ACE AVIATION

Third Quarter 2009
Interim Unaudited
Consolidated Financial Statements and Notes

November 6, 2009

Consolidated Statement of Operations

Unaudited (Canadian dollars in millions except per share figures)		Three Months Ended September 30 2009	Three Months Ended September 30 2008	Nine Months Ended September 30 2009	Nine Months Ended September 30 2008
Operating revenues					
Passenger		$ 2,400	$ 2,766	$ 6,469	$ 7,531
Cargo		92	139	248	402
Other		178	170	674	651
		2,670	3,075	7,391	8,584
Operating expenses					
Aircraft fuel		682	1,064	1,847	2,627
Wages, salaries and benefits		437	479	1,337	1,462
Airport and navigation fees		272	275	743	771
Capacity purchase with Jazz	Note 10	246	243	746	711
Depreciation and amortization		170	174	490	514
Aircraft maintenance		183	127	557	502
Food, beverages and supplies		82	86	222	244
Communications and information technology		70	69	229	214
Aircraft rent		81	67	250	199
Commissions		51	54	140	154
Other		328	332	1,069	1,110
		2,602	2,970	7,630	8,508
Operating income (loss) before under noted item		**68**	**105**	**(239)**	**76**
Provision for cargo investigations		-	-	-	(125)
Operating income (loss)		**68**	**105**	**(239)**	**(49)**
Non-operating income (expense)					
Interest income		3	19	14	67
Interest expense	Note 2	(87)	(87)	(292)	(270)
Interest capitalized		1	6	4	31
Gain (loss) on assets	Note 2	1	-	(70)	961
Loss on repurchase of ACE convertible senior notes and preferred shares	Note 2	(10)	-	(43)	-
Gain (loss) on financial instruments recorded at fair value	Note 6	4	(93)	73	60
Equity and other investment loss		-	(19)	-	(2)
Other		(4)	(1)	(5)	(2)
		(92)	(175)	(319)	845
Income (loss) before the following items		**(24)**	**(70)**	**(558)**	**796**
Non-controlling interest		(72)	30	(20)	62
Foreign exchange gain (loss)		295	(87)	549	(128)
Recovery of (provision for) income taxes	Note 7				
Current		-	(1)	2	(2)
Future		(1)	(7)	(9)	(215)
Net income (loss) for the period		**$ 198**	**$ (135)**	**$ (36)**	**$ 513**
Net income (loss) per share	Note 5				
Basic		$ 5.57	$ (3.86)	$ (1.01)	$ 10.26
Diluted		$ 5.15	$ (3.86)	$ (1.01)	$ 7.43

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

Consolidated Statement of Financial Position

Unaudited (Canadian dollars in millions)		September 30 2009	December 31 2008
ASSETS			
Current			
Cash and cash equivalents		$ 1,176	$ 1,307
Short-term investments		167	506
		1,343	1,813
Restricted cash		58	45
Accounts receivable		736	700
Aircraft fuel inventory		60	97
Spare parts and supplies	Note 2	48	20
Collateral deposits for fuel derivatives	Note 6	105	328
Prepaid expenses and other current assets		239	206
		2,589	3,209
Property and equipment	Note 2	6,899	7,469
Intangible assets		627	698
Deposits and other assets	Note 6	500	495
		$ 10,615	**$ 11,871**
LIABILITIES			
Current			
Accounts payable and accrued liabilities		$ 1,245	$ 1,288
Fuel derivatives	Note 6	94	420
Advance ticket sales		1,264	1,333
Current portion of long-term debt and capital leases		553	663
		3,156	3,704
Long-term debt and capital leases	Note 2	4,354	4,980
Convertible preferred shares	Note 2	-	206
Future income taxes		50	50
Pension and other benefit liabilities		1,262	1,585
Other long-term liabilities		465	370
		9,287	10,895
Non-controlling interest		528	512
SHAREHOLDERS' EQUITY			
Share capital and other equity		122	307
Contributed surplus	Note 6	383	163
Retained earnings		564	600
Accumulated other comprehensive loss		(269)	(606)
		800	464
		$ 10,615	**$ 11,871**

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

Consolidated Statement of Changes in Shareholders' Equity

Unaudited (Canadian dollars in millions)		Nine Months Ended September 30 2009	Year Ended December 31 2008	Nine Months Ended September 30 2008
Share capital				
Common shares, beginning of period		$ 100	$ 243	$ 243
Repurchase and cancellation of common shares		-	(180)	(180)
Issue of shares through stock options exercised		4	37	37
Total share capital		104	100	100
Other equity				
Convertible senior notes	Note 5	18	90	90
Convertible preferred shares	Note 5	-	117	117
Total share capital and other equity		122	307	307
Contributed surplus				
Balance, beginning of period		163	504	504
Repurchase and cancellation of common shares		-	(329)	(329)
Repurchase and cancellation of ACE convertible senior notes and preferred shares	Note 2	182	-	-
Air Canada pension MOUs	Note 6	29	-	-
Air Canada warrants	Note 2	7	-	-
Fair value of stock options recognized as compensation expense (recovery)		2	(5)	(4)
Fair value of exercised stock options to share capital		-	(7)	(7)
Total contributed surplus		383	163	164
Retained earnings				
Balance, beginning of period		600	2,209	2,209
Repurchase and cancellation of common shares		-	(1,489)	(1,489)
		600	720	720
Net income (loss) for the period		(36)	(120)	513
Total retained earnings		564	600	1,233
Accumulated other comprehensive income (loss)				
Balance, beginning of period		(606)	54	54
Other comprehensive income (loss)		337	(660)	(100)
Total accumulated other comprehensive loss		(269)	(606)	(46)
Total retained earnings and accumulated other comprehensive income (loss)		295	(6)	1,187
Total shareholders' equity		**$ 800**	**$ 464**	**$ 1,658**

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

Consolidated Statement of Comprehensive Income

Unaudited (Canadian dollars in millions)		Three Months Ended September 30 2009	Three Months Ended September 30 2008	Nine Months Ended September 30 2009	Nine Months Ended September 30 2008
Comprehensive income					
Net income (loss) for the period		$ 198	$ (135)	$ (36)	$ 513
Other comprehensive income (loss), net of taxes:					
Net change in unrealized loss on Jazz Air Income Fund		-	-	-	65
Reclassification of net realized gains on Jazz Air Income Fund to income		-	-	-	(65)
Net change in unrealized gain on Aeroplan Income Fund		-	-	-	331
Reclassification of net realized gains on Aeroplan Income Fund to income		-	-	-	(331)
Net gains (losses) on fuel derivatives under hedge accounting	Note 6	-	(244)	(1)	29
Reclassification of net realized losses (gains) on fuel derivatives to income	Note 6	94	(44)	338	(129)
		94	(288)	337	(100)
Total comprehensive income (loss)		**$ 292**	**$ (423)**	**$ 301**	**$ 413**

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

Consolidated Statement of Cash Flow

Unaudited (Canadian dollars in millions)		Three Months Ended September 30 2009	Three Months Ended September 30 2008	Nine Months Ended September 30 2009	Nine Months Ended September 30 2008
Cash flows from (used for)					
Operating					
Net income (loss) for the period		$ 198	$ (135)	$ (36)	$ 513
Adjustments to reconcile to net cash from operations					
Depreciation and amortization		170	174	490	514
Loss (gain) on assets		(1)	-	70	(961)
Loss on repurchase of ACE convertible senior notes and preferred shares		10	-	43	-
Foreign exchange (gain) loss		(308)	102	(520)	103
Future income taxes		1	7	9	215
Excess of employee future benefit funding over expense		(103)	(150)	(315)	(232)
Provision for cargo investigations	Note 6	-	-	-	125
Non-controlling interest		72	(30)	20	(62)
Fuel and other derivatives	Note 6	80	106	17	(36)
Fuel hedge collateral deposits, net	Note 6	(3)	-	206	-
Equity investment loss		-	19	-	7
Changes in non-cash working capital balances		(361)	(374)	(203)	6
Other		5	16	31	(11)
		(240)	**(265)**	**(188)**	**181**
Financing					
Issue of common shares		-	-	-	30
Repurchase and cancellation of common shares		-	-	-	(1,998)
Borrowings	Note 2	437	-	780	313
Repurchase of ACE convertible senior notes	Note 2	-	-	(233)	-
Repurchase of ACE convertible preferred shares	Note 2	(74)	-	(260)	-
Reduction of long-term debt and capital lease obligations		(256)	(67)	(856)	(709)
		107	**(67)**	**(569)**	**(2,364)**
Investing					
Short-term investments		252	226	339	222
Proceeds from sale of Aeroplan units		-	-	-	692
Proceeds from sale of Jazz units		-	-	-	182
Exercise of ACTS Aero put option		-	-	-	(19)
Proceeds from escrow related to sale of ACTS		-	-	-	40
Additions to capital assets		(34)	(105)	(190)	(733)
Proceeds from contractual commitment	Note 1C	230	-	230	-
Proceeds from sale of assets	Note 2	3	-	96	27
Proceeds from sale-leaseback transactions	Note 2	-	-	172	708
Other		7	51	(21)	85
		458	**172**	**626**	**1,204**
Increase (decrease) in cash and cash equivalents		**325**	**(160)**	**(131)**	**(979)**
Cash and cash equivalents, beginning of period		851	1,481	1,307	2,300
Cash and cash equivalents, end of period		**$ 1,176**	**$ 1,321**	**$ 1,176**	**$ 1,321**
Cash payments of interest		$ 66	$ 68	$ 247	$ 222
Cash payments (recoveries) of income taxes		$ -	$ (1)	$ (2)	$ 2

Cash and cash equivalents exclude Short-term investments of $167 as at September 30, 2009 (as at September 30, 2008 - $617).

