ACE AVIATION

2009

Management's Discussion and Analysis of Results of Operations and Financial Condition

February 11, 2010

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1. Preface

ACE Aviation Holdings Inc. ("ACE"), which was incorporated on June 29, 2004, is an investment holding company of aviation interests. ACE is listed on the Toronto Stock Exchange ("TSX") where its Class A variable voting shares and Class B voting shares are traded under the symbols ACE.A and ACE.B, respectively.

On December 14, 2009, ACE redeemed the remaining convertible senior notes for an aggregate purchase price of $64 million. In addition, on January 6, 2010, ACE completed a substantial issuer bid and purchased $20 million of its shares at a purchase price of $6.20 per share. 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.

ACE's financial statements have been prepared on a going concern basis of presentation. The going concern basis of presentation assumes continuity of operations, realization of assets and satisfaction of liabilities in the ordinary course of business. Effective October 27, 2009, ACE no longer consolidates Air Canada's financial position, operating results and cash flows. ACE's investment in Air Canada has since been 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.

This MD&A should be read in conjunction with ACE's audited consolidated financial statements and notes for 2009. Reference to "Corporation" in this MD&A 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. Except as otherwise noted, all monetary amounts are stated in Canadian dollars. For an explanation of certain terms used in this MD&A, refer to section 18 "Glossary of Terms". Except as otherwise noted, this MD&A is current as of February 11, 2010. Certain comparative figures have been reclassified to conform to the financial statement presentation adopted in the current period.

Forward-looking statements are included in this MD&A. See "Caution Regarding Forward-Looking Information" in section 2 of this MD&A for a discussion of risks, uncertainties and assumptions relating to these statements. For a description of the risks relating to ACE, see section 15 "Risk Factors" of this MD&A.

The ACE Audit, Finance & Risk Committee has reviewed this MD&A and the 2009 audited consolidated financial statements and notes and ACE's Board of Directors approved these documents prior to their release. For further information on ACE's public disclosure file, including ACE's Annual Information Form, please consult SEDAR at www.sedar.com, or ACE's website at www.aceaviation.com.

2. Caution Regarding Forward-Looking Information

ACE's public communications may include written or oral forward-looking statements within the meaning of applicable securities laws. Such statements are included in this MD&A and may be included in other filings with regulatory authorities and securities regulators. Forward-looking statements relate to analyses and other information that are based on forecasts of future results and estimates of amounts not yet determinable. These statements may involve, but are not limited to, comments relating to strategies, expectations, planned operations or future actions. 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.

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, amongst other things, changing external events and general uncertainties of the business. Actual results may differ materially from results indicated in forward-looking statements due to a number of factors, including without limitation, industry, market, credit and economic conditions, the ability to reduce operating costs and secure financing, pension issues, energy prices, currency exchange and interest rates, employee and labour relations, competition, war, terrorist acts, epidemic diseases, insurance issues and costs, changes in demand due to the seasonal nature of the business, supply issues, changes in laws, regulatory developments or proceedings, pending and future litigation and actions by third parties as well as the factors identified throughout this MD&A and, in particular, those identified in section 15 “Risk Factors” of this MD&A. The forward-looking statements contained in this MD&A represent ACE's expectations as of the date of this MD&A, 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, except as required under applicable securities regulations.

3. ACE's Assets, Obligations and Net Assets at Fair Value

The following table presents the assets and liabilities of ACE at fair value as at January 31, 2010 and December 31, 2009. The objective of this information is to present information on the assets and liabilities of ACE as certain of ACE's shareholders use this information to assess ACE's financial position. This non-GAAP information including net assets at fair value is not prepared in accordance with standards prescribed by Canadian generally accepted accounting principles ("GAAP") and may not be comparable to other similar information provided by other companies. This is not presented as a substitute for the balance sheet of ACE which has been prepared in accordance with Canadian GAAP and has been prepared on a going concern basis. Further, this presentation is not intended to reflect ACE's net asset value on a liquidation basis and does not purport to represent the fair value of ACE as a whole or per share.

