transparency and flexibility for the customer and is resulting in greater passenger volume, higher passenger load factors and increased cost efficiency for Air Canada and Jazz.

The new revenue model in North America is based on five simple fare types ranging from low one-way fares, substantially similar to those offered by low-cost carriers, to Executive Class fares. The new fares are based on a different combination of product attributes, including the ability to make changes to reservations, seat selection, meal service and Aeroplan mileage earning. The new model provides transparency by allowing customers to compare prices and travel options and select the most suitable fare. The Corporation believes that this establishes a clear link between price and value and will be a key driver in achieving customer loyalty.

The new revenue model was introduced in Air Canada's and Jazz's domestic markets in May 2003. In February 2004, the new revenue model was expanded to all destinations in the continental United States served by Air Canada and Jazz in cooperation with United Airlines, one of Air Canada's Star Alliance® partners.

For international markets, Air Canada has taken a similar approach to simplifying its fare offering and associating value-added attributes to each fare type. On January 4, 2006, Air Canada expanded its low, simplified fare structure for flights to and from London Heathrow and Manchester. This simplified fare structure was then expanded to include flights to and from Italy, Israel and France. Air Canada plans to convert more international destinations to its simplified fare structure in the near future.

The Corporation believes that its increasing use of the Internet to improve its distribution network has facilitated market acceptance of its new revenue model. Air Canada currently operates or has in development websites to serve customers and travel agents in Canada, United States, the Caribbean region, the United Kingdom, France, Germany, Italy, Ireland, Scandinavia, the Netherlands, Switzerland, Australia and Hong Kong. Air Canada's Internet strategy will continue to focus on expanding distribution reach, creating compelling products and content

suited to the web, and enabling its websites with functionality that will allow customers to service themselves at all relevant points in their shopping and travel experience.

Another key step in the implementation of its new revenue model was the introduction starting in spring 2004 of a range of online pass products that offer significant savings for frequent travelers who commit to purchasing multiple flights in advance. This product also provides online convenience that underlines Air Canada's commitment to lead the way by giving customers the ability to plan their travel budgets upfront and enjoy price predictability throughout the life of their pass. Among the products are: the North America Pass, which allows travel within zones throughout North America, the Sun Pass for travel between Eastern Canada and Florida, Arizona or Nevada or between Western Canada and Arizona, Nevada or California; the Hawaii Pass for travel between Western Canada and the Hawaiian Islands, and the Oil Express Pass for travel between Ft. McMurray and Atlantic Canada, among others. In addition, in September of 2005, Air Canada expanded its line of multi-trip pass products to include the airline industry's first-ever subscription to unlimited flights. This “North America Unlimited Pass” provided pass holders the freedom to fly as often as they wished to more than 100 destinations served by Air Canada and Jazz in North America for a two-month period from October 1 to November 30, 2005.

New Corporate Structure to Maximize the Value of Subsidiaries

A new corporate structure was established pursuant to which the various business segments that were formerly within Air Canada became stand-alone subsidiaries of ACE. The new corporate structure was designed to:

(i) put in place separate management and business plans for each subsidiary to better focus their strategic direction and profit making efforts;

(ii) align management, capital and human resource needs within each individual business;

(iii) facilitate the development of each business segment to its fullest individual potential including, where appropriate, through the pursuit of third party business; and

(iv) maximize subsidiaries' value that was not fully recognized.

ACE's subsidiaries are at varying stages of their corporate development, and maximizing value at these entities is a priority in the efforts of senior management. ACE's value enhancement strategy for its stand-alone subsidiaries includes considering stand-alone financings, sales or distributions of equity interests and involving outside investors for these and other purposes.

From time to time, ACE reviews acquisition opportunities in respect of businesses or assets that may be complementary to its own. Where appropriate, to increase shareholder value, ACE may consider entering into other investment opportunities.

BUSINESS OF ACE

ACE's businesses are operated as four reportable segments which include: (i) transportation services; (ii) Aeroplan; (iii) Jazz; and (iv) ACTS LP. The table below sets forth the relative financial result of each business activity for the year ended December 31, 2005:

	ACE Successor Company Year ended December 31, 2005					
(in millions)	**Transportation Services[1]**	**Aeroplan[2]**	**Jazz[3]**	**ACTS LP**	**Inter-Segment Elimination**	**Consolidated Total**
Operating Revenue						
Passenger Revenue	$8,269	-	-	-	-	$8,269
Cargo Revenue	620	-	-	-	-	620
Other Revenue[4]	117	627	10	187	-	941
Inter-segment Revenue	194	13	1,013	567	(1,787)	-
Total Revenue	9,200	640	1,023	754	(1,787)	9,830
Operating Expenses	9,026	538	894	707	(1,787)	9,378
Operating Income	$ 174	$102	$ 129	$ 47	-	$ 452

(1) Includes transportation revenues for services provided both on Air Canada and Jazz aircraft and costs for Air Canada operations and fees charged by Jazz under the capacity purchase agreement with Air Canada, as well as AC Cargo LP, ACGHS LP, Touram LP and ACE operations.
(2) ACE held an 85.6% ownership interest in Aeroplan as at December 31, 2005 and currently holds a 75.5% ownership interest in Aeroplan.
(3) Includes Jazz's operations under the capacity purchase agreement with Air Canada. ACE held a 100% ownership interest in Jazz as at December 31, 2005 and currently holds a 79.7% ownership interest in Jazz.
(4) Includes revenues and costs for Ground Handling Services, Touram LP, and Destina eCommerce Group LP.

TRANSPORTATION SERVICES

Air Canada and Jazz are the Corporation's mainline and regional airline carrier, respectively. Passenger transportation is the principal business of the Corporation and, for the years ended December 31, 2004 and 2005, its passenger revenues were derived from domestic, transborder and international services in the proportions shown in the table below:

	Passenger Revenues for the Period ended December 31, 2004	**Passenger Revenues for the Year ended December 31, 2005**
Domestic	40%	42%
Transborder	20%	19%
International	40%	39%
Total	100%	100%

Air Canada is Canada's largest domestic and international full-service airline and the largest provider of scheduled passenger services in the domestic market, the transborder market and each of the Canada-Europe, Canada-Pacific, Canada-Caribbean/Central America and Canada-South America markets. According to OAG data in 2005, Air Canada ranked as the 14th largest carrier in the world, based on ASMs.

Jazz, the Corporation's regional carrier, provides service to lower density markets and to higher density markets at off-peak times throughout Canada and to certain destinations in the United States, and forms an integral part of Air Canada's domestic and transborder market strategy. Jazz's regional network connects passengers and provides valuable traffic feed to Air Canada's mainline routes.

Domestic Services

Air Canada and Jazz provide the largest network and most extensive product offering in Canada, with scheduled direct passenger service to 56 Canadian destinations in the first quarter of 2006. Based on OAG data, the Corporation estimates that in March 2006, it will provide approximately 61% of the Canadian airline industry's overall domestic scheduled capacity as measured by ASMs. The most important Canadian routes, in terms of operating revenues, are the transcontinental routes linking Toronto, Montreal and Ottawa with major Western Canadian cities, including Vancouver, Calgary, Edmonton and Winnipeg. Air Canada and Jazz operate several short-haul commuter routes, including Rapidair routes, linking Toronto, Montreal and Ottawa. The Corporation also offers frequent service linking major centres within Western Canada and operates numerous flights between Calgary and Vancouver and between Calgary and Edmonton. In addition to transcontinental and commuter routes, Air Canada and Jazz provide service between and within Central Canada, the Prairies and the Atlantic Provinces.

Unaffiliated regional carriers, referred to as tier III carriers, replace Jazz in markets not sufficiently large to be served directly. In the first quarter of 2006, these airlines operate flights under Air Canada's designator code and provide service to an additional 10 domestic destinations under commercial agreements with the Corporation. The Corporation does not own equity interests in any of these carriers.

Transborder Services

With the most non-stop destinations and flights to the United States, Air Canada and Jazz carry more passengers between Canada and the United States than any other airline. Based on OAG data, the Corporation estimates that in March 2006, it will provide approximately 42% of the overall transborder scheduled capacity as measured by ASMs. Air Canada and Jazz directly serve 42 U.S. destinations with an additional seven destinations served by tier III carriers, operating a total of approximately 390 daily flights in the first quarter of 2006. Air Canada's network reach is also increased by its extensive connections to, and Code-sharing flights with, United Airlines, one of its Star Alliance® partners.

International Services

Air Canada is uniquely positioned as Canada's largest scheduled international airline. In the first quarter of 2006, Air Canada provided scheduled service directly to 51 destinations in Europe, the Middle East, Asia, Australia, the Caribbean/Central America and South America. Based on OAG data, the Corporation estimates that in March 2006, it will provide approximately 46% of the overall scheduled international capacity between Canada and Europe and Canada and Asia, as measured by ASMs.

Air Canada has major trans-Atlantic operations to the United Kingdom, Germany and France. Air Canada currently operates nine daily flights to London Heathrow, four daily flights to Frankfurt, one daily flight to Munich and two daily flights to Paris.

Air Canada also has significant operations to the Asia-Pacific market via its Vancouver and Toronto hubs. Air Canada operates daily non-stop flights to Japan (Vancouver and Toronto to Tokyo and Vancouver to Osaka), China (Vancouver and Toronto to Beijing and Shanghai), Hong Kong (out of Vancouver and Toronto) and Korea (Vancouver and Toronto to Seoul). The Corporation also operates daily flights (one-stop) to India (Toronto to Delhi). In addition to targeting business travelers, these services also capitalize on the high volume of passengers who visit friends and relatives in Asia and Canada. The Corporation believes that the Asia-Pacific market currently represents an area of growth for air travel.

In addition, Air Canada has expanded its services to South America, Australia and Central America/Caribbean. Currently, Air Canada provides service directly to six destinations in South America, one in Australia, six in Central America/Mexico, and 23 in the Caribbean.

Star Alliance®

Air Canada is a founding member of the Star Alliance® network, the world's largest airline alliance group. Air Canada operates an extended global network in conjunction with its international partners.

The Star Alliance® network has grown, since its inception in 1997, to include the following 16 airlines: Air Canada, United Airlines, Lufthansa, SAS, Thai Airways, VARIG, Air New Zealand, All Nippon Airways, Austrian Airlines, Singapore Airlines, bmi, Asiana Airlines, Spanair, LOT Polish Airlines, US Airways and TAP Portugal. Swiss International Airlines is expected to join on April 1, 2006 and South African Airways on April 10, 2006. The Star Alliance® network also includes three regional members: Blue 1 (Finland), Adria Airways and Croatia Airlines.

Through its strategic and commercial arrangements with Star Alliance® members and several other airlines, Air Canada offers service to over 795 destinations in 139 countries, with reciprocal participation in frequent flyer programs and use of airport lounges. The Star Alliance® facilitates Code-sharing and passenger connections and transfers by providing a higher level of service between network connection points (which may include one stop check-in). The airlines have implemented initiatives, such as common utilization of facilities, and are focusing on capturing potential synergies in various areas. Air Canada now Code-shares with all Star Alliance® members, except US Airways, TAP Portugal and the three regional members. In August 2005, the Star Alliance® implemented an interline ticketing service which enables customers to travel across the entire Star Alliance® network using a single electronic ticket.

Fuel

Aircraft fuel is a major expense to companies operating within the airline industry. Since fuel costs represent a significant portion of the Corporation's operating costs, substantial changes in fuel costs would materially affect operating results. Fuel prices continue to be susceptible to factors such as political unrest in various parts of the world, Organization of Petroleum Exporting Countries (OPEC) policy, the level of demand from emerging economies, such as China, the level of inventory carried by the industry, the level of fuel reserves maintained by governments, disruptions to production and refining facilities and the weather. These and other factors will affect the price of fuel, which in turn affects the Corporation's financial performance. Based on 2005 volumes, the Corporation estimates that a US$1 per barrel movement in the price of West Texas Intermediate crude oil would have resulted in an approximate C$31 million change in 2005 fuel expense for Air Canada (excluding any impact of fuel surcharges and fuel hedging), assuming flying capacity remained unchanged and that refining spreads between West Texas Intermediate crude oil and jet fuel as well as foreign exchange rates remained constant.

In order to minimize the Corporation's exposure to the volatility of fuel prices, a systematic fuel risk management strategy was implemented in September 2005. The strategy involved using financial instruments to build up the Corporation's hedge position in increments of approximately 4% per month to a maximum of 50% of its anticipated fuel requirements for a 24-month period. In February 2006, the hedging strategy was revised to allow greater flexibility in terms of increasing or decreasing the scale, nature and timing of fuel hedging. The Corporation is no longer required to hedge a minimum percentage of its anticipated fuel consumption per month.

Competition

The Canadian airline industry is characterized by a limited number of high density markets, which account for the majority of passenger traffic and revenue. Domestic low-cost carriers have achieved a material presence in all major domestic markets and they continue to expand. The Corporation has redefined its business strategy in order to compete effectively.

Competition in the transborder market is primarily from the U.S. legacy carriers, which tend to operate flights between the United States and Canada via their hubs for connecting flights. U.S. legacy carriers with transborder operations include, without limitation, American Airlines, Delta Airlines, Continental Airlines, United Airlines and Northwest Airlines. Canadian low-cost carriers operate transborder services and are expanding their operations in the transborder market. WestJet currently provides transborder services to Orlando, Tampa, Fort Myers, Fort Lauderdale, Los Angeles, Palm Springs, Phoenix, Las Vegas, Honolulu and Maui. CanJet currently provides transborder services to New York and Orlando, Florida, year-round, and seasonally to other destinations in Florida including, St Petersburg, West Palm Beach, Fort Lauderdale and Sarasota.

In the trans-Atlantic and trans-Pacific markets, Air Canada primarily competes with foreign legacy carriers and, to a lesser extent, with charter and low-cost carriers on higher density routes, primarily during peak travel seasons. U.S. legacy carriers also provide indirect competition by flying Canadian passengers through their hubs to

international markets. However, management believes that the U.S. government policy requiring a visa from residents of certain countries for transit through the United States has provided an advantage to Air Canada since there is currently no equivalent requirement that applies to transit through Canada.

Air Canada Fleet

The Corporation has simplified its fleet structure to support its new business strategy. This fleet simplification includes the elimination of older, less efficient aircraft which are not economically viable in the new market environment and the increased utilization of new large regional jet aircraft which have lower trip costs. The new regional jet aircraft are key to the Corporation's strategy, which involves offering high flight frequency on key domestic and transborder routes, while maintaining competitive frequency on other domestic and transborder routes. The use of regional jet aircraft also allows the Corporation to better match capacity with demand, by reducing the average seating capacity per departure, and supports the more efficient use of the Corporation's network and hubs.