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

Notes to the Interim Consolidated Financial Statements (unaudited)
(currencies in millions – Canadian dollars)

1. BASIS OF PRESENTATION, CHANGES IN ACCOUNTING POLICIES, AND AIR CANADA LIQUIDITY

ACE Aviation Holdings Inc. ("ACE"), which was incorporated on June 29, 2004, is a holding company of aviation interests. Reference to the "Corporation" in the following notes to the financial statements refers to, as the context may require, ACE and its aviation interests collectively, ACE and one or more of its aviation interests, one or more of ACE's aviation interests, or ACE itself.

As at September 30, 2009, ACE holds:

- a 75.0% (75 million Class B Voting Shares) ownership interest in Air Canada[1];
- a secured loan of $150 to Air Canada as part of the Air Canada secured term credit facility (refer to Note 2); and
- a 28.4% direct interest in Aero Technical Support & Services Holdings sarl ("ACTS Aero"), which owns 100% of Aveos Fleet Performance Inc. Since December 31, 2008, the carrying value of the Corporation's investment in ACTS Aero is nil.

[1] In October 2009 ACE's ownership interest in Air Canada was diluted to 27% through the issuance of shares by Air Canada. Refer to Note 12 for a detailed description.

A) BASIS OF PRESENTATION

These financial statements have been prepared on a going concern basis of presentation. Under a going concern basis of presentation, Air Canada is consolidated within ACE's financial statements under accounting policies applicable to a going concern. The going concern basis of presentation assumes continuity of operations, realization of assets and satisfaction of liabilities in the ordinary course of business.

The unaudited interim consolidated financial statements for the Corporation are based on the accounting policies consistent with those disclosed in Note 2 to the 2008 annual consolidated financial statements of the Corporation, with the exception of the changes in accounting policies described below in part B) Changes in Accounting Policies.

In accordance with Canadian generally accepted accounting principles ("GAAP"), these interim financial statements do not include all of the financial statement disclosures required for annual financial statements and should be read in conjunction with the 2008 annual consolidated financial statements of the Corporation. In management's opinion, the financial statements reflect all adjustments that are necessary for a fair presentation of the results for the interim periods presented.

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

B) CHANGES IN ACCOUNTING POLICIES

Stock-based Compensation Plans

The Corporation changed its accounting policy for awards of stock based compensation granted to Corporation employees with a graded vesting schedule. Prior to January 1, 2009, the fair value of stock options with a graded vesting schedule was recognized as compensation expense and a credit to Contributed surplus on a straight line basis over the applicable vesting period. Effective January 1, 2009, the fair value of stock options with a graded vesting schedule is determined based on different expected lives for the options that vest each year, as it would be if the award is viewed as several separate awards, each with a different vesting date, and it is accounted for on that basis. The new accounting policy provides more reliable and relevant information about the consequences of the transactions.

The impact of the change in accounting policy for awards granted to Corporation employees with a graded vesting schedule was immaterial to any prior period and therefore was not adjusted.

Goodwill and Intangible Assets

Effective January 1, 2009 the Corporation adopted the new Canadian Institute of Charted Accountants ("CICA") accounting standard section 3064, *Goodwill and Intangible Assets* which provides guidance on the recognition, measurement, presentation and disclosure for goodwill and intangible assets, other than the initial recognition of goodwill or intangible assets acquired in a business combination. The Corporation's accounting policy for intangible assets is consistent with the new standard and as a result, no adjustment was recorded on transition.

Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

Effective January 1, 2009, the Corporation adopted the recommendations of the Emerging Issues Committee ("EIC") of the CICA relating to Abstract EIC-173 Credit Risk and the Fair Value of Financial Assets and Financial Liabilities. This Abstract confirms that an entity's own credit risk and the credit risk of the counterparty should be taken into consideration in determining the fair value of financial assets and liabilities, including derivative instruments. The adoption of this guidance had no significant effect on the Corporation's consolidated financial statements as collateral deposits with fuel derivative counterparties and master netting arrangements were considered in determining that no credit risk adjustment was required on the valuation of the derivatives.

The following is an overview of accounting standard changes that the Corporation will be required to adopt in future years:

Business Combinations, Consolidated Financial Statements and Non-controlling Interests

The CICA issued three new accounting standards in January 2009: section 1582, *Business Combinations*, section 1601, *Consolidated Financial Statements*, and section 1602, *Non-controlling interests*. These new standards will be effective for fiscal years beginning on or after January 1, 2011. The Corporation is in the process of evaluating the requirements of these new standards.

Section 1582 replaces section 1581, and establishes standards for the accounting for a business combination. It provides the Canadian equivalent to International Financial Reporting Standard IFRS 3 – *Business Combinations*. The section applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011.

Sections 1601 and 1602 together replace section 1600 – *Consolidated Financial Statements.* Section 1601, establishes standards for the preparation of consolidated financial statements. Section 1601 applies to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of International Financial Reporting Standard IAS 27 - *Consolidated and Separate Financial Statements* and applies to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011.

C) AIR CANADA LIQUIDITY

Air Canada has entered into the following transactions in 2009, in an effort to mitigate Air Canada's liquidity risks as described in Note 6 below and in Note 1D to the 2008 annual consolidated financial statements of the Corporation (refer to Note 2 for additional detail on these financing activities):

During October 2009

- Completed a share and warrant public offering for net proceeds of $248 (refer to Note 12 for further details).

During the third quarter of 2009

- A secured term credit facility (the "Credit Facility") for financing proceeds of $600, less fees of $20. The Credit Facility is a five-year facility, with the first principal repayment due in August 2010, and currently bears interest at 12.75%. The Credit Facility also provided for warrants entitling the debt holders to acquire up to 10% of the shares in Air Canada, which at the time of the issuance of the warrants, as described in Note 2, represented 10 million shares in Air Canada. As part of the transactions related to the closing of the Credit Facility, existing financing arrangements of $166 were repaid as follows:
    - The revolving credit facility, as further described in Note 9 (j) of the 2008 annual consolidated financial statements of the Corporation, was repaid in the amount of $49. The rights of the lender under this facility were assigned to the lenders under the Credit Facility;
    - The spare engine financing agreement, as further described in Note 2, was partially repaid in the amount of $38. This represented the repayment related to 22 engines under the spare engine financing agreement, with 10 engines remaining under the agreement with a loan value of $76 as at September 30, 2009;
    - The Aeroplan Canada Inc. ("Aeroplan") loan, as further described in Note 2, was repaid in the amount of $79. Aeroplan is a participating lender under the Credit Facility.

- Extended or renewed labour agreements for 21 months with all of Air Canada's Canadian-based unions became effective. The agreements provide for no increases to wage rates, no changes to group insurance coverage or benefits, or pension benefit levels during the contract extension or renewal periods;

- Pension funding agreements with all of Air Canada's Canadian-based unions (the "Pension MOUs") and the adoption of the *Air Canada Pension Funding Regulations, 2009* (the "Air Canada 2009 Pension Regulations"). The Air Canada 2009 Pension Regulations relieve Air Canada from making any special (past service cost) payments for the period beginning April 1, 2009 and ending December 31, 2010. Thereafter, in respect of the period from January 1, 2011 to December 31, 2013, the aggregate annual past service contributions shall equal the lesser of (i) $150, $175, and $225 in respect of 2011, 2012, and 2013, respectively and (ii) the maximum past service contributions permitted under the Income Tax Act. Pursuant to the Pension MOUs, on October 26, 2009 Air Canada issued, to a trust, 17,647,059 Class B Voting Shares. This number of shares represented 15% of the shares of Air Canada issued and outstanding as at the date of the Pension MOUs and the date of issuance (after taking into account such issuance). All net proceeds of the sale of such shares held by the trust are to be contributed to the pension plans. Refer to Note 12 for a description of subsequent events;

- An agreement with a supplier for non-refundable proceeds of $230 in consideration of various contractual commitments. For accounting purposes, the recognition of these proceeds was deferred and will be applied to reduce the cost of these contractual commitments;

- Amendments to credit card processing agreements (initiated in the second quarter and completed in July 2009) with one of its principal credit card processors to revise the levels of unrestricted cash (as defined per the agreement and generally based on the balances as reported in Cash and cash equivalents and Short-term investments) required to be maintained as described further below;

- An extension to a short-term loan of $82 (US$75) entered into in 2008, which was originally due in 2009, to 2013. This loan is described in Note 9 (l) of the 2008 annual consolidated financial statements of the Corporation, except for the amendment to extend the repayment to 2013;

- A memorandum of understanding with GE Capital Aviation Services (the "GECAS MOU") for the sale and leaseback of three Boeing 777 aircraft. The sale and leaseback transactions were substantially completed in early November 2009 and provided initial net cash proceeds of $95 (net of deposits), with additional net proceeds of $20 to be received upon completion of a remaining part of the transaction, which is expected to occur later in the fourth quarter of 2009; and

- An agreement amending the terms related to Air Canada's capacity purchase agreement with Jazz Air LP ("Jazz"), effective August 1, 2009, which provides for a reduction to rates paid under the agreement.