(Canadian dollars in millions)	January 31 2010	December 31 2009
Cash and cash equivalents (2)	$ 50	$ 71
Interest receivable on Air Canada loan	5	3
Air Canada shares (1)	100	99
Air Canada secured loan (1)	150	150
	305	323
Current obligations	(3)	(3)
Contingencies (3)	-	-
	(3)	(3)
Net assets at fair value (2)	**$ 302**	**$ 320**
Net assets at fair value per share – Basic (2)	**$ 9.30**	**$ 8.97**

(1) *As at January 31, 2010, ACE's held a 27.0% ownership interest in Air Canada consisting of 75 million Class B Voting Shares and held a secured loan of $150 million to Air Canada as part of the Air Canada 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. An additional 1,250,000 warrants were issued to ACE on October 19, 2009 with an exercise price of $1.44 per share, exercisable at any time, and expiring four years after the date of issuance. The Air Canada shares of $100 million as at January 31, 2010 and $99 million as at December 31, 2009 are based on the market prices of $1.33 per Air Canada Class B share as at January 31, 2010 and $1.32 per Air Canada Class B share as at December 31, 2009, as quoted on the TSX. The Air Canada secured loan is included in the table above at its principal amount of $150 million.*

(2) *As detailed in section 9.5 of this MD&A, on January 6, 2010 ACE completed a substantial issuer bid and purchased $20 million of its shares at a purchase price of $6.20 per share. As at January 31, 2010, there were 32,465,484 issued and outstanding common shares (December 31, 2009, 35,691,289)*

(3) *ACE is subject to ongoing audits by Canadian tax authorities for the years 2005 to 2009 and no liabilities that may arise have been included above. See Section 12 for Off-balance sheet arrangements. Should ACE proceed to a liquidation in the future, additional costs and other liabilities may arise.*

4. Significant Events

The following significant events occurred during the period January 1, 2009 to February 11, 2010:

On January 19, 2009, ACE announced that $259 million principal amount of 4.25% convertible senior notes due 2035 were deposited and taken up under a substantial issuer bid, at a purchase price of $900 for each $1,000 principal amount of notes, for an aggregate purchase price of $233 million. ACE also announced on January 19, 2009 that 8.3 million convertible preferred shares, at a purchase price of $20.00 per preferred share, were deposited and taken up under a substantial issuer bid, for an aggregate purchase price of $166 million.

On March 19, 2009, ACE announced that it had taken up and accepted for purchase and cancellation 1.0 million of its convertible preferred shares, at a purchase price of $20.00 per preferred share, for an aggregate purchase price of $20 million in accordance with the terms of the substantial issuer bid.

On July 29, 2009, ACE announced that its participation in the Air Canada credit facility of $600 million, amounted to $150 million. ACE's $150 million loan participation is repayable in equal consecutive quarterly installments of $7.5 million starting August 1, 2010, with a final payment of $30 million due by the fifth anniversary of the initial drawdown. Under the Credit Facility, ACE received 1,250,000 warrants on July 30, 2009 for the purchase of Air Canada's 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. An additional 1,250,000 million warrants were issued to ACE under the credit facility on October 19, 2009 and have an exercise price of $1.44 per share, exercisable at any time, and expiring four years after the date of issuance.

On September 21, 2009, ACE announced it had entered into an agreement with Morgan Stanley Canada Limited pursuant to which ACE indirectly acquired for cancellation all of its remaining 3.2 million preferred shares at a price of $23.00 per preferred share for an aggregate purchase price of $74 million.

On October 27, 2009, Air Canada completed an offering of 160,500,000 units with each unit comprised of one share and one-half of a warrant. On October 26, 2009, Air Canada issued 17.6 million shares under the pension funding agreements, announced in July 2009. As a result of these share issuances by Air Canada, ACE's ownership in Air Canada was reduced from 75% to 27%. As at January 31, 2010, there were 90.25 million warrants outstanding to acquire Air Canada shares at exercise prices between $1.44 and $2.20.

Effective October 27, 2009, ACE no longer consolidates Air Canada's financial position, operating results and cash flows. ACE's investment in Air Canada has since been 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 and other comprehensive income.

On December 14, 2009, ACE paid an aggregate purchase price of $64 million for the redemption of its remaining convertible senior notes.

On January 6, 2010, ACE announced that it had accepted for purchase and cancellation a total of 1,401,094 Class A Variable Voting Shares and 1,824,711 Class B Voting Shares at $6.20 per share for an aggregate purchase price of $20 million in accordance with the terms of the substantial issuer bid.