In addition, a cornerstone of the Corporation's strategy going forward will be the growth of its international operations. In order to support the expansion of these operations, Air Canada concluded agreements with Boeing for the acquisition of new widebody aircraft. The Corporation is scheduled to take delivery of these Boeing widebody aircraft starting in 2007. The Boeing order consists of 18 firm Boeing 777 aircraft and 14 firm Boeing 787 aircraft.

The Air Canada operating fleet at December 31, 2005 and the planned operating fleets for 2006 to 2008 are shown below:

	Number of Operating Aircraft as at December 31, 2005	**Planned Operating Aircraft as at December 31, 2006**	**Planned Operating Aircraft as at December 31, 2007**	**Planned Operating Aircraft as at December 31, 2008**	**Planned Operating Aircraft based on Future Committed Aircraft net of Projected Aircraft Removals(5)**
Widebody Aircraft					
Airbus A340-300	10	10	9	6	—
Airbus A340-500	2	2	0	0	—
Airbus A330-300	8	8	8	8	—
Boeing 767-300 ER	33	32	32	32	33
Boeing 767-200/200ER	12	11	9	9	—
Boeing 777/ 200LR	0	0	3	12	12
Boeing 777-200F(3)	0	0	0	0	2
Boeing 777- 300ER(4)	0	0	5	5	5
Boeing 787(3)	0	0	0	0	14
Total Widebody Aircraft	65	63	66	72	66
Narrowbody Aircraft					
Airbus A321	10	10	10	8	7
Airbus A320	51	48	42	42	41
Airbus A319	48	45	43	43	45
CRJ-100 (1)	10	0	0	0	—
ERJ-190	3	20	44	45	45
ERJ-175	14	15	15	15	15
Total Narrowbody Aircraft	136	138	154	153	153
Total (Air Canada)(2)	201	201	220	225	219

(1) 15 Bombardier CRJ-100 were transferred from Air Canada's fleet to Jazz's fleet in 2005 and the remaining Bombardier 10 CRJ-100 are expected to be transferred by July 2006.
(2) In addition to operating aircraft, as at December 31, 2005, Air Canada had 10 widebody aircraft and 18 narrowbody aircraft that were parked.
(3) The following aircraft are scheduled to be delivered after 2008: two Boeing B777-200F (2009) and 14 Boeing 787 (2010/2011).
(4) Air Canada has entered into a letter of intent with an aircraft lessor for one Boeing 777-300ER which is due to be delivered in 2007.
(5) These aircraft changes are expected to be completed by 2011.

Boeing

In November 2005, Air Canada concluded agreements with The Boeing Company ("Boeing") for the acquisition of up to 36 Boeing 777 aircraft and up to 60 Boeing 787 Dreamliners. The agreements include firm orders for 18 Boeing 777 aircraft, plus purchase rights for an additional 18 aircraft, in a yet-to-be determined mix of the 777 family's newest models. Deliveries of the Boeing 777 aircraft are scheduled to commence in March 2007. Seven Boeing 777 aircraft are expected to be delivered in 2007, nine aircraft in 2008, and two aircraft in 2009. The agreements also include firm orders for 14 Boeing 787 Dreamliners, plus options and purchase rights for an additional 46 aircraft. Air Canada's first Boeing 787 aircraft is scheduled for delivery in 2010. As a result of the new committed Boeing 777 and 787 aircraft, the Corporation expects to eventually remove from operations all 20 Airbus A330 and A340 aircraft as well as all 12 Boeing 767-200 aircraft.

Embraer

In 2004, Air Canada signed a definitive purchase agreement with Empresa Brasileira de Aeronautica S.A. ("Embraer") covering firm orders for 45 Embraer 190 series aircraft as well as 15 Embraer 175 series aircraft. The purchase agreement also contains rights to exercise options for up to 60 additional Embraer 190 series aircraft as well as providing for conversion rights to other Embraer models.

Deliveries of the 15 Embraer 175 series aircraft commenced in July 2005 and the last aircraft was delivered in January 2006. As of the date hereof, Air Canada had received six 93-seat ERJ 190 aircraft. Thirty-nine additional Embraer ERJ 190 aircraft under firm order are scheduled for delivery during the remainder of 2006 and during 2007.

Description of Aircraft

Widebody Aircraft

At December 31, 2005, Air Canada's operating widebody fleet comprised 65 aircraft, configured in two classes of service: Executive First or Executive Class, and Hospitality Service. The Airbus A340-300 is a four-engine 285-286-seat aircraft that serves Air Canada's trans-Pacific and trans-Atlantic routes. The Airbus A340-500 aircraft, with 267 seats, is a longer range aircraft than the A340-300 which currently serves Air Canada's Toronto-Hong Kong route on a non-stop basis. The Airbus A330-300 aircraft, with 274 seats, is a twin-engine variant of the Airbus A340-300 that Air Canada operates mainly on trans-Atlantic routes. The Boeing 767-300 ER is a long-range 203-222-seat aircraft used mainly on international routes. The Boeing 767-200 is a 207-seat aircraft used on domestic and international routes.

Narrowbody and Regional Jet Aircraft

At December 31, 2005, Air Canada operated 136 narrowbody aircraft, including 109 Airbus narrowbody aircraft. These aircraft are configured in two classes of service: Executive Class and Hospitality Service (except for the 10 remaining Bombardier regional jets (see Jazz Fleet section), which are only configured in Hospitality Service). The Airbus A320 aircraft is a 140-seat, twin-engine aircraft. The twin-engine Airbus A319 offers 120 seats and is essentially a shortened version of the Airbus A320 aircraft, with the same engines, operating systems and flight deck. The twin-engine Airbus A321 is the largest narrowbody aircraft in the Airbus family, with 166 seats. The Embraer 190 and 175 aircraft are 93-seat and 73-seat aircraft with twin-engines. These large regional jets have lower trip operating costs than conventional narrowbody aircraft. All of these narrowbody aircraft types primarily serve Air Canada's domestic and transborder routes.

Trademarks

The following are some of the key trademarks owned by the Corporation: Air Canada Jetz®, Air Canada Jazz™, Jazz™, Destina.ca®, Acetek™, Air Canada Vacations®, Vacances Air Canada®, EnRoute®, Executive First®, Executive Class®, Expedair®, AC Expedair™, AC Priority™, AC Air Freight™, AC Lynx®, Hospitality Service®, Service Hospitalité®, Rapidair®, Maple Leaf™, Feuille d' Érable™, AC WEBSAVER™, Super Elite™ and Super Élite™. Star Alliance® is a trademark of the Corporation and of other members of the Star Alliance® group.

Other Businesses

Cargo Services

AC Cargo LP and Air Canada provide Cargo Services on domestic, transborder and international passenger flights and with dedicated all-cargo freighter aircraft. AC Cargo LP and Air Canada are Canada's largest providers of air cargo services as measured by cargo capacity. AC Cargo LP offers Cargo Services on domestic and transborder flights, utilizing the cargo capacity on aircraft operated by Air Canada and Jazz on domestic and transborder routes. Air Canada offers Cargo Services on its international passenger flights and also uses chartered all freighter aircraft for Canada-Europe and Canada-Asia services. Cargo Services offered by AC Cargo LP and Air Canada include services for high priority shipments (AC Expedair and AC Priority) and air freight services (AC Air Freight) to Air Canada destinations worldwide and Jazz destinations in North America. Combined, AC Cargo LP and Air Canada provide direct Cargo Services to over 200 Canadian and international destinations and have sales representatives in over 50 countries.

Air Canada's cargo terminal at Pearson International Airport is equipped with modern cargo handling technology to ensure efficient cargo handling to meet the needs of customers. Air Canada and AC Cargo LP together are one of the largest suppliers of air cargo services to Canada Post Corporation.

Air Canada's freight management system, AC Lynx, offers the visibility and tools needed to track cargo on-line from initial booking to delivery. Air Canada, United Airlines and Northwest Airlines, in cooperation with Unisys, are the founding carriers of the new Cargo Portal Service introduced in 2003. Endorsed by key freight forwarders globally and their industry associations, this portal represents a one-stop-shop web tool for air cargo shipping requirements by offering a large number of services on a growing number of major air carriers.

Destina eCommerce Group LP

Destina eCommerce Group LP owns the Destina.ca online travel site and provides the Internet technology platform that supports the on-line travel site. In addition, Destina eCommerce Group LP contributes to the development of Air Canada's on-line distribution strategy and forms an integral part of the airline's effort to grow its commercial websites worldwide. Destina eCommerce Group LP's mandate also includes managing and providing operational and technical support for all of Air Canada's commercial websites, providing travel industry partners with on-line tools for direct booking, and implementing and managing future corporate direct booking tools.

A corporate reorganization involving Destina eCommerce Group LP is scheduled to occur on May 1, 2006. Pursuant to such corporate reorganization, it is currently contemplated that the assets of Destina eCommerce Group LP related to the hotel and car rental booking business previously conducted by it, as well as its shares in NetTel Assistance Inc. will be transferred to Destina eCommerce Group General Partner Inc. All other assets and all liabilities of Destina eCommerce Group LP will be assigned to and assumed by Air Canada.

Touram LP / Air Canada Vacations

Touram LP conducts business under the trade names Air Canada Vacations. Air Canada Vacations is a major Canadian tour operator, offering a variety of leisure vacation package options which include air transportation supplied by Air Canada and its Star Alliance® partners, hotel accommodations, cruises, Aeroplan Miles and airport transfer/car rentals to popular destinations for Canadians in the Caribbean, Asia, Central and South America and the United States, including Las Vegas, Florida and Hawaii. Air Canada Vacations customers benefit from access to the Star Alliance® network as well as the Air Canada network.

Netair, a national consolidator that sells surplus seat inventory aboard Air Canada exclusively to travel agents, is another division of Touram LP.

Ground Handling Services

ACGHS LP (and its United States subsidiary, ACGHS US Inc.) and Air Canada provide Ground Handling Services to numerous airlines, including major foreign airlines at Canadian and international airports. These services include passenger check-in, gate management, baggage and cargo handling and processing, as well as aircraft ramp services.

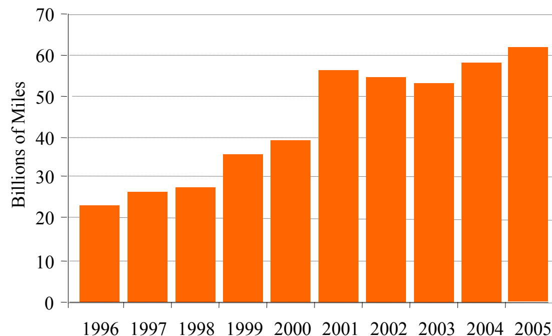
AEROPLAN

ACE currently holds a 75.5% ownership interest in Aeroplan, Canada's premier loyalty program. Aeroplan provides its commercial partners with loyalty marketing services to attract and retain customers and stimulate demand for these partners' products and services. Aeroplan's objective is to offer its commercial partners superior value relative to other marketing alternatives through access to Aeroplan's base of members and the design and execution of marketing programs aimed at increasing revenue, market share, and customer loyalty. The Aeroplan Program is one of Canada's longest standing loyalty programs. It was founded in 1984 by Air Canada, to manage the airline's frequent flyer program. Aeroplan benefits from its unique strategic relationship with Air Canada in addition to its contractual arrangements with leading commercial partners including Amex Bank of Canada ("AMEX"), Bell Canada, Canadian Imperial Bank of Commerce ("CIBC"), Best Buy Canada Ltd., which operates the Future Shop stores in Canada ("Future Shop"), Imperial Oil (Esso), Star Alliance® member airlines and numerous hotel chains and car rental companies.

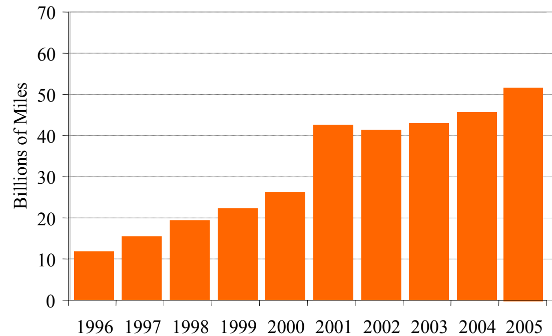
Aeroplan offers its approximately five million active members the ability to accumulate Aeroplan Miles throughout its partner network through purchases of products and services. Aeroplan sells Aeroplan Miles to its extensive network of over 60 commercial partners, representing over 100 brands, in the financial services, travel services and consumer products and services industries. Today, financial services partners generate the majority of Aeroplan's revenues. In 2005, over 62 billion Aeroplan Miles were accumulated by members representing an equivalent of approximately $40 billion in consumer spending to earn these Aeroplan Miles. Once members have accumulated a sufficient number of Aeroplan Miles, they can redeem such Aeroplan Miles for air travel and other attractive rewards. Upon the redemption of Aeroplan Miles by its members, Aeroplan incurs the cost to acquire the desired reward.

The following charts illustrate the number of Aeroplan Miles issued and redeemed on an annual basis for the last ten years. The increase in 2001 reflects the integration of Canadian Airlines' frequent flyer program, Canadian Plus, with the Aeroplan Program. In addition, the charts include 103 billion of the Aeroplan Miles that were earned by members prior to January 1, 2002, for which the responsibility to provide air rewards rests with Air Canada.

Annual Number of Aeroplan Miles Issued



Annual Number of Aeroplan Miles Redeemed



Aeroplan's Business Model

In general terms, Aeroplan's business is based on two major streams of activity: (i) the sale of Aeroplan Miles and marketing services to Aeroplan's commercial partners; and (ii) delivering rewards to Aeroplan's members.

Sale of Aeroplan Miles and Marketing Services to Partners

Aeroplan derives its revenues from the sale of Aeroplan Miles and marketing services to its commercial partners. The marketing services consist primarily of advertising, promotion and data analysis. In addition, Aeroplan derives service fees for managing Air Canada's tier membership program for its most frequent flyers.

Members accumulate Aeroplan Miles through their purchase of products and services from an extensive network of over 60 commercial partners, representing over 100 brands, in the airline, car rental, consumer products and services, entertainment, financial services, hotel and telecommunication industries.

The gross proceeds received by Aeroplan at the time of the sale of Aeroplan Miles to its partners, known as "gross billings", are deferred and recognized by Aeroplan as revenue upon the redemption of Aeroplan Miles for GAAP purposes, except for breakage as described below. Upon the redemption of Aeroplan Miles, Aeroplan purchases airline seats or other products or services in order to deliver the reward chosen by the member. At such time, Aeroplan incurs and recognizes an expense equal to the cost of the reward, and the deferred revenue related to the Aeroplan Miles being redeemed is recognized by Aeroplan as earned revenue from the sale of Aeroplan Miles for GAAP purposes. The other significant expenses incurred by Aeroplan include call centre expenses and selling and administrative expenses.