During the second quarter of 2009

- A secured loan with Aeroplan for net proceeds of $79. This loan, as described above, was terminated in July 2009 pursuant to the transactions relating to the Credit Facility; and;

- Net return of collateral deposits on fuel derivatives in the amount of $72 partially offset by the settlement of fuel derivative contracts in favour of counterparties in the amount of $17.

During the first quarter of 2009

- Financing arrangements secured by spare parts, spare engines and a Boeing 777 aircraft for aggregate proceeds of $267, net of fees of $5. The spare engine financing was partially repaid in July 2009, as described above;

- Sale lease-back of a Boeing 777 aircraft for aggregate proceeds of $172 and the required repayment of a debt obligation related to the aircraft of $128, which included a prepayment fee of $14;

- Inventory financing arrangement under which Air Canada acquired certain spare parts inventories expected to be consumed over the next 12 months in exchange for the issuance of bills of exchange due in February 2010. Subsequent to the initial transaction, Air Canada has settled or holds as collateral certain of the bills and as a result the expected final payment in 2010 is $18 (US$17), as at October 31, 2009;

- Repayment of pre-delivery financing of $83 on the Boeing 777 aircraft received during the first quarter; and;

- Net return of collateral deposits on fuel derivatives in the amount of $147 more than offset by the settlement of fuel derivative contracts in favour of counterparties in the amount of $217.

At October 31, 2009, Air Canada had Cash and cash equivalents and Short-term investments of $1,460 ($1,005 as at December 31, 2008).

2. FINANCING AND INVESTING ACTIVITIES

ACE Convertible Senior Notes and Convertible Preferred Shares

In January, 2009, ACE completed a substantial issuer bid to purchase for cancellation 80% of its convertible senior notes outstanding as at December 31, 2008, at a purchase price of $900 dollars in cash for each $1,000 dollars principal amount of notes. The aggregate principal amount of the repurchased Convertible senior notes was $259. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 for the notes tendered.

In January 2009 and March 2009, ACE completed two substantial issuer bids to purchase for cancellation 9.3 million of its convertible preferred shares at a purchase price of $20 dollars per preferred share. The Corporation paid an aggregate purchase price of $186 for the shares tendered. In September 2009, the Corporation entered into an agreement with Morgan Stanley Canada Limited pursuant to which ACE indirectly acquired for cancellation all of its remaining 3.2 million convertible preferred shares at a price of $23 dollars per preferred share for an aggregate purchase price of $74.

A Loss on repurchase of the convertible senior notes and preferred shares has been recorded in the third quarter of 2009 within Non-operating expense. The repurchase price of these instruments, allocated to the liability components of these compound instruments, exceeded the respective carrying values resulting in a loss of $10 being recorded in Quarter 3 2009 ($43 for the nine months ended September 30, 2009). The residual equity components of the instruments amounting to $23 ($182 for the nine months ended September 30, 2009) have been transferred directly to Contributed surplus in the consolidated statement of changes in shareholders' equity.

Refer to the Note 12 - Subsequent Events for the announcement concerning ACE's redemption of its convertible senior notes.

ACE Loan to Air Canada

During the third quarter of 2009, ACE participated in the $600 Air Canada Credit Facility with a number of other lenders providing financing of $150 which represented 25% of the Credit Facility. Refer to the Air Canada Financing section below for a detailed description of the Credit Facility.

Under the Credit Facility, ACE received 1,250,000 warrants on July 30, 2009 for the purchase of Air Canada Class B Voting Shares with an exercise price of $1.51 per share, exercisable at any time, and expiring four years after the date of issuance. On October 19, 2009, ACE received an additional 1,250,000 warrants with an exercise price of $1.44 per share, exercisable at any time, and expiring four years thereafter.

ACE’s loan and warrants have been eliminated upon the consolidation of Air Canada.

AIR CANADA FINANCING

Air Canada Term Credit Facility

In July 2009, Air Canada received financing proceeds of $600, less financing fees of $20 under a secured term credit facility (the “Credit Facility”). On or before the first anniversary and subject to satisfaction of certain conditions, Air Canada may request the increase of the facility by up to an additional $100 by obtaining new commitments from either the existing or new lenders. The Credit Facility is repayable in sixteen (16) consecutive quarterly installments commencing in August 2010 of $30 with the final installment of $120 due in July 2014. Any increase to the facility would increase, on a pro rata basis, the scheduled repayments, including the final payment.

The Credit Facility bears interest at a rate based upon the greater of the bankers’ acceptance rate or 3.00% plus 9.75% (12.75% as at September 30, 2009). The Credit Facility can be repaid at any time, in whole or in part subject to a minimum repayment of $10.

Air Canada's obligations under the Credit Facility are secured by a first priority security interest and hypothec over substantially all the present and after-acquired property of Air Canada and its subsidiaries, subject to certain exclusions and permitted liens. The Credit Facility contains customary representations and warranties and is subject to customary terms and conditions (including negative covenants, financial covenants and events of default). Financial covenants require Air Canada to maintain, as of the last business day of each month, a minimum liquidity level (as defined per the Credit Facility and generally based upon the balances as reported in Cash and cash equivalents and Short-term investments) of $800 and a minimum EBITDAR (earnings before interest, income taxes, depreciation, amortization, aircraft rentals, certain non-operating income (expense) and special items) and an interest coverage ratio test determined as at the end of each fiscal quarter.

A requirement of the Credit Facility is that Air Canada maintain securities of $800 in accounts subject to securities control agreements. The securities in such accounts would become restricted if Air Canada defaults on certain terms of the agreement.

Under the Credit Facility, Air Canada issued to the lenders, concurrently with the first drawdown, warrants for the purchase of Air Canada's Class A Variable Voting Shares or Class B Voting Shares representing an aggregate of 5% or 5 million of the total issued and outstanding shares as at the closing date of the Credit Facility, allocated among the lenders based on their pro rata lending commitments under the Credit Facility. These initial 5% warrants have an exercise price of $1.51 per share, are exercisable at any time and expire four years after the date of issuance. In the event that Air Canada did not grant additional security over certain assets within 90 days of closing, Air Canada was required to issue to the lenders additional warrants representing up to an additional 5% or 5 million of the total issued and outstanding shares (determined at the time of issuance of such additional warrants) with an average exercise price established based on a volume weighted average price 5 days before issuance, exercisable at any time and expiring four years after the date of issuance. These additional warrants were issued on October 19, 2009 and have an exercise price of $1.44 per share. The ascribed value of both the initial and additional warrants, totaling 10 million warrants, have been included in Contributed surplus on the Consolidated Statement of Financial Position as at September 30, 2009 in the amount of $7

Revolving Credit Facility

As discussed in Note 1C, in connection with the entering into of the Credit Facility, the revolving credit facility, which is further described in Note 9 (j) of the 2008 annual consolidated financial statements of the Corporation, was repaid in full during the third quarter of 2009.

Spare Parts Financing

During the first quarter of 2009, Air Canada received an additional $92 (US$75) principal under the original secured spare parts financing agreement, which is further described in Note 9 (g) of the 2008 annual consolidated financial statements of the Corporation. This financing bears interest at a rate of three month LIBOR plus the lenders incremental cost of funds rate and a margin of 3.00% (September 30, 2009 – 5.94%) and matures in 2014. The balance of the loan at September 30, 2009 of $143 is secured by spare parts and other assets with a carrying value of $271. Financing fees totaling $6 were recorded for these borrowings.