Based upon past experience, management of Aeroplan anticipates that a number of Aeroplan Miles sold will never be redeemed by members. This is known as "breakage" and is presently estimated by management of Aeroplan to be 17% of current Aeroplan Miles sold. This estimate is supported by two independent studies conducted in 2004 on behalf of Aeroplan. Prior to 2004, breakage was estimated to be 19% of the Aeroplan Miles sold. For those Aeroplan Miles that Aeroplan has estimated will never be redeemed by members, Aeroplan recognizes revenue on a straight-line basis over the average time between the issuance and redemption of an Aeroplan Mile, referred to as the estimated life of an Aeroplan Mile, currently 30 months.

Management of Aeroplan believes that the issuance and redemption of Aeroplan Miles are influenced by the nature and volume of commercial partners, the types of rewards offered, the general economic activity level and the activity level of competing loyalty marketing programs. These influences could affect redemption and breakage rates. As of December 31, 2005, Aeroplan had approximately $1.3 billion in deferred revenue that will be recognized for GAAP purposes in the future upon the redemption of outstanding unredeemed Aeroplan Miles.

On an ongoing basis, the total estimated redemption cost for outstanding Aeroplan Miles is determined by Aeroplan as the product of (i) total outstanding number of unredeemed Aeroplan Miles on a specific measurement date net of estimated breakage, and (ii) the average unit cost per Aeroplan Mile redeemed in the period. Given that the future unit cost per Aeroplan Mile redeemed may fluctuate, the future redemption cost liability is periodically reevaluated using the average unit cost per Aeroplan Mile redeemed in the most recent period.

Service fees are charged for the sale of marketing services to Aeroplan's partners and for the management of Air Canada's frequent flyer tier membership program. In addition, Aeroplan collects various fees that may be charged to members upon redemption of Aeroplan Miles, including booking, service and administrative fees.

Redemption Rewards

Once members have accumulated a sufficient number of Aeroplan Miles, members are entitled to redeem their Aeroplan Miles from Aeroplan's reward portfolio. Initially, these rewards were restricted to air travel. Beginning in 2003, Aeroplan made a strategic shift to expand the reward portfolio in order to directly respond to all key areas of interest of the membership. By 2005, in addition to air travel on Air Canada, Jazz and the Star Alliance® carriers, the reward portfolio now includes worldwide car and hotel rewards, a broad selection of brand

name merchandise, unique experiential rewards, electronics from Future Shop, and gift cards from a network of over 20 well known national retailers such as Gap, The Body Shop, Holt Renfrew, Pier One, Blockbuster, Williams-Sonoma, Pottery Barn, Linens ‘n Things, Birks and The Running Room. Member response has been consistently positive to the increasing choice and value the new rewards offer, and demand for these rewards has increased significantly each year since 2003.

Air travel remains the most popular reward among members, representing approximately 90% of all rewards claimed by Aeroplan members in 2005. Aeroplan has issued nearly ten million air travel rewards over the last ten years, and over 1.3 million in 2005 alone.

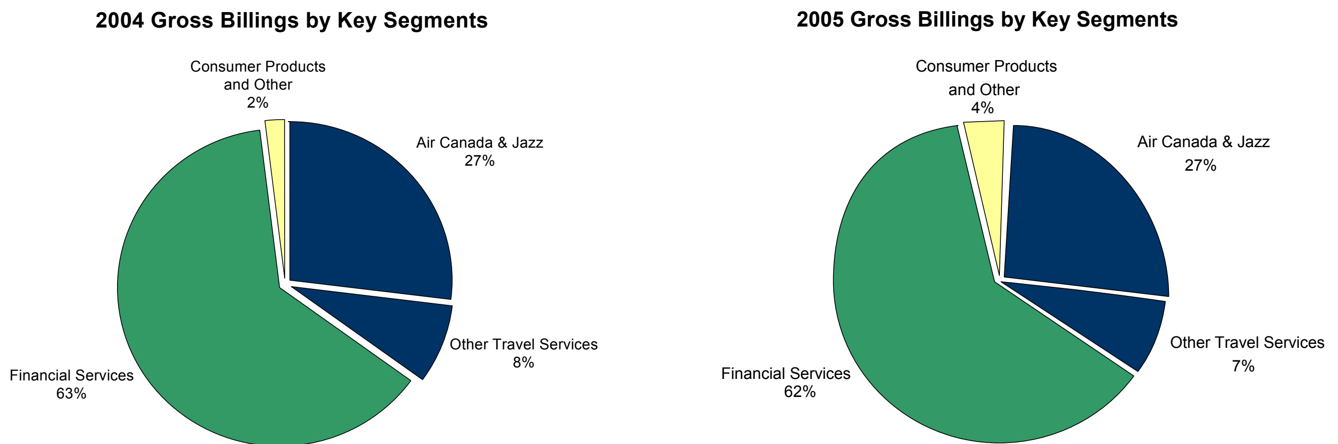
Commercial Partners

Aeroplan attracts and retains commercial partners based on the value of its member base as a target market, the loyalty demonstrated by Aeroplan members with their sustained purchases of partners' products and services, and a portfolio of value-added marketing services.

Today, Aeroplan has commercial relationships with over 60 leading companies, representing over 100 brands, which can be divided into three main categories:

- financial services partners;
- travel services partners; and
- consumer products and services partners.

The charts below illustrate gross billings in 2004 and 2005 from the sale of Aeroplan Miles by category of partners.



Redemption Rewards

Once members have accumulated a sufficient number of Aeroplan Miles, members are entitled to redeem their Aeroplan Miles from Aeroplan's reward portfolio, which includes air travel, car rentals, hotel stays, vacation packages, brand name merchandise, gift certificates, and unique experiential rewards.

Airline Seat Rewards

Aeroplan has entered into long-term agreements for the purchase of airline seat capacity with Air Canada and many of the other Star Alliance® member airlines. Such agreements enable Aeroplan to offer its members access to an extensive and worldwide source of airline travel rewards. In 2005, approximately 90% of rewards claimed by Aeroplan members were air travel rewards.

Prior to 2004, 10% of the seat capacity on AC Flights (as defined below) was allocated for Aeroplan rewards. Since April 2004, such allocation has been increased to a total of 15% of the capacity on flights operated by Air Canada and its affiliate, Jazz, and certain other air carriers under the "AC" code (collectively, the "AC Flights"), 8% of which is at a fixed low redemption cost and the balance of 7% is at a higher fixed redemption cost. The rates charged for such seat capacity are fixed through the end of 2007. Thereafter, any upwards or downwards adjustments to such rates must maintain aggregate discounts at least as favourable to Aeroplan as those set out in the current rates. The adjustments are also based on an identified set of parameters. Through recently completed arrangements with Air Canada to be implemented in 2006 or early 2007, Aeroplan will have access to unlimited seat capacity on AC Flights. Under the new arrangements, Aeroplan will continue to have access to 8% of the seat capacity at a fixed low redemption cost (subject to adjustments described above) and can purchase additional inventory based on published fares with a variable discount depending on the fare type. Any adjustments to this variable discount are based on an identified set of parameters. The CPSA (as defined below) also provides that Aeroplan will be charged the lowest fares charged to any other loyalty program and such fares will take into account Aeroplan's status as the largest consumer of Air Canada's seat inventory. These new arrangements will allow Aeroplan to provide its members with greater access to air travel rewards. To reflect the cost of the additional seats acquired, Aeroplan may adjust the number of Aeroplan Miles required to claim air travel rewards under the new arrangements.

Aeroplan also provides its members with access to an extensive and world-wide source of airline travel rewards through contractual arrangements between Aeroplan and the Star Alliance® member airlines, at competitive rates to Aeroplan. During the year ended December 31, 2005, Aeroplan members booked over 750,000 seats on Star Alliance® member airlines.

Other Travel Rewards

In October 2005, Aeroplan significantly expanded its portfolio of complementary travel rewards with the launch of a fully redesigned online redemption tool and the addition of seven new partner brands. Hotel rewards are now available worldwide from Delta Hotels, Sheraton Hotels & Resorts, Westin Hotels & Resorts, Four Points by Sheraton, W Hotels, St. Regis and The Luxury Collection. Rewards start at 9,000 Aeroplan Miles for a one-night hotel stay. Car rental rewards have been expanded to include Avis and Hertz locations around the world, and can be fully booked online at *www.aeroplan.com* using industry leading technology. Car rental rewards start at just 5,000 Aeroplan Miles for a one day rental. Also in 2005, and in conjunction with Air Canada Vacations, Aeroplan added various Disney resort packages to its wide variety of vacation packages available for reward redemption.

Indulgence Rewards

In 2005, Aeroplan regrouped all of its non-travel reward offerings under the Indulgence Rewards banner. A new consolidated online reward catalogue features over 300 rewards that include the latest in electronics from Future Shop, a broad selection of brand name merchandise, unique experiential rewards, and gift cards from a network of over 20 well known national retailers such as Gap, The Body Shop, Holt Renfrew, Pier One, Blockbuster, Williams-Sonoma, Pottery Barn, Linens ‘n Things, Birks and The Running Room.

This portfolio of rewards is the largest diversified group of rewards ever offered by Aeroplan and is one of the most extensive in the Canadian loyalty marketing sector. The portfolio is designed to directly respond to members' interests for reward opportunities, while ensuring broad affordability, with new rewards added every month. Rewards beyond air travel are available online only exclusively at *www.aeroplan.com*. Member response to the 2005 expansion of the reward portfolio and redesigned user experience has been consistently positive, with the demand for these rewards having significantly increased compared to the previous year.

Members

Membership

Aeroplan has approximately five million active members, consisting of those members who have completed at least one transaction (either accumulating or redeeming an Aeroplan Mile) during the last three years.

Communications to Members

Regular communication with individual members through newsletters, monthly statements and periodic special mailings is a cornerstone of the Aeroplan Program. Subsequent to the completion of a study in 2003 and 2004 on the effectiveness of its member communications, Aeroplan's portfolio of member communications and its list of strategic suppliers were revised to offer members more choice in channels, more flexible tools and increased potential for highly targeted and relevant messages.

These changes to Aeroplan's communications strategies have resulted in significant cost and time savings. Nearly two million members now receive statements and other information from Aeroplan by electronic mail.

Operations

Member Segmentation and Data Analysis

Aeroplan develops member segmentation models using its members' purchasing behaviour data. The current model identifies six categories of members based on key behavioural indicators including flying patterns, accumulation sources and rate, tenure in the Aeroplan Program and other factors. The information emerging from the model drives Aeroplan's communications with its members which have become more relevant and meaningful to members. Aeroplan's capacity to provide targeted communications presents a value-added marketing tool to its commercial partners at competitive rates to alternative mass media.

Member Servicing and Distribution

Prior to 2002, Aeroplan rewards were exclusively distributed through call centres. Since then, other channels have been developed and distribution is now handled through a combination of call centres and Aeroplan's Internet site *www.aeroplan.com*. Aeroplan is introducing an automated speech platform which will improve self-service functionality. The introduction of the speech platform commenced in December 2005 and is expected to be fully implemented by the end of 2006. These channels provide Aeroplan with an effective distribution strategy that offers its members a variety of options when redeeming rewards.

Systems and Infrastructure

Aeroplan's technology organization consists of skilled individuals with strong business knowledge. While project management, systems analysis, strategy and architecture functions are performed internally, Aeroplan relies on external technology partners to perform systems operations and applications development. All systems and infrastructure are designed to safeguard and protect Aeroplan's members' data from unauthorized access, use or disclosure.

Long-Term Strategic Relationship with Air Canada

Aeroplan has a long-term strategic relationship with Air Canada, Canada's largest domestic and international full-service airline.

Management believes that Aeroplan's strategic relationship with Air Canada results in several competitive advantages to Aeroplan, including:

- an affiliation with the strong Air Canada brand;

- being Air Canada's exclusive loyalty marketing provider based in Canada;
- attractive rates for seat capacity on the Air Canada and Jazz networks based on Aeroplan's status as Air Canada's largest customer; and
- access to Air Canada's passengers for the purposes of acquiring new Aeroplan members.

Aeroplan is a party to the following five major agreements with Air Canada: (i) an Amended and Restated Commercial Participation and Services Agreement dated June 9, 2004, as amended, including by the agreements dated May 13, 2005 (the "CPSA"); (ii) a Database Agreement dated May 13, 2005, effective January 1, 2002; (iii) an Amended and Restated Master Services Agreement dated May 13, 2005, effective January 1, 2005; (iv) a General Services Agreement dated May 13, 2005, effective January 1, 2005; and (v) a Trademark License Agreement dated May 13, 2005. A full description of these agreements appears under the heading "The Aeroplan Business - Long-Term Strategic Relationship with Air Canada" in the 2006 Annual Information Form of Aeroplan Income Fund. The 2006 Annual Information Form of Aeroplan Income Fund is available on SEDAR at *www.sedar.com*.

Competition

Aeroplan generally competes with other forms of marketing services, including advertising, promotions and other loyalty incentives, both traditional and on-line, for a portion of a client's total marketing budget. In addition, Aeroplan competes against proprietary loyalty programs developed by Aeroplan's existing and potential commercial partners. Aeroplan's principal competitors in Canada include the Air Miles™ program, frequent flyer programs operated by airlines and the loyalty programs operated by consumer products and services retailers, financial services institutions and gasoline retailers.

For each of Aeroplan's marketing services, Aeroplan expects competition to intensify as more competitors enter its market. In addition, competitors of the Aeroplan Program may target its commercial partners and members as well as draw rewards from Aeroplan's redemption rewards suppliers. Aeroplan's ability to generate revenue from commercial partners will depend on its ability to differentiate itself through the products and services it offers and the attractiveness of its Aeroplan Program to consumers. The continued attractiveness of the Aeroplan Program will depend in large part on its ability to remain affiliated with commercial partners that are valuable to consumers and to offer rewards that are both attainable and attractive to consumers. Intensifying competition will make it more difficult for Aeroplan to accomplish this. For Aeroplan's database marketing services, its ability to continue to capture detailed transaction data on consumers is critical in providing effective customer relationship management strategies for Aeroplan's commercial partners.

Logos and Trademarks

Aeroplan®, Aéroplan®, Aeroplan Design®, Aéroplan Design®, AeroCorporate®, AéroEntreprise®, Aeroplan Plus®, Aerogold® and Aéro Or® are registered trademarks owned by Aeroplan in Canada. Aeroplan also owns additional trademarks in connection with its loyalty marketing business. Air Canada has granted Aeroplan LP a license to use the Air Canada® and Air Canada Roundel® trademarks around the world solely in association with the Aeroplan Program. Aeroplan Income Fund has been granted a license to use the Aeroplan®, Aéroplan®, Aeroplan Design® and Aéroplan Design® trademarks in Canada.

Aeroplan's intangible assets are an important part of its business. Aeroplan benefits from the goodwill established for the Aeroplan brand name. Aeroplan protects its proprietary information, including its trademarks and database, through trademark laws, contractual provisions and confidentiality procedures. Employees, service providers and partners are contractually bound to protect Aeroplan's proprietary information in order to control access to and the distribution of any such information.