Spare Engine Financing

During the first quarter of 2009, Air Canada obtained an additional $46 (US$37) principal and included an additional 22 engines under the original secured financing agreement, which is further described in Note 9 (f) of the 2008 annual consolidated financial statements of the Corporation. This financing bears interest at a rate of three month LIBOR plus 3.40% (September 30, 2009 – 3.69%) and matures in 2013. As discussed in Note 1C, as a result of receiving the Credit Facility during the third quarter of 2009, the spare engine financing was partially repaid in the amount of $38. The balance of the loan at September 30, 2009 of $76 is secured by 10 engines with a carrying value of $115. Financing fees totaling $2 were recorded for these borrowings.

The principal and interest for the remaining spare engine financing is included in the maturity table in Note 11 – Commitments.

Pre-delivery Financing

During the first quarter of 2009, as a result of the delivery of a Boeing 777 aircraft, Air Canada made repayments of $83 (US$66) on the pre-delivery financing as described in Note 9 (m) to the 2008 annual consolidated financial statements of the Corporation. This was the final repayment on the pre-delivery financing.

Aeroplan Financing

During the second quarter of 2009 Air Canada and Aeroplan entered into a financing agreement for proceeds of $79. As discussed in Note 1C, in connection with the entering into of the Credit Facility the Aeroplan financing was repaid in full and terminated during the third quarter of 2009.

Boeing Aircraft

During the first quarter of 2009, Air Canada took delivery of a Boeing 777 aircraft. The aircraft was financed with guarantee support from the Export-Import Bank of the United States (“EXIM”). The initial principal of $136 (US$109) bears interest at a rate of three month LIBOR (September 30, 2009 – 0.46%) and matures in 2021. The loan is secured by the delivered aircraft with a carrying value of $139. Financing fees of $4 were recorded for this borrowing.

Sale Lease-back

During the first quarter of 2009, Air Canada entered into a sale lease-back transaction for a Boeing 777 aircraft, which was originally delivered in 2007 and debt financed. The proceeds from the transaction of $172 were used to repay the outstanding loan of $114. Air Canada recorded a charge of $17 in interest expense for this transaction including a prepayment fee of $14 and $3 for the write off of deferred financing charges. The gain on sale of the aircraft of $26 has been deferred and will be recognized in Depreciation and amortization over the term of the lease. The lease is accounted for as a capital lease with a 12 year term, with monthly lease payments.

Spare Parts Inventory

During the first quarter of 2009, Air Canada purchased $103 of spare parts inventory. Consideration for the purchase was in the form of the issuance of bills of exchange due in February 2010. Subsequent to the initial transaction, Air Canada has settled or holds as collateral certain of the bills and as a result the expected final payment in 2010 is $18 (US$17), as at October 31, 2009.

Disposals of and Provisions for Assets

There were no significant disposals or provisions during the third quarter of 2009.

During the second quarter of 2009:

- Air Canada recorded an impairment charge of $67 related to previously capitalized costs incurred pertaining to the development of a new reservation system, referred to as POLARIS. Air Canada is currently working towards the implementation of certain components of the solution such as web and fare technology but has suspended activity relating to the implementation of the reservation system.

- Air Canada sold two A340 aircraft for proceeds of $91 with a book value of $93, resulting in a loss on sale of $2. Air Canada made a repayment of $82 for the associated debt.

There were no significant disposals or provisions during the first quarter of 2009.

There were no significant disposals or provisions during the second and third quarters of 2008.

During the first quarter of 2008:

- Air Canada recorded an impairment charge of $38 on its fleet of B767-200 aircraft due to the revised retirement date of the aircraft.
- Air Canada sold an A319 aircraft for proceeds of $23 with a book value of $21, resulting in a gain on sale of $2.

3. PENSION AND OTHER BENEFIT LIABILITIES

Pension and Other Benefit Expense

Air Canada maintains several defined benefit and defined contribution plans providing pension, other postretirement and post-employment benefits to its employees, including those employees of Air Canada who are contractually assigned to work at Aeroplan and ACTS Aero.

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	**2008**	**2009**	**2008**
Pension benefit expense	$ 2	$ 22	$ -	$ 67
Other employee future benefits expense	20	26	60	78
	22	**48**	**60**	**145**
Amount charged to Aveos and Aeroplan	(6)	(10)	(23)	(30)
Net pension benefit and other employee future benefits expense	**$ 16**	**$ 38**	**$ 37**	**$ 115**

Employee benefits expense is reduced from 2008 levels as a result of revised actuarial assumptions. The actuarial assumptions used for recording pension expense under GAAP differ from those used in determining the solvency deficit.

In May 2009, Air Canada and Aeroplan reached an agreement with the Canadian Auto Workers (CAW) Local 2002 providing for a process for the approximately 750 Air Canada employees then working in the Aeroplan contact centres to choose to transition to employment at Aeroplan, effective June 1, 2009, or to remain employees of Air Canada. Employees at Air Canada work locations who become surplus to Air Canada's needs due to employees then working at Aeroplan contact centres who are senior to them choosing to remain employees of Air Canada were given the option to transition to employment at Aeroplan. Effective October 4, 2009, all affected employees have completed the transition to Aeroplan. For those employees transitioning to Aeroplan, their service, which largely determines benefit levels under the Air Canada pension and other employee benefit plans, will cease to accrue as of the date of employment with Aeroplan.

4. LABOUR RELATED PROVISIONS

Air Canada offers certain severance programs to certain employees from time to time. The cost of these programs is recorded within Operating expenses.

The following table outlines the changes to labour related provisions which are included in long-term employee liabilities:

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Beginning of period	$ 68	$ 62	$ 54	$ 66
Interest accretion	1	1	3	3
Charges recorded in wages, salaries, and benefits	-	7	24	20
Amounts disbursed	(7)	(8)	(19)	(27)
End of period	62	62	62	62
Current portion in Accounts payable and accrued liabilities	(25)	(27)	(25)	(27)
	$ 37	**$ 35**	**$ 37**	**$ 35**

5. SHARE INFORMATION

The issued and outstanding common shares of ACE as at September 30, 2009, along with potential common shares, are as follows:

Outstanding shares ('000s)	September 30 2009	December 31 2008
Issued and Outstanding		
Class A variable voting shares	25,510	25,614
Class B voting shares (1)	10,181	9,293
Total issued and outstanding	**35,691**	**34,907**
Potential common shares		
Convertible preferred shares (2)	-	11,863
Convertible senior notes (3)	2,600	13,133
Stock options (4)	54	61
Total potential common shares	**2,654**	**25,057**

(1) In May 2009, the Chairman, President and Chief Executive Officer of ACE requested that the after-tax amount of severance and benefits of $4.2 be paid to him in the form of shares of ACE. As a result, on May 22, 2009, the Chairman, President and Chief Executive Officer's after-tax amount was used to acquire and retain 784,350 Class B Voting Shares of ACE. Such subscription was effected through a grant of options that were exercised immediately upon the grant at an exercise price of $5.34, which is equal to the market price determined under the terms of the Stock Option Plan.

(2) In January 2009 and March 2009, the Corporation completed two substantial issuer bids to purchase for cancellation 9.3 million of its convertible preferred shares at a purchase price of $20 dollars per preferred share. The Corporation paid an aggregate purchase price of $186 for the shares tendered. In September 2009 the Corporation entered into an agreement with Morgan Stanley Canada Limited pursuant to which the Corporation indirectly acquired for cancellation all of its remaining 3.2 million convertible preferred shares at a price of $23 dollars per preferred share for an aggregate purchase price of $74. Refer to Note 2 for a detailed description of the loss on the repurchase of the convertible preferred shares.

(3) In January 2009, the Corporation completed a substantial issuer bid to purchase for cancellation 80% of its convertible senior notes outstanding as at December 31, 2008, at a purchase price of $900 dollars in cash for each $1,000 dollars principal amount of notes. The aggregate principal amount of the repurchased Convertible senior notes was $259. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 for the notes tendered.

Refer to the Note 12 - Subsequent Events for the announcement concerning ACE's redemption of its convertible senior notes.

(4) The Corporation's stock option plan is described in Note 13 to the 2008 annual consolidated financial statements. At September 30, 2009, a total of 54,443 stock options with a weighted exercise price of $14.49 were outstanding (61,230 stock options with a weighted exercise price of $14.11 outstanding as at December 31, 2008). The decrease of 6,787 stock options since December 31, 2008 is due to forfeitures experienced in Quarter 1 2009 of 3,167 and Quarter 3 2009 of 3,620.

(5) As described in Note 12 - Subsequent Events, ACE intends, subject to regulatory compliance, to launch a substantial issuer bid to repurchase $20 of its Class A Variable Voting Shares and Class B Voting Shares.

6. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Summary of Gain (Loss) on Financial Instruments Recorded at Fair Value

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	**2008**	**2009**	**2008**
Ineffective portion of fuel hedges	$ -	$ (58)	$ -	$ 24
Fuel derivatives not under hedge accounting	2	(54)	78	31
Cross currency interest rate swaps	-	19	-	6
Other	2	-	(5)	(1)
Gain (loss) on financial instruments recorded at fair value [(1)]	**$ 4**	**$ (93)**	**$ 73**	**$ 60**

(1) See Fuel Price Risk for a discussion of losses on fuel derivatives recorded in Other comprehensive income ("OCI").

Air Canada Risk Management

Liquidity risk

Liquidity risk is the risk that Air Canada will encounter difficulty in meeting obligations associated with its financial liabilities and other contractual obligations. Air Canada monitors and manages liquidity risk by preparing rolling cash flow forecasts, monitoring the condition and value of assets available to be used as security in financing arrangements, seeking flexibility in financing arrangements, and establishing programs to monitor and maintain compliance with terms of financing agreements. Air Canada's principal objective in managing liquidity risk is to maintain a minimum unrestricted cash balance in excess of a target liquidity level of 15% of annual operating revenues. As at September 30, 2009, the Cash and cash equivalents and Short-term investments were 12% of the preceding four quarters operating revenues (15% as at October 31, 2009, which includes the net proceeds under the offering as described in Note 12).

Air Canada management believes that the significant events as described in Note 1C improve Air Canada's current liquidity position. However risks remain such as those related to the current economic environment, including risks related to market volatility in the price of fuel, foreign exchange and interest rates and increased competitive pressures, as well as risks relating to restrictive terms under Air Canada's financing, credit card processing and other arrangements and other risks identified in Note 1 to the 2008 annual consolidated financial statements of the Corporation. The H1N1 influenza virus may also adversely impact demand for air travel. Air Canada is continuing to monitor the H1N1 influenza virus risk. While Air Canada has developed contingency plans related to the H1N1 influenza virus risk, it is unable to predict the likelihood of this risk materializing or the impact on Air Canada to the extent this risk does materialize. This note on liquidity risk updates Air Canada's year-end disclosures and should be read in conjunction with Note 1 to the 2008 annual consolidated financial statements of the Corporation, as updated for the events described above. Refer to Note 11 for a listing of commitments and the Corporation's maturity analysis.

Pension Funding Obligations

Air Canada maintains several defined benefit pension plans as described in Note 11 to the 2008 annual consolidated financial statements of the Corporation. As at December 31, 2008, Air Canada reported that the aggregate solvency deficit as at January 1, 2009 in the registered pension plans, which is used to determine funding requirements, was estimated to be approximately $3,200. As a result of updated information, including a change in the annuity rate applied by Canadian actuaries in discounting pension obligations, the aggregate solvency deficit was determined to be $2,835 in the actuarial valuation reports as at January 1, 2009 filed with the Office of the Superintendent of Financial Institutions (OSFI) on July 30, 2009.

In July 2009, the Federal Government of Canada adopted the Air Canada 2009 Pension Regulations. The Air Canada 2009 Pension Regulations relieve Air Canada from making any past service contributions (i.e. special payments to amortize the plan deficits) to its ten domestic defined benefit registered pension plans in respect of the period beginning April 1, 2009 and ending December 31, 2010. Thereafter, in respect of the period from January 1, 2011 to December 31, 2013, the aggregate annual past service contribution shall equal the lesser of (i) $150, $175, and $225 in respect of 2011, 2012, and 2013, respectively, on an accrued basis, and (ii) the maximum past service contribution permitted under the Tax Act.

The Air Canada 2009 Pension Regulations were adopted in coordination with the Pension MOUs identified in Note 1C. Pursuant to the Pension MOUs, on October 26, 2009, Air Canada issued to a trust, 17,647,059 Class B Voting Shares. This number of shares represented 15% of the shares of Air Canada issued and outstanding as at the date of the Pension MOUs and the date of issuance (after taking into account such issuance). All net proceeds of sale of such shares by the trust are to be contributed to the pension plans. The shares were recorded as a contribution to Deposits and other assets offset by an increase to Contributed surplus in the amount of $29 as at July 29, 2009. On October 26, 2009, upon the issuance of the shares to the trust, Air Canada reversed the contribution to Deposits and other assets and decreased its Pension and other benefit liabilities in the amount of $29. In addition, Air Canada reversed the contribution to Contributed surplus and recognized an increase to Share capital in the amount of $29. The effect of this transaction will be excluded from the ACE financial statements effective with the second dilution of ACE's interests in Air Canada upon closing of Air Canada's share and warrant offering on October 27, 2009 and the resulting deconsolidation of Air Canada. Refer to Note 12. For so long as the trust continues to hold at least 2% of the issued and outstanding shares of Air Canada, the trustee will have the right to designate one nominee (who shall not be a member or officer of any of Air Canada's Canadian-based unions) to Air Canada's board of directors, subject to completion of Air Canada's usual governance process for selection and confirmation of director nominees. Current service contributions will continue to be made in the normal course while the Air Canada 2009 Pension Regulations are in effect.

Based upon the effect of the Air Canada 2009 Pension Regulations, pension funding payments during 2009 will be approximately $407, a decrease of $49 compared to 2008.

Covenants in Credit Card Agreements

Air Canada has various agreements for the processing of customer credit card transactions, as further described in Note 1 to the 2008 annual consolidated financial statements of the Corporation. During the second quarter of 2009 and in July 2009, Air Canada entered into amendments with one of its principal credit card processors to amend certain credit card processing agreements under which the levels of unrestricted cash (as defined per the agreement and generally based on the balances as reported in Cash and cash equivalents and Short-term investments) required to be maintained by Air Canada is reduced to $800 (versus $1,300 prior to the amendments) and Air Canada provides the processor with deposits, to be accumulated over time, and security. The triggering event (which would require deposits of cash) based on a debt service coverage ratio is no longer applicable under the amended agreements. The agreements provide that should Air Canada maintain unrestricted cash of more than $1,200 for two consecutive months, the unrestricted cash requirement increases to $1,100 at which time the processor will return to Air Canada all deposits and security previously provided by Air Canada. This occurred during the third quarter of 2009, and as a result, no deposit was provided under these processing agreements as at September 30, 2009. As long as unrestricted cash remains at or above $1,100 at each month-end, Air Canada will have no obligation to provide deposits or security to the processor. Pursuant to the amendments entered into in July 2009, should Air Canada's unrestricted cash be less than $1,100 at any month-end, its obligation to provide deposits to the processor would be capped at an amount not to exceed $75, provided unrestricted cash is not less than $800.

Cargo Investigations and Proceedings

Air Canada is exposed to potential liabilities related to the proceedings and investigations of alleged anti-competitive cargo pricing activities, as described in Note 20 to the 2008 annual consolidated financial statements of the Corporation. This preliminary estimate recorded by Air Canada during 2008 is based upon the current status of the investigations and proceedings and Air Canada's assessment as to the potential outcome for certain of them. This provision does not address the proceedings and investigations in all jurisdictions, but only where there is sufficient information to do so. Air Canada management has determined it is not possible at this time to predict with any degree of certainty the outcome of all proceedings and investigations. Additional material provisions may be required. Amounts could become payable within the year and may be materially different than Air Canada management's preliminary estimate.

Fuel Price Risk

In order to manage its exposure to jet fuel prices and to help mitigate volatility in operating cash flows, Air Canada enters into derivative contracts with financial intermediaries. Air Canada uses derivative contracts on jet fuel and other crude oil-based commodities, heating oil and crude oil. Heating oil and crude oil commodities are used due to the relative limited liquidity of jet fuel derivative instruments on a medium to long-term horizon since jet fuel is not traded on an organized futures exchange. Air Canada does not purchase or hold any derivative financial instrument for speculative purposes.

As a result of a thorough analysis of the costs and benefits specific to the application of cash flow hedge accounting, Air Canada has elected to discontinue hedge accounting for all fuel derivatives effective the third quarter of 2009. The derivative instruments will continue to be recorded at fair value in each period with both realized and unrealized changes in fair value recognized immediately in earnings in non-operating income (expense). Amounts deferred to Accumulated Other Comprehensive Income ("AOCI") for derivatives previously designated under hedge accounting will be taken into fuel expense in the period in which the derivative was originally scheduled to mature.

There were no fuel derivative contracts entered into during the first nine months of 2009.

As of September 30, 2009, approximately 32% of Air Canada's anticipated purchases of jet fuel for the remainder of 2009 are hedged at an average West Texas Intermediate ("WTI")-equivalent capped price of US$105 per barrel and approximately 18% is subject to an average WTI-equivalent floor price of US$85 per barrel. Air Canada has also hedged approximately 13% of its 2010 anticipated jet fuel purchases in crude oil-based contracts hedged at an average capped price of US$110 per barrel and approximately 12% is subject to an average floor price of US$101 per barrel.

The following table outlines the notional volumes per barrel along with the weighted average floor and capped price for each year currently hedged by type of derivative instrument. These average contract prices represent the equivalent price in WTI using the forward prices for WTI, heating oil, and jet fuel as at September 30, 2009.

Derivative Instruments	Term	Volume (BBLs)	WTI-equivalent Average Floor Price (US$/bbl)		WTI-equivalent Average Capped Price (US$/bbl)	
Call options (a)	2009	750,000		n/a	$	121
	2010	400,000		n/a	$	134
Swaps (a)	2009	285,000	$	99	$	99
	2010	1,070,000	$	99	$	99
Collars (a)	2009	620,000	$	79	$	90
	2010	1,560,000	$	102	$	112

(a) Air Canada is expected to generate fuel hedging gains if oil prices increase above the average capped price and is exposed to fuel hedging losses if prices decrease below the average floor price.

During the third quarter of 2009, fuel derivative contracts cash settled with a fair value of $14 in favour of the counterparties ($76 in favour of the counterparties in the first nine months of 2009) ($76 in favour of Air Canada in the third quarter of 2008 and $220 in favour of Air Canada in the first nine months of 2008).

As at September 30, 2009, the net amount of existing losses reported in AOCI that are expected to be reclassified to net income (loss) during the following 12 months is $236 before tax. Due to the discontinuation of hedge accounting the AOCI balance related to fuel hedging contracts will be completely depleted as of December 31, 2010.

Air Canada currently holds within its hedging program derivative instruments, such as swaps and put options within collar structures, which may expose Air Canada to the potential of providing collateral deposits to its counterparties. When fuel prices decrease causing Air Canada's derivative position to be in a liability position below the set credit thresholds with counterparties, Air Canada is responsible for extending collateral to the counterparties. As at September 30, 2009 Air Canada had extended $105 of collateral to counterparties (December 31, 2008 – $328).

During the first quarter of 2009, Air Canada modified its fuel hedge portfolio with the termination of swap and put option contracts for $172, in favour of the counterparties. The collateral held by the counterparties covered the majority of the settlement amount, therefore minimal additional cash outflows resulted. Certain of these contracts were previously designated under hedge accounting. The value of the AOCI balance recognized in connection with these derivatives while designated under hedge accounting will be taken into fuel expense in the period where the derivative was scheduled to mature.

The following information summarizes the financial statement impact of fuel derivatives:

		Three Months Ended September 30 2009	Three Months Ended September 30 2008	Nine Months Ended September 30 2009	Nine Months Ended September 30 2008
Consolidated Statement of Operations					
Operating expenses					
Aircraft fuel	Realized effective gain (loss) on derivatives designated under hedge accounting	$ (94)	$ 64	$ (334)	$ 190
Non-operating income (expense)					
Gain (loss) on financial instruments recorded at fair value	Ineffective gain (loss) on derivatives designated under hedge accounting	n/a	$ (58)	$ -	$ 24
	Fair market value gain (loss) on economic hedges	$ 2	$ (54)	$ 78	$ 31
Consolidated Statement of Comprehensive Income (Loss)					
	Effective gain (loss) on derivatives designated under hedge accounting	n/a	$ (328)	$ (1)	$ 73
	Tax expense on effective gain	n/a	$ 84	$ -	$ (44)
	Reclassification of net realized (gain) loss on fuel derivatives designated under hedge accounting to Aircraft fuel expense	$ 94	$ (64)	$ 334	$ (190)
	Tax on reclassification	$ -	$ 20	$ 4	$ 61

		September 30 2009	December 31 2008
Consolidated Statement of Financial Position			
Current assets	Collateral deposits for fuel derivatives	$ 105	$ 328
Current liabilities*	Fair market value of fuel derivatives designated under hedge accounting	$ -	$ (405)
	Fair market value of fuel derivatives economic hedges	$ (94)	$ (15)
Shareholders' equity (AOCI)	Net loss from fuel derivatives designated under hedge accounting	$ (269)	$ (606)

* The balance is reflected within Current liabilities on the Consolidated Statement of Financial Position due to the counterparty's ability to terminate the derivatives at fair value at any time prior to maturity.

Aeroplan

On April 21, 2008 ACE sold a total of 20.4 million trust units of Aeroplan Income Fund ("AIF") at a price of $17.50 per unit representing total net proceeds to ACE of $343 and realized a gain on sale of $413 ($340 after tax). Following the sale, ACE held 9.9% of the issued and outstanding units of AIF.

On June 2, 2008, ACE sold the remaining trust units of AIF for total net proceeds to ACE of $349, and realized a gain on sale of $417 ($344 after tax). ACE no longer has an ownership interest in Aeroplan.

With the reduction of the ownership interest below 20% and the termination of the Securityholders' Agreement on May 9, 2008, ACE no longer had significant influence over Aeroplan. The equity investment ACE had in Aeroplan was classified as available-for-sale and the investment was adjusted to fair value. The adjustment to fair value recorded to OCI was $331, net of tax of $72, which was subsequently realized into income on June 2, 2008 as part of the final sale.

Jazz

On January 24, 2008 ACE sold a total of 13 million trust units of Jazz Air Income Fund ("JAIF") at a price of $7.45 per unit representing total net proceeds to ACE of $97 and realized a gain on sale of $89 ($71 net of taxes). Following the sale, ACE held 9.5% of the issued and outstanding units of JAIF.

On June 2, 2008, ACE sold its remaining trust units of JAIF for total net proceeds to ACE of $85, and realized a gain on sale of $78 ($62 net of taxes). Net realized gains of $65, net of tax of $14, were taken into income from OCI. ACE no longer has an ownership interest in Jazz.

With the reduction of the ownership interest below 20% and the termination of the Securityholders' Agreement on February 7, 2008, ACE no longer had significant influence over Jazz. The equity investment ACE had in Jazz was classified as available-for-sale and unrealized period changes in fair value were recorded in OCI. The adjustment to fair value recorded in OCI amounted to $71, net of tax of ($15) during Quarter 1, 2008. During Quarter 2, 2008, the period change in fair value of ($6), net of tax of $1, was recorded in OCI.

7. INCOME TAXES

Components of the provision for income taxes in the Corporation's consolidated statement of operations are as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Recovery of (provision for) income taxes before under noted items	$ (1)	$ (8)	$ 1	$ (37)
Repurchase of ACE convertible senior notes	-	-	(8)	-
Disposal of Aeroplan units	-	-	-	(146)
Disposal of Jazz units	-	-	-	(34)
Provision for income taxes	**$ (1)**	**$ (8)**	**$ (7)**	**$ (217)**

Refer to Note 6 for future income taxes recorded in other comprehensive income related to fuel derivatives designated under hedge accounting.

8. SEGMENT INFORMATION

Composition of Business Segments

ACE has two reportable segments: Air Canada and Corporate Items and Eliminations ("CIE").

CIE includes the corporate, financing and investing activities of ACE. ACE's investments in Aeroplan, Jazz and ACTS Aero were changed in 2007 from the consolidation to equity method of accounting reported under the CIE segment. As of May 9, 2008 and February 7, 2008, ACE no longer equity accounted for Aeroplan and Jazz, respectively, but distributions from Aeroplan and Jazz were recorded in the CIE segment. Since June 2, 2008, subsequent to the sale of all remaining AIF and JAIF units, ACE has no ownership interest in Aeroplan or Jazz. Future income taxes are recorded within the applicable taxable entities and are not allocated to non-taxable entities.

Segment financial information has been prepared consistent with how financial information is produced internally for the purposes of making operating decisions. Segments negotiate transactions between each other as if they were unrelated parties.