JAZZ

Jazz forms an integral part of Air Canada's domestic and transborder market presence and strategy. Under the CPA with Air Canada, Jazz provides service to and from lower density markets as well as higher density markets at off-peak times throughout Canada and to and from certain destinations in the United States.

Jazz is the focal point of Air Canada's regional passenger strategy, providing Air Canada with approximately 96% of its regional airline capacity based on ASMs. Jazz and Air Canada have linked their regional and mainline networks in order to serve connecting passengers more efficiently and to provide valuable traffic feed to Air Canada's mainline routes. Jazz's operations also complement Air Canada's operations by allowing more frequent service in lower density markets than could be provided economically with conventional large jet aircraft.

Jazz's business model was transformed upon the emergence of Air Canada and Jazz from the CCAA by virtue of the implementation of significant cost reductions, the introduction of new regional jet aircraft and the entering into of the Initial CPA which was in effect from September 30, 2004 to December 31, 2005. The Initial CPA was replaced with the CPA effective January 1, 2006 between Air Canada and Jazz.

Capacity Purchase Agreement with Air Canada

Pursuant to the CPA, Air Canada purchases capacity from Jazz on Jazz's aircraft which are subject to the CPA (the "Covered Aircraft") in consideration for the payment of certain fees by Air Canada to Jazz. During the period from October 1, 2004 to December 31, 2005, Jazz derived substantially all of its revenues (99%) from the Initial CPA. Management expects this to continue under the CPA.

All of the 121 aircraft in Jazz's operating fleet as of December 31, 2005 are Covered Aircraft under the CPA except for one Dash 8-100 aircraft being used for charter purposes. Of the 135 aircraft scheduled to make up Jazz's operating fleet by July 2006, 133 aircraft will be Covered Aircraft under the CPA and the remaining two aircraft (Dash 8s) are scheduled to be used for third party charter purposes. Pursuant to the CPA, Air Canada purchases capacity from Jazz representing substantially all of the capacity of the Covered Aircraft. In addition, the current 2006 – 2008 high level operating plan provided by Air Canada to Jazz for rate setting purposes only (the "2006 – 2008 High Level Operating Plan") provides for Air Canada to continue to purchase substantially all of the capacity of the Covered Aircraft for such period. The 2006 – 2008 High Level Operating Plan is subject to annual and seasonal (twice-a-year) revisions.

Notwithstanding any revisions to the 2006 – 2008 High Level Operating Plan, Air Canada has agreed to pay Jazz for certain daily minimum levels of operating capacity based on aircraft type and calculated in terms of a minimum number of minutes elapsing from the time the chocks are removed from the wheels of an aircraft until the chocks are next again returned to the wheels of the aircraft, divided by 60 (the "Block Hours") for each Covered Aircraft other than aircraft being modified, undergoing schedule maintenance or being painted (the "Active Aircraft") until the expiry of the CPA in December 2015. The minimum average daily utilization guarantee for the 2006 calendar year represents approximately 86% of the estimated Block Hours currently scheduled to be flown by Jazz's Covered Aircraft during such period, as contemplated in the 2006 annual operating plan provided by Air Canada to Jazz for budget and planning purposes only (the "2006 Annual Operating Plan").

Under the CPA, Jazz operates flights on behalf of Air Canada using the Covered Aircraft, and provides all crews (flight and cabin), aircraft maintenance and, in some cases, airport operations for such flights (the "Scheduled Flights"). Air Canada determines routes and controls scheduling, ticket prices, product distribution, seat inventories, marketing and advertising for these flights. Air Canada is entitled to all revenues (except bar and buy-on board sales) resulting from the Scheduled Flights and from cargo services carried on Scheduled Flights including, without limitation, ticket sales, baggage charges, passenger charges and employee pass travel service charges.

In addition to being reimbursed for all pass-through costs, as defined in the CPA, Jazz is paid fees by Air Canada on a variety of different metrics based on an estimate of all costs and expenses to be incurred and paid by Jazz for the applicable period with respect to Scheduled Flights and other services to aircraft, other than Jazz's pass-through costs (the "Controllable Costs"), marked-up by a specified percentage. Such mark-up equates to a specified margin on Jazz's estimated Scheduled Flights Revenue (as defined in the CPA) for each calendar year in the

applicable period. The fees payable by Air Canada to Jazz on a monthly basis are broken down into a number of categories. These payment categories fall into two broad groups: there are those that are variable depending on the Covered Aircraft utilization and those that remain unchanged regardless of how often or where or with what load factors the Covered Aircraft are utilized.

The most important of the variable payments for establishing Jazz's revenue is the Block Hour payment paid by Air Canada for each Block Hour flown by Jazz's Covered Aircraft. This payment varies with the Block Hours flown. The other variable payments such as the cycle payment and, even more so, the passenger payment, are relatively small and calibrated to cover the specific costs associated with the activity (either a cycle or flying a passenger) to which they are linked. The other group of payments such as aircraft rent do not change regardless of the Covered Aircraft's utilization and are designed to meet Jazz's costs for these items plus a mark-up.

Scope Clause

Scope clauses are an industry norm for network airlines operating in conjunction with regional carriers and are usually found in collective agreements of pilot union groups. Jazz, like many regional airlines, is restricted by scope provisions in the collective agreement between Air Canada and the Air Canada Pilots Association ("ACPA"). Prior to the CCAA restructuring, Jazz's operations were limited by scope provisions restricting Jazz's operations to 39 55-seat regional jet aircraft including ten grandfathered BAe-146 aircraft, which have since been retired. The scope provisions in place at the time also required that growth beyond the 39 55-seat regional jet aircraft could only take place with growth in the Air Canada fleet.

As a result of the CCAA process, a unique arrangement was reached between Air Canada, Jazz, ACPA and the Air Line Pilots Association ("ALPA"). The agreement, known as the Small Jets Settlement Agreement, modifies the existing scope clauses, provides a process to allocate the current orders of regional jets between Air Canada and Jazz, determines the types and number of jets that can be flown by Jazz and provides mechanisms for resolving disputes over future regional jet additions to either fleet. There are no limits to the number of turboprop aircraft that Jazz may operate.

The Small Jets Settlement Agreement provides that:

(i) Jazz may maintain a fleet of 50 CRJ-100s/200s and 15 CRJ-705s made up as follows: (i) ten CRJ-100s, 15 CRJ-200s and 15 CRJ-705s, and (ii) 25 CRJ-100s originally operated by Air Canada, of which 15 have already been transferred to Jazz as of December 31, 2005, with the remaining ten expected to be transferred by July 2006.

(ii) If either Air Canada or Jazz seeks to increase the fleet beyond what is outlined above, they must notify ACPA and ALPA in writing of the proposed increase and then meet with ACPA and ALPA to discuss and, if possible, agree on the increase and any terms in connection therewith. Where no agreement is reached, the matter is referred to an arbitrator or a mediator who will then make a decision, taking into account the business case put forward by the respective parties and the impact of the matter at hand on the respective pilots groups.

(iii) Jazz may not operate the CRJ-705 aircraft if configured in excess of 75 seats, inclusive of all classes.

(iv) As was previously the case, Air Canada must ensure that a minimum of ASMs is flown by Air Canada compared to the ASMs flown by Jazz.

Air Canada is scheduled to transfer to Jazz 25 CRJ-100s originally operated by Air Canada, of which 15 have already been transferred to Jazz as of December 31, 2005, and the remaining ten by July 2006. ACPA has filed a grievance under its collective agreement with Air Canada challenging the timing of the transfer of such 25 CRJ-100s from Air Canada to Jazz prior to the inclusion of the Embraer ERJ-190 aircraft into the Air Canada fleet which commenced in December 2005. Air Canada has informed ACPA that it believes that this matter should be resolved through binding arbitration under the Small Jets Settlement Agreement. Although the outcome of the arbitration or the grievance resolution procedure cannot be determined with certainty, based on previous arbitrations relating to the deployment of aircraft at Jazz, Management of Jazz expects that the current schedule for the transfer of the 25 CRJ-100s should not be affected.

Competition

As Canada's only nationwide regional airline and as the only regional carrier in Canada operating regional jets, Jazz enjoys a unique position in the Canadian regional airline market. All other carriers in the Canadian regional airline market are smaller operators of turboprop aircraft, most of which operate aircraft in the 19 to 50 seats range. These carriers are primarily stand-alone operations, operating in niche markets. Few other regional airlines in Canada operate under capacity purchase agreements, and those who do have relationships with Air Canada for turboprop aircraft with less than 19 seats. All of these carriers are privately held or family-run companies. None of these carriers approach the size and scope of operation of Jazz as their fleets range from one to 12 aircraft. Low-cost carriers, including WestJet and Canjet, also compete with Air Canada on certain routes in Canada operated by Jazz.

On transborder markets, Air Canada and Jazz compete against a variety of United States network airlines and their regional carriers, most of whom operate under capacity purchase agreements with various major United States network airlines. These carriers operate under their capacity purchase agreement partner brands such as United Express, America West Express, US Airways Express, Continental Express, Northwest Airlink, Delta Connection, American Eagle and Horizon Airlines.

Jazz Fleet

The Jazz operating fleet at December 31, 2005 and the planned operating fleets for 2006 to 2008 are shown below:

	Number of Operating Aircraft as at December 31, 2005[4]	**Planned Operating Aircraft as at December 31, 2006**	**Planned Operating Aircraft as at December 31, 2007**	**Planned Operating Aircraft as at December 31, 2008**
CRJ-100/200[1][2][3]	42	58	58	58
CRJ 705	15	15	15	15
Dash-8-300	26	26	26	26
Dash-8-100	38	36	36	36
Total	121	135	135	135

(1) Excludes four aircraft which were delivered by December 31, 2005, but are not yet in active service and thus not shown as operating aircraft.

(2) 15 Bombardier CRJ-100 aircraft were transferred from Air Canada's fleet to Jazz's fleet in 2005 and the remaining 10 Bombardier CRJ-100 aircraft are expected to be transferred by July 2006.

(3) During 2005, Air Canada leased an additional eight CRJ-200 aircraft from an aircraft lessor. These aircraft were delivered to Jazz starting in 2005 and as the date hereof, Jazz has received all eight aircraft.

(4) As of March 1, 2006, Jazz had 129 operating aircraft and two aircraft which had been delivered to Jazz but were not yet in active service.

Bombardier

In 2004, Air Canada signed a definitive purchase agreement with Bombardier Inc. ("Bombardier") for the acquisition of regional jet aircraft. The agreement with Bombardier covered firm orders for 15 Bombardier CRJ705 and 15 Bombardier CRJ200 aircraft, all of which were delivered to the Corporation between late 2004 and January 2006. The agreement with Bombardier contains orders for 15 additional Bombardier CRJ200 aircraft which can be cancelled without penalty. The agreement also contains options for an additional 45 aircraft.

Description of Aircraft

Regional Jet and Turboprop Aircraft

At December 31, 2005, Jazz operated 57 regional jet aircraft and Air Canada operated 10 regional jet aircraft. The 50-seat Bombardier CRJ-100/200 is a twin engine regional jet aircraft designed to provide superior

performance and operating efficiencies for the regional airline industry. The 50-seat Bombardier CRJ-100/200 is used primarily to serve lower density markets on routes of less than 1,000 miles, and to serve larger markets at "off peak" times. These aircraft are also used in selected "point-to-point" markets, transborder markets, and to develop selected domestic markets. The 75-seat Bombardier CRJ-705 feature leather seats and are configured into 10 Executive Class seats and 65 Hospitality Class seats. The CRJ-705 is an economical aircraft due to its operational efficiencies and lower trip costs.

As at December 31, 2005, Jazz operated 64 Bombardier Dash-8 aircraft. The Dash 8-100 is a twin engine turboprop medium range aircraft with seating capacity of 37 passengers. The 50-seat Bombardier Dash 8-300 has advanced turboprop characteristics that approach those of a jet aircraft. Turboprop aircraft continue to serve certain segments of the Canadian domestic market more efficiently than regional or larger jet aircraft. On short-haul routes with lower traffic volumes, turboprops often present the most economical and efficient way to serve these markets. Compared with larger jet aircraft, the turboprop is more profitable to operate on shorter routes with low levels of passenger demand due to its generally lower break-even passenger load factor.

Trademarks

Air Canada has granted Jazz a license to use the Air Canada Jazz™, Jazz™, Air Canada®, Air Canada Design®, Air Canada and Design® and other trademarks in Canada and the United States in association with the provision of scheduled airline services in regions of Canada and across the Canada — United States border. Jazz also owns additional trademarks in connection with its regional airline business.

ACTS

ACTS LP is a full service MRO organization that competes on a global basis. ACTS LP offers the following MRO services in its portfolio:

1. Airframe services;
2. Engine and auxiliary power unit (APU) services;
3. Component services; and
4. Specialized services, including aircraft painting, cabin conversions and modifications, engineering, fleet management, non-destructive testing, regulatory compliance and airworthiness, supply chain management, technical training, technical records management, and technical publications.

The major maintenance facilities for ACTS LP are located in Montreal, Vancouver, Winnipeg and Toronto.

ACTS LP provides MRO services for Air Canada and other airline customers worldwide. ACTS LP has currently over 100 customers, including Air Canada, Department of National Defence, Delta Air Lines, JetBlue Airways, Jazz, US Airways, Air Norterra, Air Transat, Chromalloy Gas Turbine, USA 3000, Skyservice Airlines, ABX Air, Hartford Aviation, Mexicana, Lufthansa CityLine, Snecma Services, Pratt & Whitney, British West Indies Airways (BWIA), Air France, KLM, United Airlines, and Comair.

In addition, ACTS LP secured a new market niche of aircraft lessors, including GECAS (GE Capital Aviation Services), ILFC (International Lease Finance Corporation), and RBS (Royal Bank of Scotland).

ACTS LP has a highly skilled and experienced workforce. During CCAA, the restructuring process allowed ACTS LP to implement important labour costs reductions resulting from higher productivity, a rationalized workforce, and lower average salaries. ACTS LP has the ability to significantly increase its business volume with its current infrastructure and facilities. The Corporation's strategy is to continue to leverage ACTS LP's unused capacity by developing relationships with third party customers, especially American carriers that have recently started to outsource their maintenance work.

Increasingly, many airlines and leasing companies prefer to deal with a single MRO provider that has the expertise necessary to manage all of their MRO work, including airframe overhauls, component and engine repairs, and specialized services. ACTS LP is positioning itself to pursue a greater market share by profitably providing value-added full-service integrated maintenance solutions that offer continuous cost improvement to its airline customers.

During its first full year of operations in 2005, ACTS LP continued to focus on increasing its customer base and developing into a stand-alone MRO. During this period of growth, financial results were impacted due to greater than expected operational challenges relating to significant production capacity growth at ACTS's Montreal and Vancouver airframe maintenance centers. These operational challenges required the integration of additional staff and new customer processes.

ACTS LP's strategy going forward is centered on the following pillars:

(i) Operational excellence: Implement systems and processes to provide agility and flexibility to meet customer demands.

(ii) Profitability: ACTS LP is continuing to develop its profitable business model to reduce costs and generate cash while focusing on its operations, turnaround times, productivity, processes, and systems.

(iii) Growth: Establish a greater global presence through possible partnerships, joint ventures, or acquisitions.

(iv) Customer Experience: Become a "virtual extension of the customers" by delivering products and services that consistently exceed expectations and ensure satisfaction and loyalty.

(v) Safety, Quality, and Reliability: Continuously strive to improve safety, quality, and reliability in the workplace.

EMPLOYEES

In 2003 and 2004, the Corporation concluded long-term collective agreements with all union groups which expire in 2009. These collective agreements provide for a process to revise wage levels in 2006 by negotiation or, failing negotiation, by mediation or arbitration without resort to strike or lock-out.

With respect to non-unionized employees, workforce reductions occurred in some areas in 2005 and 2006. Further non-unionized reductions have been announced and are planned to occur in 2006.

In the fourth quarter of 2005, the Corporation had an average of 33,090 full-time equivalent ("FTE") employees compared to an average of 31,991 FTE employees in the fourth quarter of 2004. This reflects a 3% increase from the fourth quarter of 2004, as shown in the table below:

	Union	Fourth Quarter 2005	Fourth Quarter 2004	Change	% Change
Transportation Services					
Management & Administrative Support		3,565	3,523	42	1
Pilots	ACPA	2,541	2,563	(22)	(1)
Flight Attendants	CUPE	6,010	5,837	173	3
Customer sales & Service Agents	CAW / IBT	3,927	3,942	(15)	(0)
Technical Services, Ramp & Cargo	IAMAW	6,924	6,775	149	2
UK Unionized employees	AMICUS / TGWU	682	749	(67)	(9)
Other unionized		528	494	34	7
Transportation Services total (1)		24,177	23,883	294	1
Aeroplan		1,057	1,185	(128)	(11)
Jazz(2)		3,801	3,363	438	13
ACTS LP		4,055	3,560	495	14
Total		33,090	31,991	1,099	3

(1) Transportation Services includes the following FTEs: Air Canada 15,414; AC Cargo LP 1,223; ACGHS LP 7,038; Air Canada Vacations 441; Other 61.

(2) Includes unionized and non-unionized employees.

RISK FACTORS

A discussion of risks affecting the Corporation and its business appears under the heading "Risk Factors" in the 2005 Management's Discussion and Analysis of ACE which is incorporated by reference herein. The 2005 Management's Discussion and Analysis is available on SEDAR at *www.sedar.com*.

MARKET FOR SECURITIES

The Variable Voting Shares and the Voting Shares are traded on the Toronto Stock Exchange under the trading symbols "ACE.RV" and "ACE.B", respectively. On May 8, 2006, the trading symbol for the Variable Voting Shares is expected to be changed from ACE.RV to ACE.A. The following table sets forth the price range and trading volume of the Variable Voting Shares and the Voting Shares as reported by the Toronto Stock Exchange for the months of January to, and including, December 2005:

	Variable Voting Shares				Voting Shares			
2005	High	Low	Average Daily Trading Volume	Total Monthly Volume	High	Low	Average Daily Trading Volume	Total Monthly Volume
January	$36.41	$32.10	710,057	14,201,149	$36.50	$32.10	90,607	1,812,130
February	$35.50	$32.10	249,484	4,989,675	$35.52	$32.25	103,437	2,068,734
March	$38.50	$31.25	1,189,653	26,172,368	$38.83	$31.25	219,651	4,832,331
April	$38.78	$33.90	758,670	15,932,076	$38.77	$34.00	139,252	2,924,291
May	$40.00	$33.00	1,097,700	23,051,710	$39.90	$33.00	126,400	2,654,406
June	$43.03	$37.90	1,270,907	27,959,964	$43.00	$37.85	198,734	4,372,149
July	$41.25	$37.76	603,348	12,066,958	$41.22	$37.80	161,186	3,223,717
August	$40.25	$35.70	627,562	13,806,369	$40.29	$35.66	109,538	2,409,838
September	$40.15	$34.02	918,105	19,280,204	$40.10	$34.00	235,536	4,946,250
October	$35.70	$30.25	675,806	13,516,113	$35.65	$30.29	141,324	2,826,476
November	$39.96	$30.81	1,200,059	26,401,298	$40.01	$30.85	601,866	13,241,041
December	$39.50	$36.60	413,394	8,267,874	$39.51	$36.45	137,286	2,745,721

The Notes are traded on the Toronto Stock Exchange under the trading symbol "ACE.NT.A". The following table sets forth the price range and trading volume of the Notes as reported by the Toronto Stock Exchange for the months of March to, and including, December 2005:

	Notes			
2005(1)	High	Low	Average Daily Trading Volume	Total Monthly Volume
March	$101.35	$100.65	252,810	252,810
April	$101.00	$96.70	24,102	506,150
May	$101.00	$93.50	8,292	174,122
June	$105.40	$98.47	16,701	367,430
July	$103.25	$99.00	5,279	105,570
August	$101.00	$98.00	10,797	237,530
September	$101.75	$95.50	13,008	273,170
October	$96.10	$90.99	3,213	64,250
November	$100.75	$93.00	9,895	217,700
December	$100.00	$96.67	7,391	147,810

(1) The Notes began trading on the Toronto Stock Exchange on March 31, 2005.

DIVIDEND RECORD

The Corporation has not paid dividends on its Voting Shares, Variable Voting Shares or Preferred Shares for the year ended December 31, 2005.

DESCRIPTION OF CAPITAL STRUCTURE

The share capital of ACE is composed of an unlimited number of Variable Voting Shares and Voting Shares and of 12,500,000 Preferred Shares. In addition, ACE has issued debt securities in the form of Notes. The following summary describes the rights, privileges, restrictions and conditions that are attached to the Variable Voting Shares, Voting Shares and Preferred Shares, and includes a description of the Notes and the ratings ascribed to them. This summary does not purport to be complete and is subject to, and is qualified in its entirety by, reference to the terms of the ACE Articles of Arrangement.

Variable Voting Shares

Voting

The holders of the Variable Voting Shares shall be entitled to receive notice of, and to attend and vote at, all meetings of the shareholders of ACE, except where the holders of a specified class are entitled to vote separately as a class as provided in the CBCA.

The Variable Voting Shares may be held only by persons who are not Canadians (as such term is defined in the *Canada Transportation Act*) and are entitled to one vote per Variable Voting Share unless (i) the number of Variable Voting Shares outstanding (including the Preferred Shares, on an as converted basis), as a percentage of the total number of votes attaching to Voting Shares outstanding exceeds 25% or (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares (including the Preferred Shares, on an as converted basis) at any meeting exceeds 25% of the total number of votes that may be cast at such meeting. If either of the above noted thresholds would otherwise be surpassed at any time, the vote attached to each Variable Voting Share will decrease proportionately such that (i) the Variable Voting Shares as a class (including the Preferred Shares on an as converted basis) do not carry more than 25% of the aggregate votes attached to all issued and outstanding voting shares of ACE and (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares (including the Preferred Shares on an as converted basis) at any meeting do not exceed 25 % of the votes that may be cast at such meeting.

Dividends

Subject to the rights, privileges, restrictions and conditions attaching to the shares of ACE of any other class ranking senior to the Variable Voting Shares, the holders of the Variable Voting Shares shall, at the discretion of the directors, be entitled to receive, out of monies, assets or property of ACE properly applicable to the payment of dividends, any dividends declared and payable by ACE on the Variable Voting Shares and the Variable Voting Shares shall rank equally as to dividends on a share for share basis with the Voting Shares and the Preferred Shares participating on an as converted basis. All dividends declared in any fiscal year of ACE shall be declared in equal or equivalent amounts per share on all Variable Voting Shares, Voting Shares and the Preferred Shares participating on an as converted basis at the time outstanding, without preference or distinction.

Subdivision or Consolidation

No subdivision or consolidation of the Variable Voting Shares or the Voting Shares shall occur unless, simultaneously, the shares of the other class are subdivided or consolidated in the same manner, so as to maintain and preserve the relative rights of the holders of the shares of each of the said classes.

Rights upon Liquidation, Dissolution or Winding Up

Subject to the rights, privileges, restrictions and conditions attaching to the shares of ACE ranking prior to the Variable Voting Shares, including the Preferred Shares, upon liquidation, dissolution or winding up of ACE or other distribution of ACE's assets among its shareholders for the purpose of winding up its affairs, the holders of the Variable Voting Shares and Voting Shares shall be entitled to receive the remaining property of ACE and shall be entitled to share equally, share for share, in all distributions of such assets.

Conversion

Each issued and outstanding Variable Voting Share shall be converted into one Voting Share, automatically and without any further act of ACE or of the holder, if (i) such Variable Voting Share becomes held, beneficially owned and controlled, directly or indirectly, otherwise than by way of security only, by a Canadian; or (ii) the provisions contained in the *Canada Transportation Act* relating to foreign ownership restrictions are repealed and not replaced with other similar provisions.

In the event that an offer is made to purchase Voting Shares and the offer is one which must, pursuant to applicable securities legislation or the rules of a stock exchange on which the Voting Shares are then listed, be made to all or substantially all the holders of the Voting Shares in a province of Canada to which the requirement applies, each Variable Voting Share shall become convertible at the option of the holder into one Voting Share that shall be subject to the offer at any time while the offer is in effect and until one day after the time prescribed by applicable securities legislation for the offeror to take up and pay for such shares as are to be acquired pursuant to the offer. The conversion right may only be exercised in respect of Variable Voting Shares for the purpose of depositing the resulting Voting Shares in response to the offer and the transfer agent shall deposit the resulting Voting Shares on behalf of the shareholder.

If the Voting Shares resulting from the conversion and deposited pursuant to the offer are withdrawn by the shareholder or are not taken up by the offeror or the offer is abandoned or withdrawn, the Voting Shares resulting from the conversion shall be reconverted automatically and without further act from ACE or the holder, into Variable Voting Shares.

There shall be no right to convert the Variable Voting Shares into Voting Shares or to convert Voting Shares into Variable Voting Shares, except in accordance with the conversion procedure set forth in the ACE Articles of Arrangement.

Constraints on Ownership of Shares

The Variable Voting Shares may only be held, beneficially owned or controlled, directly or indirectly, by persons who are not Canadians.

Voting Shares

Voting

The holders of the Voting Shares shall be entitled to receive notice of, and to attend and vote at, all meetings of the shareholders of ACE (except where the holders of a specified class are entitled to vote separately as a class as provided in the CBCA) and each Voting Share shall confer the right to one vote in person or by proxy at all meetings of shareholders of ACE.

Dividends

Subject to the rights, privileges, restrictions and conditions attaching to the shares of ACE of any other class ranking senior to the Voting Shares, the holders of the Voting Shares shall, at the discretion of the directors, be entitled to receive, out of monies, assets or property of ACE properly applicable to the payment of dividends, any dividends declared and payable by ACE on the Voting Shares and the Voting Shares shall rank equally as to

dividends on a share for share basis with the Variable Voting Shares and the Preferred Shares participating on an as converted basis and all dividends declared in any fiscal year of ACE shall be declared in equal or equivalent amounts per share on all Voting Shares, Variable Voting Shares and the Preferred Shares on an as converted basis at the time outstanding, without preference or distinction.

Subdivision or Consolidation

No subdivision or consolidation of the Voting Shares or the Variable Voting Shares shall occur unless, simultaneously, the shares of the other class are subdivided or consolidated in the same manner, so as to maintain and preserve the relative rights of the holders of the shares of each of the said classes.

Rights upon Liquidation, Dissolution or Winding Up

Subject to the rights, privileges, restrictions and conditions attaching to the shares of ACE ranking senior to the Voting Shares, including the Preferred Shares, upon liquidation, dissolution or winding up of ACE or other distribution of ACE's assets among its shareholders for the purpose of winding up its affairs, the holders of the Voting Shares and Variable Voting Shares shall be entitled to receive the remaining property of ACE and shall be entitled to share equally, share for share, in all distributions of such assets.

Conversion

Unless the foreign ownership restrictions of the *Canada Transportation Act* are repealed and not replaced with other similar restrictions, an issued and outstanding Voting Share shall be converted into one Variable Voting Share, automatically and without any further act of ACE or the holder, if such Voting Share becomes held, beneficially owned or controlled, directly or indirectly, otherwise than by way of security only, by a person who is not a Canadian.

Constraints on Ownership of Shares

The Voting Shares may only be held, beneficially owned and controlled, directly or indirectly, by Canadians.

Preferred Shares

Voting

The holders of Preferred Shares will be entitled to vote on an as converted basis with the Variable Voting Shares and the Voting Shares and to the extent that they are held by persons who are not Canadians they shall be subject to the same proportionate reduction in voting percentage as if, for voting purposes only, the Preferred Shares had been converted into Variable Voting Shares.

Participation

The holders of Preferred Shares shall participate on an as converted basis with the Variable Voting Shares and the Voting Shares with respect to all dividends, distributions, spin off, split-off, subscription rights or other offers or rights made available to holders of Variable Voting Shares and the Voting Shares and any other similar transactions.

Liquidation Preference

In the event of any liquidation, dissolution or winding up of ACE (with each holder of the Preferred Shares being entitled to treat the occurrence of a merger, amalgamation, sale of all or substantially all of the assets of ACE or other similar transaction involving a change in control of ACE as a liquidation for these purposes), then the holders of the Preferred Shares shall be entitled to receive, prior to and in preference to the holders of Variable Voting Shares and the Voting Shares, an amount per Preferred Share equal to the Fully Accreted Value of such

Preferred Shares, determined as of the date of such event. For the purposes of the terms of the Preferred Shares, "Fully Accreted Value" means, with respect to each Preferred Share issued on September 30, 2004 to the Cerberus Affiliate, as of any date, the initial purchase price of such Preferred Share, increased at a rate of 5% per annum, compounded semi annually from the date of issuance of such Preferred Shares.

Optional Conversion

The Preferred Shares shall be convertible at the option of the holders thereof at any time into Variable Voting Shares, if held by a non Canadian, or into Voting Shares, if held by a Canadian, at a conversion rate equal to the Fully Accreted Value per Preferred Share (as of the conversion date) divided by the Conversion Price. For the purposes of the terms of the Preferred Shares, "Conversion Price" is initially equal to 135% of the initial per share value attributed to the Variable Voting Shares and Voting Shares on September 30, 2004, being $20.00. The Conversion Price was adjusted automatically downward on the first anniversary of the date of issuance of the Preferred Shares to 130% of the subscription price, subject to (i) adjustment as described in "Mandatory Redemption/Conversion" below and (ii) customary public company anti-dilution protection for stock splits, stock dividends, subdivisions, combinations and similar transactions. There shall be no special adjustment for below market or below Conversion Price issuances.