A reconciliation of the total amounts reported by each business segment to the applicable amounts in the consolidated financial statements follows:

	Three Months Ended September 30					
	Air Canada	CIE	2009 Total ACE	Air Canada	CIE	2008 Total ACE
Operating revenues						
Passenger	$ 2,400	$ -	$ 2,400	$ 2,766	$ -	$ 2,766
Cargo	92	-	92	139	-	139
Other	178	-	178	170	-	170
Total revenues	**2,670**	**-**	**2,670**	**3,075**	**-**	**3,075**
Operating expenses						
Aircraft fuel	682	-	682	1,064	-	1,064
Wages, salaries and benefits	437	-	437	472	7	479
Airport and navigation fees	272	-	272	275	-	275
Capacity purchase with Jazz	246	-	246	243	-	243
Depreciation and amortization	171	(1)	170	176	(2)	174
Aircraft maintenance	183	-	183	127	-	127
Food, beverages and supplies	82	-	82	86	-	86
Communications and information technology	70	-	70	69	-	69
Aircraft rent	81	-	81	67	-	67
Commissions	51	-	51	54	-	54
Other	327	1	328	330	2	332
Total operating expenses	**2,602**	**-**	**2,602**	**2,963**	**7**	**2,970**
Operating income (loss) before under noted item	**68**	**-**	**68**	**112**	**(7)**	**105**
Provision for cargo investigation	-	-	-	**-**	**-**	**-**
Operating income (loss)	**68**	**-**	**68**	**112**	**(7)**	**105**
Non-operating income (expense)						
Interest income	2	1	3	13	6	19
Interest expense	(87)	-	(87)	(72)	(15)	(87)
Interest capitalized	1	-	1	6	-	6
Gain on assets	1	-	1	-	-	-
Loss on repurchase of ACE convertible senior notes and preferred shares	-	(10)	(10)	-	-	-
Gain (loss) on financial instruments recorded at fair value	4	-	4	(93)	-	(93)
Equity and other investment loss	-	-	-	-	(19)	(19)
Other	(4)	-	(4)	(1)	-	(1)
	(83)	(9)	(92)	(147)	(28)	(175)
Loss before the following items	**(15)**	**(9)**	**(24)**	**(35)**	**(35)**	**(70)**
Non-controlling interest	(3)	(69)	(72)	(2)	32	30
Foreign exchange gain (loss)	295	-	295	(87)	-	(87)
Provision for income taxes	-	(1)	(1)	(8)	-	(8)
Segment net income (loss) for the period	**$ 277**	**$ (79)**	**$ 198**	**$ (132)**	**$ (3)**	**$ (135)**

** Aeroplan and Jazz equity investment income is recorded up to May 9, 2008 and February 7, 2008 respectively. Subsequent to these effective dates, distribution income from Aeroplan and Jazz was recorded within CIE until June 2, 2008. Equity income of nil relating to ACE's equity investments is included in Equity and other investment loss ($(19) for the period ended September 30, 2008).*

	Nine Months Ended September 30					
			2009 Total			2008 Total
	Air Canada	CIE	ACE	Air Canada	CIE	ACE
Operating revenues						
Passenger	$ 6,469	$ -	$ 6,469	$ 7,531	$ -	$ 7,531
Cargo	248	-	248	402	-	402
Other	674	-	674	650	1	651
External revenue	**7,391**	**-**	**7,391**	**8,583**	**1**	**8,584**
Inter-segment revenue	-	-	-	1	(1)	-
Total revenues	**7,391**	**-**	**7,391**	**8,584**	**-**	**8,584**
Operating expenses						
Aircraft fuel	1,847	-	1,847	2,627	-	2,627
Wages, salaries and benefits	1,333	4	1,337	1,433	29	1,462
Airport and navigation fees	743	-	743	771	-	771
Capacity purchase with Jazz	746	-	746	711	-	711
Depreciation and amortization	495	(5)	490	520	(6)	514
Aircraft maintenance	557	-	557	502	-	502
Food, beverages and supplies	222	-	222	244	-	244
Communications and information technology	229	-	229	214	-	214
Aircraft rent	250	-	250	199	-	199
Commissions	140	-	140	154	-	154
Other	1,062	7	1,069	1,102	8	1,110
Total operating expenses	**7,624**	**6**	**7,630**	**8,477**	**31**	**8,508**
Operating income (loss) before under noted item	**(233)**	**(6)**	**(239)**	**107**	**(31)**	**76**
Provision for cargo investigation	-	-	-	**(125)**	**-**	**(125)**
Operating loss	**(233)**	**(6)**	**(239)**	**(18)**	**(31)**	**(49)**
Non-operating income (expense)						
Interest income	12	2	14	46	21	67
Interest expense	(286)	(6)	(292)	(231)	(39)	(270)
Interest capitalized	4	-	4	31	-	31
Gain (loss) on assets	(70)	-	(70)	(29)	990	961
Loss on repurchase of ACE convertible senior notes and preferred shares	-	(43)	(43)	-	-	-
Gain on financial instruments recorded at fair value	73	-	73	60	-	60
Equity and other investment loss	-	-	-	-	(2)	(2)
Other	(5)	-	(5)	(3)	1	(2)
	(272)	(47)	(319)	(126)	971	845
Income (loss) before the following items	**(505)**	**(53)**	**(558)**	**(144)**	**940**	**796**
Non-controlling interest	(11)	(9)	(20)	(8)	70	62
Foreign exchange gain (loss)	549	-	549	(128)	-	(128)
Provision for income taxes	(1)	(6)	(7)	(18)	(199)	(217)
Segment net income (loss) for the period	**$ 32**	**$ (68)**	**$ (36)**	**$ (298)**	**$ 811**	**$ 513**

**Aeroplan and Jazz equity investment income is recorded up to May 9, 2008 and February 7, 2008 respectively. Subsequent to these effective dates, distribution income from Aeroplan and Jazz was recorded within CIE until June 2, 2008. Equity income of nil relating to ACE's equity investments is included in Equity and other investment loss ($(7) for the period ended September 30, 2008).*

Included within Depreciation and amortization is depreciation of property and equipment related to the Air Canada segment for the three months ended September 30, 2009 of $155 (nine months ended September 30, 2009 - $446) (three months ended September 30, 2008 - $163, nine months ended September 30, 2008 - $483).

A reconciliation of the total amounts reported for Passenger revenue and Cargo revenue on the Consolidated Statement of Operations is as follows:

Passenger revenues	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Canada	$ 998	$ 1,150	$ 2,708	$ 3,148
US Transborder	406	467	1,236	1,455
Atlantic	588	631	1,345	1,489
Pacific	256	328	630	775
Other	152	190	550	664
	$ 2,400	**$ 2,766**	**$ 6,469**	**$ 7,531**

Cargo revenues	Three Months Ended September 30		Nine Months Ended September 30	
	2009	2008	2009	2008
Canada	$ 17	$ 27	$ 47	$ 77
US Transborder	3	5	10	14
Atlantic	30	49	89	167
Pacific	32	46	74	110
Other	10	12	28	34
	$ 92	**$ 139**	**$ 248**	**$ 402**

Passenger and cargo revenues are based on the actual flown revenue for flights with an origin and destination in a specific country or region. Atlantic refers to flights that cross the Atlantic Ocean with origins and destinations principally in Europe. Pacific refers to flights that cross the Pacific Ocean with origins and destinations principally in Asia. Other passenger and cargo revenues refer to flights with origins and destinations principally in South America, South Pacific, and the Caribbean. Other operating revenues are principally derived from customers located in Canada.

Segment Asset Information

	September 30, 2009		
	Air Canada	CIE	Total
Cash and cash equivalents	$ 1,042	$ 134	$ 1,176
Short-term investments	167	-	167
	$ 1,209	**$ 134**	**$ 1,343**
Additions to capital assets for the three months	$ 34	$ -	$ 34
Total assets	**$ 10,774**	**$ (159)**	**$ 10,615**

	December 31, 2008		
	Air Canada	CIE	Total
Cash and cash equivalents	$ 499	$ 808	$ 1,307
Short-term investments	506	-	506
	$ 1,005	**$ 808**	**$ 1,813**
Additions to capital assets for the twelve months	$ 883	$ -	$ 883
Total assets	**$ 11,364**	**$ 507**	**$ 11,871**

The total assets of CIE are net of the inter-company eliminations between each of the segments.

9. RELATED PARTY TRANSACTIONS

Air Canada and Aveos entered into an agreement dated October 28, 2008 pursuant to which Air Canada has agreed to temporarily extend payment terms to Aveos under certain related party agreements. In exchange for the extended payment terms, certain letters of credit related to the Pension and Benefits Agreement, as described in Note 21 of the 2008 annual consolidated financial statements of the Corporation, were cancelled. The extended payment terms to Aveos were originally scheduled to begin reducing in May 2009 with a corresponding return of the letters of credit to Aveos.

As a result of amendments during the year, the payment terms were extended. The extended payment terms will be reduced starting in November 2009 with the expiration of the extended payment terms to be completed over the following six months. During April 2010, following expiration of the extended payment terms, the letters of credit are to be reinstated to the levels then required under the Pension and Benefits Agreement between the two parties.

ACE is a participant lender in the Credit Facility as described in Note 2. ACE's participation in the Credit Facility represents $150 of the outstanding loan of $600 as at September 30, 2009. The participant lenders participate on a pro-rata basis with respect to any warrants and principal and interest payments. ACE's pro-rata share of interest expense reported during the period amounts to $3.

10. JAZZ CAPACITY PURCHASE AGREEMENT

Air Canada and Jazz are parties to a capacity purchase agreement ("Jazz CPA") pursuant to which Air Canada purchases substantially all of Jazz's fleet capacity based on predetermined rates, in addition to reimbursing Jazz, without mark-up, for certain pass-through costs as defined in the Jazz CPA which include fuel, airport and user fees and other costs. The fees include both a variable component that is dependent on Jazz aircraft utilization and a fixed component and are recorded in the applicable category within the operating expenses in the results of Air Canada.