Mandatory Redemption/Conversion

The holders of Preferred Shares shall be required to convert the Preferred Shares into Variable Voting Shares (if the Preferred Shares are not owned and controlled by a Canadian) or Voting Shares (if the Preferred Shares are owned and controlled by a Canadian), within 10 days after the seventh anniversary of the date of issuance of the Preferred Shares (the "Initial Mandatory Conversion Date") provided, however, that if the closing price of Variable Voting Shares or Voting Shares, as the case may be, does not exceed the Fully Accreted Value of a Preferred Share on at least 30 of the 100 trading days immediately prior to the Initial Mandatory Conversion Date then the holders thereof shall not be required to convert their Preferred Shares into Variable Voting Shares or Voting Shares, as the case may be, and on the Initial Mandatory Conversion Date the then applicable Conversion Price shall automatically be reduced by 3.75%.

In the event the Preferred Shares have not been converted on or prior to the Initial Mandatory Conversion Date, on each six month anniversary of the Initial Mandatory Conversion Date (each a "Subsequent Mandatory Conversion Date") until and including the 10 year anniversary of the date of issuance of the Preferred Shares (the "Final Maturity Date"), the Preferred Shares shall be subject to mandatory conversion within 10 days of any Subsequent Mandatory Conversion Date if, and only if, the closing price of Variable Voting Shares or Voting Shares, as the case may be, exceeds the Fully Accreted Value of a Preferred Share on at least 30 of the 100 trading days immediately prior to such Subsequent Mandatory Conversion Date and, if such threshold is not met, the then applicable Conversion Price shall automatically be reduced by an additional 3.75% on each such Subsequent Mandatory Conversion Date. If the foregoing test is not met with respect to the Subsequent Mandatory Conversion Date that is the Final Maturity Date, the holders of Preferred Shares shall have the right to require ACE to redeem each of the Preferred Shares in cash on the Final Maturity Date at a per share redemption price equal to the Fully Accreted Value (as at the Final Maturity Date).

Notwithstanding the foregoing, the Preferred Shares shall not be subject to mandatory conversion as described above unless the Variable Voting Shares and Voting Shares are then listed and posted on the Toronto Stock Exchange, and a registration statement, prospectus or similar offering document permitting the distribution and sale of such Variable Voting Shares and Voting Shares throughout Canada and/or the United States of America is then effective covering all of the Variable Voting Shares and Voting Shares into which the Preferred Shares are convertible at the time of such mandatory conversion.

Mandatory Conversion

If at any time during (i) the period commencing on the date of issuance of the Preferred Shares and ending on and including the first anniversary thereof the closing price of the Variable Voting Shares or Voting Shares, as the case may be, for each of 30 consecutive trading days exceeds 200% of the then applicable Conversion Price or (ii) any period after the first anniversary of the date of issuance of the Preferred Shares the closing price of the

Variable Voting Shares or Voting Shares, as the case may be, for each of 30 consecutive trading days exceeds 175% of the then applicable Conversion Price, and, in each case, if the Variable Voting Shares or Voting Shares are then listed and posted on the Toronto Stock Exchange and a registration statement, prospectus or other similar offering document permitting the distribution and sale of such Variable Voting Shares and Voting Shares throughout Canada and/or the United States of America is then effective covering all of the Variable Voting Shares and Voting Shares into which the Preferred Shares are convertible, then ACE may require the holders of Preferred Shares to convert the Preferred Shares into Variable Voting Shares, if the Preferred Shares are not owned by a Canadian, or Voting Shares, if the Preferred Shares are owned by a Canadian.

Organic Change

With respect to any recapitalization, reorganization, reclassification, consolidation, amalgamation, arrangement, merger, sale of all or substantially all of ACE's assets to another person or other transaction which is effected in such a way that holders of Variable Voting Shares and Voting Shares are entitled to receive (either directly or upon subsequent liquidation) stock, securities or assets with respect to or in exchange for Variable Voting Shares or Voting Shares, as the case may be (each an "Organic Change") which includes a sale of all or substantially all of ACE's assets or where ACE is not the surviving entity, the holders of the Preferred Shares shall be entitled to cause ACE to either (i) require that the surviving entity or its publicly traded parent issue to the holders of Preferred Shares in exchange for such shares, a security of the surviving or publicly traded parent entity evidenced by a written instrument substantially similar in form and substance to the Preferred Shares, including, without limitation, having the same economic rights and preferences as the Preferred Shares and having a rank senior to all capital stock of such issuing entity or (ii) make appropriate adjustments contemporaneously to the rights attached to the Preferred Shares so as to preserve in all respects the benefits conferred on the holders of the Preferred Shares by the terms of the Preferred Shares.

With respect to any reorganization, amalgamation, arrangement, merger or other similar transaction that does not constitute an Organic Change, appropriate adjustments shall contemporaneously be made to the rights (including, without limitation, the conversion right) attached to the Preferred Shares so as to preserve in all respects the benefits conferred on the holders of the Preferred Shares by the terms of the Preferred Shares.

Pre-emptive Rights

If ACE proposes to issue or sell any Variable Voting Shares or Voting Shares or other equity securities, rights, options, warrants or other convertible securities which represent rights to purchase Variable Voting Shares or Voting Shares, as the case may be, each holder of Preferred Shares shall be entitled to purchase a number of such Variable Voting Shares or Voting Shares, as the case may be, or other equity securities, rights, options, warrants or other convertible securities sufficient to allow such holder to maintain its proportionate equity ownership in ACE, on a fully diluted basis at the level of such interest immediately prior to such issuance or sale, subject to exceptions for issuances under management and employee stock incentive plans approved by the board of directors of ACE.

Notes

4.25% Convertible Senior Notes

ACE has an amount of $330 million long-term debt securities (the "Notes") issued and outstanding. The Notes are senior unsecured obligations of ACE and rank equally in right of payment to all other senior unsecured indebtedness of ACE and senior in right of payment to any subordinated indebtedness of ACE. The Notes are subordinated to all existing and future secured indebtedness of ACE. In addition, the Notes are effectively subordinated to all existing and future indebtedness and other liabilities and commitments of the subsidiaries of ACE.

Each Note is convertible at the option of the holder into Voting Shares (if the Notes are owned and controlled by a Canadian) or into Variable Voting Shares (if the Notes are not owned and controlled by a Canadian) at an initial conversion price of C$48.00 per Share, being an initial ratio of approximately 20.8333 Shares per $1,000 principal amount of Notes, subject to adjustment in certain events in accordance with the indenture

governing the Notes. On March 22, 2006, ACE announced that, following the special distribution of 0.18 units of Aeroplan Income Fund per Variable Voting Share, Voting Share and Preferred Share, the conversion ratio in effect immediately prior to the opening of business on March 22, 2006 is 22.2838 Shares for each $1,000 principal amount of Notes. Holders converting their Notes will not receive any payment upon conversion representing accrued but unpaid interest on such Notes. Subject to the satisfaction of certain conditions, ACE may, in lieu of delivering Voting Shares or Variable Voting Shares upon conversion of all or a portion of the Notes, elect to pay cash or a combination of cash and Voting Shares or Variable Voting Shares.

Ratings

Ratings generally address the ability of a company to repay principal and interest or dividends on securities. The Notes are rated by Dominion Bond Rating Service Limited ("DBRS").

This section describes the credit ratings that ACE has received for its Notes. These ratings provide investors with an independent measure of credit quality of an issue of securities. Each rating should be evaluated independently.

These ratings are not recommendations to purchase, hold or sell the Notes, or a comment on the market price or suitability for a particular investor. There is no assurance that any rating will remain in effect for any given period of time or that any rating will not be revised or withdrawn in the future by a rating agency.

The table below shows the range of credit ratings that DBRS assigns to long-term debt instruments.

Agency	**Highest Quality of Securities Rated**	**Lowest Quality of Securities Rated**
DBRS	AAA	D

The DBRS long-term debt rating scale indicates the risk that a company may not meet its obligations to pay interest and principal in a timely manner. Every DBRS rating is based on quantitative and qualitative considerations relevant to the borrowing entity.

ACE has received the following credit rating for the Notes it has issued.

Agency	**Long-Term Debt Credit Rating**
DBRS	B (high)

The DBRS B (high) rating on long-term debt rank 14th among the 26 long-term debt credit ratings given by DBRS. According to DBRS, a company with a long-term debt rated B is considered highly speculative and there is a reasonably high level of uncertainty as to the ability of the entity to pay interest and principal on a continuing basis in the future, especially in periods of economic recession or industry adversity.

ESCROWED SECURITIES

As of December 31, 2005, the Monitor appointed by the Court in connection with the restructuring of Air Canada and certain of its subsidiaries held 27,927 Variable Voting Shares in escrow, which amounted to 0.04% of the total outstanding Variable Voting Shares as at December 31, 2005. These Variable Voting Shares were released from escrow and distributed in accordance with the terms of the Plan. As of the date hereof, the Monitor appointed by the Court in connection with the restructuring of Air Canada and certain of its subsidiaries does not hold any Variable Voting Shares or Voting Shares in escrow.

DIRECTORS AND OFFICERS

Directors

The name, municipality of residence and principal occupation of each of the directors are, as of the date hereof, as set forth below. Such individuals have served as directors of ACE since the dates and hold the number of shares of ACE set forth opposite their respective names.

Name and Municipality of Residence	Principal Occupation	Director Since	Shares Held
Bernard Attali(4)(6) Paris, France	Country Advisor / Texas Pacific Group France	September 30, 2004	5,000(2)
Robert E. Brown(4)(5) Montreal, Québec	President and Chief Executive Officer CAE Inc.	September 30, 2004	10,000(1)
Carlton D. Donaway(4)(6) Redmond, Washington	Senior Advisor – Operations Cerberus Capital Management, L.P.	December 15, 2004	Nil
Michael M. Green(4)(6) Radnor, Pennsylvania	Managing Director and President-Operations Cerberus Capital Management, L.P.	September 30, 2004	Nil
W. Brett Ingersoll(3)(5) New York, New York	Managing Director Cerberus Capital Management, L.P.	September 30, 2004	Nil
Pierre Marc Johnson(4)(5) Montreal, Québec	Senior Counsel Heenan Blaikie LLP	September 30, 2004	5,000(1)
Richard H. McCoy(4)(5)(6) Toronto, Ontario	Corporate Director	August 3, 2005	4,000(1)
John T. McLennan(3)(6) Mahone Bay, Nova Scotia	Corporate Director	September 30, 2004	10,000(1)
Robert A. Milton Westmount, Québec	Chairman, President and Chief Executive Officer, ACE	June 29, 2004	24,336(1)
David I. Richardson(3)(5) Grafton, Ontario	Corporate Director	September 30, 2004	10,000(1)
Marvin Yontef (4) Toronto, Ontario	Senior Partner Stikeman Elliott LLP	June 29, 2004	5,000(1)

(1) Voting Shares.
(2) Variable Voting Shares.
(3) Member of the Audit, Finance and Risk Committee.
(4) Member of the Governance and Corporate Matters Committee.
(5) Member of the Human Resources and Compensation Committee.
(6) Member of the Nominating Committee.

Unless otherwise indicated below, each of the directors has held the occupation listed above for more than five years. Mr. Brown was Chairman of Air Canada from 2003 to 2004 and President and Chief Executive Officer of Bombardier from 1999 to 2002. Mr. Donaway was Executive Chairman of DHL Holdings USA from 2003 to 2004, Chairman, President and Chief Executive Officer of Airborne Inc. from 2002 to 2003 and President and Chief Executive Officer of ABX Air Inc. from 1992 to 2003. Mr. Ingersoll was a Partner at J.P. Morgan Partners from 1994 to 2002. Mr. McLennan was Vice Chairman and Chief Executive Officer of AT&T Canada (which was renamed Allstream Inc.) from 2000 to 2004. Mr. Richardson was Chairman, Ernst & Young Inc. and Senior Partner, Ernst & Young LLP (Canada) from 1987 to 2002.

The term of office of all of the above directors will expire at the next annual meeting of shareholders of ACE or until their successors are appointed or elected.

Officers

The name, municipality of residence and position held with ACE of each of the officers are as set forth below:

Name and Municipality of Residence	Position Held
Robert A. Milton .... Westmount, Québec	Chairman, President and Chief Executive Officer, ACE, Chairman, Air Canada, Chairman, Aeroplan and Chairman, Jazz
Brian Dunne .... Westmount, Québec	Executive Vice President and Chief Financial Officer
Greg Cote .... Toronto, Ontario	Senior Vice President, Corporate Finance and Strategy
Duncan Dee .... Ottawa, Ontario	Senior Vice President, Corporate Affairs and Chief Administrative Officer
Sydney John Isaacs .... Westmount, Québec	Senior Vice President, Corporate Development and Chief Legal Officer
Jack McLean .... Winnipeg, Manitoba	Controller
Carolyn M. Hadrovic................................. Beaconsfield, Québec	Corporate Secretary

Unless otherwise indicated below, each of the officers has held a position with Air Canada similar to that listed above for more than five years. Brian Dunne was a partner at Arthur Andersen prior to taking up the position of Chief Financial Officer of Aer Lingus in October 2001. Mr. Dunne joined ACE in September 2005. Greg Cote was a partner at Ernst & Young since 1997 prior to joining ACE in September 2005. Duncan Dee was appointed Executive Assistant to the President & Chief Executive Officer, Air Canada in May 2000, Vice President, Corporate Affairs, Air Canada in November 2002, Senior Vice President, Corporate Affairs, Air Canada in April 2004 and Senior Vice President, Corporate Affairs & Chief Administrative Officer, ACE in December 2004. Sydney John Isaacs joined Air Canada in 2000, initially in a business development capacity, and subsequently became Senior Director, Mergers & Acquisitions, and then Senior Director, Restructuring before being appointed Senior Vice President, Corporate Development and Chief Legal Officer of ACE in November 2004. Jack McLean was General Manager, Finance, Air Canada since 1999 before being appointed Controller of ACE in November 2004. Carolyn Hadrovic was Deputy Secretary of ACE before being appointed Corporate Secretary in December 2005 and previously, Senior Counsel, Regulatory and International Law, with Air Canada.

The name, municipality of residence and position held with Air Canada, Aeroplan, Jazz, ACTS LP and other subsidiaries of ACE of each of the following officers are set forth below:

Name and Municipality of Residence	Position Held with Air Canada
Montie R. Brewer...................................... Hudson, Québec	President and Chief Executive Officer, Air Canada
Joshua Koshy .... Richmond Hill, Ontario	Executive Vice President and Chief Financial Officer, Air Canada
Rob Reid .... Oakville, Ontario	Executive Vice President and Chief Operating Officer, Air Canada

Sean Menke.. Baie D'Urfe, Québec	Executive Vice President and Chief Commercial Officer, Air Canada
Lise Fournel .... Lachine, Québec	Chief Information Officer, Air Canada and President and Chief Executive Officer, Destina.ca

Name and Municipality of Residence	**Position Held with Aeroplan**
Rupert J. Duchesne.................................... Montreal, Québec	President and Chief Executive Officer, Aeroplan
Rob Peterson .... Beaconsfield, Québec	Executive Vice President, Finance and Chief Financial Officer, Aeroplan

Name and Municipality of Residence	**Position Held with Jazz**
Joseph D. Randell................................... Waverly, Nova Scotia	President and Chief Executive Officer, Jazz
Allan Rowe .... Halifax, Nova Scotia	Senior Vice President and Chief Financial Officer, Jazz

Name and Municipality of Residence	**Position Held with ACTS LP**
Chahram Bolouri...................................... Beaconsfield, Québec	President and Chief Executive Officer, ACTS LP
Pat Iaconi.. Montréal, Québec	Vice President and Chief Financial Officer, ACTS LP

Name and Municipality of Residence	**Position Held with other Subsidiaries**
Claude Morin .... Montreal, Québec	President and Chief Executive Officer, AC Cargo LP
Chantal Baril .... Pointe-Claire, Québec	President and Chief Executive Officer, ACGHS LP
Benjamin M. Smith .... Toronto, Ontario	Acting President and Chief Executive Officer, Air Canada Vacations Vice President, Planning, Air Canada

As at March 21, 2006, the directors and officers mentioned above as a group owned, directly or indirectly, or had control or direction over 71,593 Voting Shares representing approximately 0.29% of the outstanding Voting Shares and 5,000 Variable Voting Shares representing approximately 0.006% of the outstanding Variable Voting Shares. As at March 21, 2006, the directors and officers mentioned above as a group owned, directly or indirectly, or had control or direction over 85,700 units of Aeroplan Income Fund representing approximately 0.18% of the outstanding units of Aeroplan Income Fund. As at March 21, 2006, the directors and officers mentioned above as a group owned, directly or indirectly, or had control or direction over 101,000 units of Jazz Air Income Fund representing approximately 0.4% of the outstanding units of Jazz Air Income Fund.

Corporate Cease Trade Orders or Bankruptcies

To the knowledge of ACE, in the last ten years, no director or executive officer of ACE is or has been a director or executive officer of any company that, while that person was acting in that capacity, (a) was the subject of a cease trade order or similar order, or an order that denied the relevant company access to any exemptions under securities legislation, for a period of more than 30 consecutive days, (b) was the subject of an event that resulted, after that person ceased to be a director or executive officer, in the company being the subject of a cease trade order or similar order or an order that denied the relevant company access to an exemption under securities legislation, for a period of more than 30 consecutive days or (c) or within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or

instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets except for the following:

(i) Following the acquisition of Canadian Airlines International Ltd. ("CAIL") by Air Canada in 2000, Robert A. Milton became a director of CAIL. Thereafter, CAIL restructured under the CCAA pursuant to a plan of compromise which became effective on July 5, 2000. CAIL's common shares and non-voting shares were suspended from trading by the Toronto Stock Exchange on June 27, 2000 and delisted on July 6, 2000. Robert A. Milton was President and Chief Executive Officer and a director of Air Canada when it filed for protection under the CCAA on April 1, 2003;

(ii) Pierre Marc Johnson was a director of Air Canada when it filed for protection under the CCAA on April 1, 2003;

(iii) Robert E. Brown was a director of Air Canada when it filed for protection under the CCAA on April 1, 2003. Mr. Brown was a director of Nortel Networks Corporation when, on or about May 31, 2004, cease trade orders were issued against directors, officers and certain other current and former employee of Nortel Networks Corporation and Nortel Networks Limited (collectively, "Nortel Networks"). The management cease trade orders were imposed in response to the failure by Nortel Networks to file certain financial statements with the Canadian securities regulators;

(iv) John T. McLennan was the Chief Executive Officer of AT&T Canada when it filed for protection under the CCAA on October 15, 2002;

(v) Rupert J. Duchesne was President and Chief Executive Officer, Aeroplan when Air Canada filed for protection under the CCAA on April 1, 2003;

(vi) Michael M. Green was a director of Anchor Glass Container Corporation when it filed a voluntary petition for reorganization under Chapter 11 of the US Bankruptcy Code in August 2005; and

(vii) Montie R. Brewer was Senior Vice President, Planning for United Airlines until March 31, 2002. UAL Corp., the parent company of United Airlines, filed for protection under Chapter 11 of the US Bankruptcy Code on December 9, 2002.

Penalties or Sanctions

To the knowledge of ACE, no director or executive officer of ACE, (i) has been subject to any penalties or sanctions imposed by a court relating to securities legislation or by a securities regulatory authority or has entered into a settlement agreement with a securities regulatory authority or (ii) has been subject to any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable investor in making an investment decision.

Personal Bankruptcies

To the knowledge of ACE, in the last ten years, no director or executive officer has become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or was subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director or executive officer.

AUDIT COMMITTEE

Audit Committee Charter

The charter of the Audit, Finance and Risk Committee ("Audit Committee") is attached as Appendix A to this Annual Information Form.

Composition of Audit Committee

The Audit Committee of ACE consists of David I. Richardson (chairman), W. Brett Ingersoll and John T. McLennan. Each member of the Audit Committee is independent and financially literate as defined under Multilateral Instrument 52-110 – *Audit Committees*.

Relevant Education and Experience of Audit Committee Members

In addition to each member's general business experience, the education and experience of each Audit Committee member that is relevant to the performance of his or her responsibilities as an Audit Committee member is as follows:

(i) David I. Richardson is a corporate director. Mr. Richardson is a director and Chairman of the audit committee of Husky Injection Molding Systems Ltd. Mr. Richardson is also a director of Air Canada, Jazz Air Holding GP Inc. and a trustee of Aeroplan Income Fund. Mr. Richardson is the former Chairman of Ernst & Young Inc. (Canada) and a former Executive Partner of Ernst & Young LLP. Mr. Richardson joined its predecessor Clarkson, Gordon & Co. in 1963 and was appointed President of The Clarkson Company Limited in 1982. Mr. Richardson was also a member of the Management and Executive Committees of Ernst & Young LLP, national managing partner of the firm's Corporate Finance practice and the senior partner in the Corporate Recovery and Restructuring practice until retirement from the partnership in 2002. Mr. Richardson holds a Bachelor of Commerce Degree from the University of Toronto, is a member and a Fellow of the Institute of Chartered Accountants of Ontario.

(ii) W. Brett Ingersoll is the Managing Director of Cerberus Capital Management, L.P. (private equity investment firm), a senior member of its Private Equity Practice and a member of its Investment Committee. Mr. Ingersoll is also a director of Aeroplan Holding GP Inc. Prior to joining Cerberus in 2002, Mr. Ingersoll was a Partner at JP Morgan Partners (formerly Chase Capital Partners) from 1993 to 2002 (private equity investment firm). Mr. Ingersoll is a director of various public and private companies including Coram Health Care, IAP Worldwide Services, Inc., AerCap B.V., Talecris Bio Therapeutics Inc. and Endura Care, LLC. Mr. Ingersoll holds a BA in economics from Brigham Young University and a MBA from Harvard University.

(iii) John T. McLennan is a corporate director. Mr. McLennan is a director of Hummingbird Ltd., Amdocs Ltd., Emera, Manitoba Telephone Systems (Vice-Chairman) and Medisys Health Services. Mr. McLennan is a director of Jazz Air Holding GP Inc. and also a trustee of Aeroplan Income Fund Mr. McLennan was recently Vice-Chairman and Chief Executive Officer of Allstream. Prior to that position, he served as AT&T Canada's Vice Chairman and Chief Executive Officer. He was also the founding President of Jenmark Consulting Inc., President and Chief Executive Officer of Bell Canada, President of Bell Ontario as well as Chairman, President and Chief Executive Officer of BCE Mobile Communications Inc. Mr. McLennan has served as President and Chief Executive Officer of Cantel Wireless and Executive Vice President of Mitel Communications Inc. Mr. McLennan holds a BSc and a MSc in Industrial Management from Clarkson University.

Pre-approval Policies and Procedures

The Audit Committee reviews and approves the nature of all non-audit services, as permitted by securities legislation and regulations, to be provided by the Corporations' external auditor prior to the commencement of such work. In this regard, the Audit Committee will prepare a report for presentation to the shareholders of the Corporation quarterly or annually, as required, regarding the Audit Committee's approval of such non-audit services in the period.

The Audit Committee will also require and review a report from the external auditor of all relationships between the external auditor and its related entities and the Corporation and its related entities, including all work performed and fees paid for such work of a non-audit nature, that in the external auditor's professional judgment may reasonably be perceived to bear on its objectivity and independence and confirming that in the external

auditor's professional judgment it is independent of the Corporation and discuss this report with the external auditor in order to evaluate the objectivity and independence of the external auditor. The Audit Committee will also review steps taken by the external auditor to address any findings in any of the foregoing reviews.

Auditors' Fees

PricewaterhouseCoopers LLP has served as the Corporation's auditing firm since April 26, 1990. Fees payable for the years ended December 31, 2005 and December 31, 2004 to PricewaterhouseCoopers LLP and its affiliates are $4,425,064 and $4,137,228, respectively. Fees payable to PricewaterhouseCoopers LLP and its affiliates in 2005 and 2004 are detailed below.

	Year ended December 31, 2005	**Year ended December 31, 2004**
Audit fees	$4,161,299	$3,356,851
Audit-related fees	$242,015	$321,269
Tax fees	$21,750	$459,108
All other fees	Nil	Nil
	$4,425,064	$4,137,228

The nature of each category of fees is described below.

Audit fees

Audit fees were paid for professional services rendered for the audit of the Corporation's annual financial statements and for services that are normally provided in connection with statutory and regulatory filings or engagements.

Audit-related fees

Audit-related fees were paid for professional services related to pension plan audits, specified procedures reports and other items related to the audit.

Tax fees

Tax fees were paid for professional services rendered with respect to commodity and income taxes.

INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS

On September 30, 2004, as part of Air Canada's restructuring process, the Cerberus Affiliate invested $250 million in ACE in consideration for the issuance of 12,500,000 Preferred Shares of ACE. The Cerberus Affiliate is an affiliate of Cerberus Capital Management, L.P. Michael M. Green, Carlton D. Donaway and W. Brett Ingersoll, all directors of ACE, are respectively President-Operations, Senior Advisor-Operations and Managing Director of Cerberus Capital Management, L.P.

TRANSFER AGENT AND REGISTRAR

The Transfer Agent and registrar for the Variable Voting Shares and Voting Shares of ACE is CIBC Mellon Trust Company at its principal transfer offices in Montreal, Toronto, Vancouver, Calgary and Halifax.

LEGAL PROCEEDINGS

A description of certain legal proceedings to which ACE is a party appears under the heading "Contingencies, Guarantees and Indemnities" in Note 18 to the consolidated audited annual financial statements of ACE for the year ended December 31, 2005. ACE's audited annual financial statements for the year ended December 31, 2005 are available on SEDAR at *www.sedar.com*.

MATERIAL CONTRACTS

The contracts that are material to the Corporation and that were entered into within the year ended December 31, 2005 or before such year but which are still in effect are the following:

(i) Standby Purchase Agreement between Deutsche Bank Securities Inc. and Air Canada dated as of October 29, 2003, as amended and restated by the amended and restated standby purchase agreement, dated as of April 29, 2004;

(ii) Investment Agreement between Cerberus ACE Investment, LLC and Air Canada dated June 23, 2004; and

(iii) The Aircraft General Terms Agreement AGTA-ACN and related agreements between The Boeing Company and Air Canada, a wholly-owned subsidiary of ACE, dated November 4, 2005.

Please refer to the section titled "Three-year Summary: Evolution of Business" for the particulars of such contracts.

EXPERTS

The Corporation's auditors are PricewaterhouseCoopers LLP, Chartered Accountants, who have prepared an independent auditor's report dated February 9, 2006 in respect of the consolidated statements of financial position of the Corporation as at December 31, 2005 and 2004 and the consolidated statements of operations and retained earnings and cash flows for the year ended December 31, 2005 and for the period from June 29, 2004 to December 31, 2004. PricewaterhouseCoopers LLP has advised that they are independent with respect to the Corporation within the meaning of the Rules of Professional Conduct of the Ordre des comptables agréés du Québec.

ADDITIONAL INFORMATION

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of the ACE's securities and securities authorized for issuance under equity compensation plans will be contained in ACE's management proxy circular for its 2006 annual meeting of shareholders. Additional financial information is provided in ACE's financial statements and management's discussion and analysis for the year ended December 31, 2005. The above information and additional information relating to ACE are available on SEDAR at *www.sedar.com.*

The following documents can be obtained by sending your request to the Corporate Secretary of ACE, at 5100 de Maisonneuve Boulevard West, Montreal, Québec, H4A 3T2 :

(i) this Annual Information Form, together with any document incorporated herein by reference;

(ii) the 2005 Management's Discussion & Analysis / 2005 Financial Statements and Notes of ACE and any interim financial statements filed after the audited financial statements for ACE's most recently completed financial year;

(iii) the Corporation's management proxy circular for the 2005 annual and special shareholder meeting filed with the Securities Commissions on September 30, 2005; and

(iv) any other documents that are incorporated by reference into a preliminary short form prospectus or a short form prospectus pursuant to which securities of ACE are in the course of a distribution.

Except when securities of ACE are in the course of distribution pursuant to a short form prospectus or a preliminary short form prospectus, ACE may require the payment of a reasonable charge from persons, other than security holders of ACE, requesting copies of these documents.

APPENDIX A -
CHARTER AUDIT, FINANCE AND RISK COMMITTEE

(the "Committee")

OF THE BOARD OF DIRECTORS OF ACE

(the "Corporation")

1. Structure, Procedure, Qualifications

The Audit, Finance and Risk Committee (the "Audit Committee") of the Corporation shall be composed of not less than three directors, all of whom shall meet the independence, experience and other membership requirements under applicable laws, rules and regulations as determined by the Board of Directors. The members of the Audit Committee shall have no relationships with management, the Corporation and its related entities that in the opinion of the Board may interfere with their independence from management and from the Corporation. In addition, an Audit Committee member shall not receive, other than for service on the Board or the Audit Committee or other committees of the Board, any consulting, advisory, or other compensatory fee from the Corporation or any of its related parties or subsidiaries. The members of the Audit Committee shall possess the mix of characteristics, experiences and skills to provide an appropriate balance for the performance of the duties of the Audit Committee and in particular each member of the Audit Committee shall be "financially literate" and at least one member shall be a "financial expert" as defined by relevant securities legislation or regulations.