The following table outlines Jazz CPA and pass-through costs for the period:

	Three Months Ended September 30		Nine Months Ended September 30	
	2009	**2008**	**2009**	**2008**
Expenses from Jazz CPA	$ 246	$ 243	$ 746	$ 711
Pass through fuel expense from Jazz CPA	71	131	188	339
Pass through airport expense from Jazz CPA	52	53	149	153
Pass through other expense from Jazz CPA	5	4	25	25
	$ 374	**$ 431**	**$ 1,108**	**$ 1,228**

Effective August 1, 2009, Air Canada reached an agreement amending the terms related to Air Canada's capacity purchase agreement with Jazz Air LP ("Jazz") which provides for a reduction to rates paid under the agreement.

11. COMMITMENTS

Boeing

During the third quarter of 2009 Air Canada and The Boeing Company ("Boeing") agreed to amend the purchase agreement for the Boeing 787 aircraft to reduce the number of options for Boeing 787 aircraft by ten, from 23 to 13, and to provide for purchase rights for ten Boeing 787 aircraft. Air Canada continues to have 37 firm orders for Boeing 787 aircraft. Air Canada and Boeing also agreed to amend certain commercial terms, including revisions to delivery dates. Air Canada's first Boeing 787 aircraft is now scheduled for delivery in the second half of 2013. Air Canada continues to hold purchase rights for 18 Boeing 777 aircraft.

For the firm aircraft orders, Air Canada has financing commitments from Boeing and the engine manufacturer covering 31 of the 37 Boeing 787 aircraft. The financing terms for 28 out of the 31 covered aircraft is for 80% of the aircraft delivery price and the term to maturity is 12 years with straight-line principal repayments. For the remaining three out of the 31 covered aircraft, the financing under the commitment covers up to 90% of the capital expenditure and the term to maturity is 15 years with principal payments made on a mortgage style basis resulting in equal installment payments of principal and interest over the term to maturity.

Embraer

During the first nine months of 2009, all remaining Embraer 190 series exercisable options expired (December 31, 2008 – 7 exercisable options remaining).

Aircraft Interior Refurbishment Program

In addition to acquiring new aircraft, Air Canada commenced a major refurbishment of the interior of its existing aircraft in April 2006, which was completed during the second quarter of 2009. Air Canada has completed the refurbishment of all its Airbus A319, A320, A321 and A330 aircraft, and 27 of its 30 Boeing 767-300 aircraft, for a total of 121 aircraft. Air Canada will complete a light aircraft interior renovation of the three remaining Boeing 767-300 aircraft by the end of 2009. The Embraer and Boeing 777 aircraft have been delivered with the new seats and entertainment systems already installed. The capital expenditures associated with this program are amortized over a five-year period.

Capital Commitments

The estimated aggregate cost of the future firm deliveries and other capital purchase commitments as at September 30, 2009 approximates $4,926. US dollar amounts are converted using the September 30, 2009 noon day rate of CDN$1.0722. The estimated aggregate cost of aircraft is based on delivery prices that include estimated escalation and, where applicable, deferred price delivery payment interest.

Remainder of 2009	2010	2011	2012	2013	Thereafter	Total
$ 11	$ 60	$ 53	$ 137	$ 753	$ 3,912	$ 4,926

Operating Lease Commitments

During the third quarter of 2009, Air Canada took delivery of a Boeing 777 aircraft. The aircraft was financed under an operating lease with International Lease Finance Corp (“ILFC”). The total lease commitment of $152 has been included in the table below.

As at September 30, 2009 the future minimum lease payments under existing operating leases of aircraft and other property amount to $2,110 using the September 30, 2009 noon day rate of CDN$1.0722.

	Remainder of 2009	2010	2011	2012	2013	Thereafter	Total
Aircraft	$ 79	$ 317	$ 281	$ 263	$ 240	$ 656	$ 1,836
Other property	15	42	38	35	24	120	274
Total	**$ 94**	**$ 359**	**$ 319**	**$ 298**	**$ 264**	**$ 776**	**$ 2,110**

The above minimum lease payments include residual value guarantees, except for those for which Air Canada has obtained residual value support.

Maturity Analysis

ACE

ACE's principal and interest repayment requirements as at September 30, 2009 on Long-term debt obligations consist of its Convertible Senior Notes repayable on June 1, 2010 in the amount of $64. This date represents the first date the holders may require ACE to purchase all or a portion of the Convertible Senior Notes at a purchase price equal to 100% of the principal amount of the notes to be purchased. Interest repayment obligations associated with the Convertible Senior Notes amount to $1 for the remainder of 2009 and $1 in 2010.

As described in Note 12 - Subsequent events, on November 5, 2009, the ACE Board authorized the redemption for cash of the Convertible Senior Notes. The notes will be repurchased by December 14, 2009. Following the redemption, ACE will not have any remaining interest repayment obligations associated with the Convertible Senior Notes.

Air Canada

Principal and interest repayment requirements as at September 30, 2009 on Long-term debt and capital leases are as follows:

	Remainder of 2009	2010	2011	2012	2013	Thereafter	Total
Principal	$ 107	$ 506	$ 799	$ 566	$ 652	$ 2,435	$ 5,065
Interest	86	320	272	226	178	447	1,529
	$ 193	**$ 826**	**$ 1,071**	**$ 792**	**$ 830**	**$ 2,882**	**$ 6,594**

The maturity analysis is based on contractual undiscounted cash flows and is based on interest rates and the applicable foreign exchange rate effective as at September 30, 2009.

Principal repayments in the table above exclude transaction costs which are offset against Long-term debt and capital leases in the Consolidated Statement of Financial Position.

12. SUBSEQUENT EVENTS

ACE Strategy Update

Over the past few months, the ACE Board has continued to consider alternatives to maximize the return to shareholders. On November 5, 2009, the Board authorized the redemption for cash of the convertible senior notes and the required notice is being sent to the Trustee. The notes will be repurchased by December 14, 2009. In addition, consistent with the overall objective of returning excess cash to shareholders, ACE intends, subject to regulatory compliance, to launch a substantial issuer bid (the "Offer") to repurchase $20 of its Class A Variable Voting Shares and Class B Voting Shares. Further details will be announced prior to the launch of the Offer. Going forward, the Board will continue to review alternatives to maximize the return to shareholders, including alternatives for its debt and equity interests in Air Canada.

Air Canada Pension MOUs

As described in Note 6, in Quarter 3 2009 Air Canada entered into the Pension MOUs providing for Air Canada to issue 17,647,059 Class B Voting Shares representing a fully diluted 15% equity ownership of Air Canada, established as of the date of the Pension MOUs, to a trust (the "Trust") with all net proceeds of the eventual sale of the shares held by the trust to be contributed to the pension plans. As a result, on October 26, 2009, Air Canada issued 17,647,059 Class B Voting Shares to the Trust.

Air Canada Share and Warrant Offering

On October 27, 2009 Air Canada completed a previously announced bought deal public offering pursuant to which it sold to an underwriting syndicate 160,500,000 units (the "Units") of Air Canada at a price of $1.62 per Unit for aggregate gross proceeds to Air Canada of $260 (net proceeds of $248 after expenses and underwriter fees). Each Unit is comprised of one Class A variable voting share (the "Variable Voting Shares") or one Class B voting share (the "Voting Shares", and, together with the Variable Voting Shares, the "Shares") of Air Canada, and one-half of one share purchase warrant. Each whole share purchase warrant is defined as a "Warrant". Each Warrant will entitle the holder thereof to acquire one Variable Voting Share or one Voting Share (each, a "Warrant Share") at an exercise price of $2.20 per Warrant Share, at any time prior to 36 months following October 27, 2009. In the event that, prior to the time of expiry of the Warrants, the 20-day volume weighted average trading price of the Variable Voting Shares on the Toronto Stock Exchange ("TSX") is equal to or greater than $4.00 or the 20-day volume weighted average trading price of the Voting Shares on the TSX is equal to or greater than $4.00 (each, an "Acceleration Event"), Air Canada shall have the right, at its option, within ten (10) business days after the Acceleration Event, to accelerate the time of expiry of the Warrants.

In addition to the amounts reported above, the Underwriters have been granted an over-allotment option to purchase up to an additional 24,075,000 Shares and/or 12,037,500 Warrants, exercisable in whole or in part at any time until November 27, 2009 which, if exercised, would further reduce ACE's ownership interest in Air Canada.

As a result of the shares issued by Air Canada completed on October 26, 2009 and October 27, 2009, ACE's ownership interest in Air Canada was reduced from 75% to 27% such that ACE ceases to control Air Canada. Effective October 27, 2009, ACE will no longer consolidate Air Canada's financial position, operating results and cash flows. ACE's investment in Air Canada will be accounted for using the equity method whereby the Air Canada investment carrying value is adjusted to include the Corporation's pro rata share of post-dilution earnings.