A quorum of the Audit Committee shall be a majority of the members, and a majority of the members present shall be required to pass a resolution of the Audit Committee. The Audit Committee shall be responsible to the Board of Directors of the Corporation. The Chairman and the members of the Audit Committee shall be appointed annually by the Board.

2. Objectives

(a) The objectives of the Audit Committee are as follows:

(i) To assist the Board in the discharge of its responsibility to monitor the component parts of the Corporation's financial reporting and audit process.

(ii) To maintain and enhance the quality, credibility and objectivity of the Corporation's financial reporting and to satisfy itself and oversee management's responsibility as to the adequacy of the supporting systems of internal financial and accounting controls.

(iii) To assist the Board of Directors in its oversight of the independence, qualifications and appointment of the external auditor.

(iv) To monitor the performance of the internal financial and accounting controls and of the internal and external auditors.

(v) To provide independent communication between the Board and the internal auditor and the external auditor.

(iv) To facilitate in-depth and candid discussions between the Audit Committee and management and the external auditor regarding significant issues involving judgment and impacting quality of controls and reporting.

3. Duties

To achieve its objectives, the Audit Committee shall:

(a) Monitor and review the quality and integrity of the Corporation's accounting and financial reporting process through discussions with management, the external auditor and the internal auditor. This will include a review of the annual and quarterly financial statements and Management's Discussion and Analyses ("MD&As") to be filed with regulatory authorities and provided to shareholders, and financial statements and other financial disclosure included in prospectuses, earnings press releases and other similar documents. The Audit Committee shall also review the Corporation's annual information form and other similar documents. These reviews will include:

(i) discussions with management and the external auditor and a consideration of the report by the external auditor to the Audit Committee of matters related to the conduct of an audit;

(ii) discussions with the external auditor respecting the auditor's judgment regarding both the acceptability and quality of the financial statements including the critical accounting policies and practices used by management in their preparation, alternative treatments and disclosures of financial information within generally accepted accounting principles that have been considered by management and their ramifications, the selection of changes in significant accounting policies, the method used to account for significant unusual transactions, the effect of significant accounting policies in controversial or emerging areas, the degree of aggressiveness or conservatism, as the case maybe, of the accounting policies adopted by the Corporation, the process used by management in formulating particularly significant accounting estimates and the basis for the external auditor's conclusions regarding the reasonableness of those estimates;

(iii) a review of significant adjustments arising from an audit;

(iv) a review of disagreements with management over the application of accounting policies as well as any disclosure in the financial statements;

(v) a review of all material off-balance sheet transactions and other relationships with non-consolidated entities that may have a material current or future effect on the financial condition of the Corporation including their disclosure or lack thereof in the applicable quarterly or annual financial statements;

(vi) a review of the external auditor's suggestions for improvements to the Corporation's operations and internal controls;

(vii) a review of the nature and size of unadjusted errors of a non-trivial amount;

(viii) a review to ascertain that various covenants are complied with; and

(ix) the selection of, and changes in, accounting policies and consideration of the appropriateness of such selections and changes.

(b) Determine, based on its review and discussion, whether to recommend the approval by the Board of such financial statements and the financial disclosure in any such annual information forms, earnings press releases, prospectuses and other similar documents.

(c) Review with management, the internal auditor and the external auditor and, if considered appropriate, approve the release of the Corporation's quarterly financial statements and related MD&A.

(d) Review with management, the external auditor and legal counsel, the Corporation's procedures to ensure compliance with applicable laws and regulations, and any significant litigation, claim or

other contingency, including tax assessments, that would have a material effect upon the financial position or operating results of the Corporation and the disclosure or impact on the results of these matters in the quarterly and annual financial statements.

(e) Meet with the Corporation's external auditor to review and approve their audit plan with particular emphasis on risk factors which could lead to a material misstatement of the financial statements, the scope and timing of the audit, the assumptions and decisions that have been made in developing the plan and co-ordination of work between the external auditor and the internal audit department.

(f) Review and approve estimated audit and audit-related fees and expenses for the current year. Pre approve any significant additional audit and audit-related fees over the estimated amount. Review and approve audit and audit-related fees and expenses for the prior year. The authority for the determination and payment of fees to the external auditor rests solely and exclusively with the Audit Committee. The Corporation shall ensure that funding is available to the Audit Committee for payment of compensation to the external auditor.

(g) Review

(i) and approve, or delegate to a member of the Audit Committee the responsibility to review and approve and subsequently report to the Audit Committee, the nature of all non-audit services, as permitted by securities legislation and regulations, to be provided by the Corporations' external auditor prior to the commencement of such work. In this regard the Audit Committee will prepare a report for presentation to the shareholders of the Corporation quarterly or annually, as required, regarding the Audit Committee's approval of such non-audit services in the period;

(ii) and implement from time to time a process in connection with non-audit services performed by the external auditor.

(h) Review a report from the external auditor of all relationships between the external auditor and its related entities and the Corporation and its related entities, including all work performed and fees paid for such work of a non-audit nature, that in the external auditor's professional judgment may reasonably be perceived to bear on its objectivity and independence and confirming, or otherwise, that in the external auditor's professional judgment it is independent of the Corporation and discuss this report with the external auditor in order to evaluate the objectivity and independence of the external auditor. The Audit Committee should specifically require the external auditor to confirm that it is a registered public accounting firm as prescribed by various applicable securities regulations. As well, at least once a year the Audit Committee will carry out a review of the credentials of the members of the firm including without limitation the biographies of the members, whether there has been any enforcement actions, issues related to the firm and law suits, if any. A formal written report will be obtained from the external auditor outlining: the auditing firm's internal quality control procedures; any material issues raised within the preceding five years by the auditing firm's internal quality control review, peer reviews or any other inquiry or investigation by governmental or professional authority relating to any audit conducted by the firm. The Committee will also review steps taken by the auditing firm to address any findings in any of the forgoing reviews.

(i) Receive reports on any consultations between management and other public accountants respecting accounting principles to be applied in preparing the quarterly or annual financial statements, and on any incidents involving fraud or illegal acts of which management, the internal audit department or the external auditor become aware. In this regard, review the relevant control procedures with management to ensure that such matters are adequately guarded against.

(j) At least once each year:

(i) Meet privately with management to assess the performance of the external auditor.

(ii) Meet privately with the external auditor, amongst other things, to understand any restrictions placed on them or other difficulties encountered in the course of the audit, including instructions on the scope of their work and access to requested information and the level of co-operation received from management during the performance of their work and their evaluation of the Corporation's financial, accounting and audit personnel and systems.

(k) Evaluate the performance of the external auditor, and if so determined, recommend that the Board either take steps to replace the external auditor or provide for the reappointment of the external auditor by the shareholders.

(l) Regarding the services provided by the internal audit department, the Audit Committee will:

(i) meet privately with internal audit, amongst other things, to understand any restrictions placed on them or other difficulties encountered in the course of their audits, including instructions on the scope of their work and access to requested information and the level of co-operation received from management during the performance of their work;

(ii) periodically review and approve the mandate, reporting relationships and resources of the internal audit group;

(iii) review the objectivity, qualifications, adequacy and experience of the internal audit staff and approve the appointment, dismissal or replacement of the head of the internal audit department;

(iv) review and approve annually the planned scope for the internal audit program, its objectives, and the resources required to attain these objectives;

(v) periodically throughout each year review the reports of the internal audit department which describe the activities of the internal audit department for the preceding period; and

(vi) review the working relationship between the internal audit department and the external auditor, and between the internal audit department and management.

(m) Obtain from both the internal audit department and the Corporation's external auditor the major audit findings and internal control recommendations reported during the period under review, the response of management to those recommendations, and review the follow-up performed by management and the internal audit department in order to monitor whether management has implemented an effective system of internal accounting control.

(n) Review significant emerging accounting and reporting issues, including recent professional and regulatory pronouncements, and assess their impact on the Corporation's financial statements.

(o) Review policies and procedures for the receipt, retention and treatment of complaints received by the Corporation from employees, shareholders and other stakeholders regarding accounting issues and financial reporting, internal controls and internal or external auditing matters. The Audit Committee should be satisfied that sufficient controls are in place to ensure that all such complaints can be received anonymously and with an appropriate degree of confidentiality and that potential employee informants are aware of the process that is in place. The Audit Committee should also be satisfied that processes are in place to ensure that all such complaints, regardless of significance, are presented to the Audit Committee.

(p) Review policies for approval of senior management expenses.

(q) Review the process relative to the periodic certifications by the Chief Executive Officer and the Chief Financial Officer of the Corporation in respect of financial disclosures, the existence of any significant deficiencies in the design or operation of internal controls which could adversely affect the Corporation's ability to record, process, summarize and report financial data and any significant changes in internal controls or changes to the environment in which the internal controls operate, including corrections of material deficiencies and weaknesses.

(r) Review with management the Corporation's computer systems, including procedures to keep the systems secure and contingency plans developed to deal with possible computer failures.

(s) Review and approve all related party transactions as such term is defined from time to time in Policy Statement Q-27 of the Quebec Securities Commission and Rule 61-501 issued by the Ontario Securities Commission, as may be amended from time to time.

(t) Review risk management systems and controls, especially in relation to derivatives, foreign currency exposure, hedging and insurance.

(u) Whenever it may be appropriate to do so, retain and receive advice from experts, including independent legal counsel and independent public accountants, and conduct or authorize the conduct of investigations into any matters within the scope of the responsibility of the Audit Committee as the Audit Committee may consider appropriate. The Corporation shall ensure that funding is available to the Audit Committee in respect of the aforementioned activities.

(v) Report regularly to the Board in writing on the activities, findings and conclusions of the Audit Committee.

(w) Review this Charter on an annual basis and recommend to the Board any changes to it that the Audit Committee considers advisable.

(x) Complete a self-assessment annually to determine how effectively the Audit Committee is meeting its responsibilities.

(y) Perform such other functions as may be delegated from time to time by the Board.

(z) Review the process for the rotation of the lead audit partner, the concurring partner and any other audit engagement team partner.

(aa) Set policies for the hiring of employees or former employees of the Corporation's external auditors.

OTHER

(a) Air Canada Pension Plans

In relation to the Air Canada pension plans, the Audit Committee shall:

(i) On the recommendation of the Chief Financial Officer, approve the investment structure for the plans, any applicable Statement of Investment Policies and Objectives ("SIP&O"), Statement of Investment Principles and Beliefs ("SIP&B") and other investment policies for the plans;

(ii) With the assistance of the Chief Financial Officer, periodically review for appropriateness of the pension funds mission, funding policy, SIP&O, SIP&B, other

investment policies and investment structure, and monitor overall pension funds operation, in particular plans funded status, compliance of funding practices with funding policy, compliance of investments with the SIP&O and as applicable, the compliance of SIP&O with the investment principles and beliefs as set out in the SIP&B;

(iii) With the assistance of the Chief Financial Officer, periodically review and monitor the total and asset class return for the defined benefit pension plans, and the investment matters relating to the defined contribution plans;

(iv) Recommend to the Board for its approval the mission for the pension funds, the funding policy, the level of annual contributions, the appointment of the external auditor and the custodians of the assets of the pension plans;

(v) Approve the actuary and consultant recommended by management;

(vi) On the recommendation of management, accept the actuarial assumptions and actuarial valuation reports for the pension plans; and

(vii) Approve the annual audited financial statements and the pension accounting for the pension plans.

(b) Public Disclosure

(i) Review and approve the Corporation's Public Disclosure Policy and any changes related thereto and ensure consistency with current developments and best practices;

(i) Where practicable, management will review with the Audit Committee or the Chairman of the Audit Committee draft news releases to be disseminated to the public related to earnings warnings or financial results forecasting by the Corporation which are expected by management to be material in relation to the market price of any of the Corporation's securities.

(c) Risk Identification and Management

The Audit Committee shall make all reasonable efforts to identify and address material financial and other risks to the business and affairs of the Corporation and its subsidiaries and make recommendations in that regard to the Board of Directors of the Corporation. The Audit Committee shall review and discuss with management, the internal audit department and the external auditor all major financial risk exposures and the steps management has taken to monitor/control those exposures. The Audit Committee shall be entitled, from time to time, to retain experts and consultants to assist the Audit Committee with the discharge of such mandate. The Audit Committee shall have the discretion in the discharge of these duties to address risks to the Corporation's and its subsidiaries' revenues and costs, as well as potentially corrupt or other practices that may lead to loss or depreciation ob business reputation.

(d) Contingent Liabilities

The Audit Committee shall establish processes and procedures to identify and monitor contingent liabilities of the Corporation and its subsidiaries. In the discharge of these duties, the Audit Committee shall have the discretion to retain experts and consultants and to review, without limitation, workplace safety, environmental issues and any other matters, whether of a financial nature or otherwise, that can give rise to a contingent liability. The Audit Committee shall make recommendations, from time to time, to the Board of Directors of the Corporation on these matters.

(e) Corporate Authorizations Policies

(i) Periodically review and approve policies relative to the financial control, conduct, regulation and administration of subsidiary companies;

(ii) Periodically review the any administrative resolutions adopted from time to time pursuant to the Corporation's By-laws pertaining to the establishment of procedures relative to commitment and transaction authorizations, the determination of the officers or other persons by whom any instrument in writing or document is to be executed and the manner of execution thereof;

(iii) Review, monitor and approve the Corporate Donations Policy and any changes thereto and the annual Corporate Donations Budget; and

(iv) Review, monitor and approve any other financial expenditure policies that would affect the Corporation's and its subsidiaries' financial condition or reputation.

(f) Performance to Budget

(i) Review actual financial performance compared to budget;

(g) Meetings

(i) The Audit Committee shall meet at least quarterly at the call of the Chairman of the Audit Committee, any other member of the Audit Committee or the external auditors.

(ii) An "in-camera" session of the members of the Committee shall be held as part of each meeting of the Committee.

(h) Responsibilities

Nothing contained in the above mandate is intended to assign to the Audit Committee the Board of Directors' responsibility to ensure the Corporation's compliance with applicable laws or regulations or to expand applicable standards of liability under statutory or regulatory requirements for the directors or the members of the Audit Committee. Even though the Audit Committee has a specific mandate and its members have financial experience and expertise, it is not the duty of the Audit Committee to plan or conduct audits, or to determine that the Corporation's financial statements are complete and accurate and are in accordance with generally accepted accounting principles. Such matters are the responsibility of management, the internal auditor and the external auditor.

Members of the Audit Committee are entitled to rely, absent knowledge to the contrary, on (i) the integrity of the persons and organizations from whom they receive information, (ii) the accuracy and completeness of the information provided, and (iii) representations made by management as to the non-audit services provided to the Corporation by the external auditor.