5. Investments

As at December 31, 2009, ACE's principal investments are:

- a 27.0% (75 million Class B Voting Shares) ownership interest in Air Canada; and
- a secured loan of $150 million to Air Canada.

ACE also has a 28.4% interest in Aero Technical Support & Services Holdings sarl ("ACTS Aero"), which owns 100% of Aveos Fleet Performance Inc. ("Aveos"). As at December 31, 2009, the carrying value of ACE's investment in ACTS Aero is nil.

These investments are more fully described below. During 2008, ACE completed the sales of its remaining investments in Aeroplan and Jazz.

Air Canada

Overview

Air Canada includes the passenger and cargo transportation services business operated by Air Canada and related ancillary services.

These services are provided through Air Canada, Air Canada Cargo Limited Partnership ("Air Canada Cargo") up to and including November 30, 2009, ACGHS Limited Partnership ("Air Canada Ground Handling Services" or "ACGHS") up to and including November 30, 2009 and Touram Limited Partnership ("Air Canada Vacations").

Effective December 1, 2009, the operations of Air Canada Cargo and Air Canada Ground Handling Services, previously operated by wholly-owned subsidiaries of Air Canada, were wound up into Air Canada and are now operated as divisions of Air Canada. These wind-ups had no impact on the consolidated financial statements.

Air Canada is Canada's largest domestic and international airline and the largest provider of scheduled passenger services in the Canadian market, the Canada-US transborder market as well as the international markets to and from Canada. Certain of the scheduled passenger services offered on domestic and Canada-US transborder routes are provided by Jazz Air LP through a capacity purchase agreement between Air Canada and Jazz. Through Air Canada's global route network, virtually every major market throughout the world is served either directly or through the Star Alliance network. In addition, Air Canada provides certain passenger charter services.

Air Canada offers air cargo services on domestic and US transborder routes using cargo capacity on aircraft operated by Air Canada and Jazz. (Prior to December 1, 2009, these services were provided by Air Canada Cargo). Air Canada offers international cargo services on routes between Canada and major markets in Europe, Asia, South America and Australia using cargo capacity on Boeing 777 and other wide body aircraft operated by Air Canada.

Up until December 1, 2009, Air Canada Ground Handling Services provided passenger handling services to Air Canada, Jazz and other airlines with a primary focus on Canadian stations. Services covered included passenger check-in, gate management, baggage and cargo handling and processing, cabin cleaning, de-icing as well as aircraft ramp services. Effective December 1, 2009 with the wind-up of ACGHS into Air Canada, Air Canada offers these services directly.

Air Canada Vacations is one of Canada's leading tour operators. Based in Montreal and Toronto, it operates its business in the outgoing leisure travel market (Caribbean, Mexico, USA, Europe, South America and Asia) by developing, marketing and distributing vacation travel packages and services through a network of independent travel agencies in Canada as well as through the Air Canada Vacations website, aircanadavacations.com.

Summary of significant events

During 2009, Air Canada entered into the following significant transactions in an effort to mitigate liquidity risks:

- Completed a share and warrant public offering for net proceeds of $249 million.

- Completed a secured term credit facility (the "Credit Facility") for financing proceeds of $600 million, less fees of $20 million. The Credit Facility is a five-year facility, with the first principal repayment due in August 2010, and currently bears interest at 12.75%. Under the Credit Facility, 10 million warrants were also issued which entitle the debt holders to acquire up to 10 million shares in Air Canada. ACE provided financing of $150 million with respect to the Credit Facility, as further described below.

- 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 million, $175 million, and $225 million 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 (in both cases 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.

- Total cash flows to Air Canada during the full year 2009 from borrowing, including the Credit Facility described above, amounted to $926 million, proceeds from sale of assets amounted to $103 million, proceeds from sale-leaseback transactions amounted to $552 million and proceeds from contractual commitments amounted to $230 million. Reductions of long-term debt during 2009, which include repayments as a result of certain of the above financings and sale-leasebacks, amounted to $1,237 million.

At December 31, 2009, Air Canada had Cash and cash equivalents and Short-term investments of $1,407 million ($1,005 million as at December 31, 2008).

Guarantee of Air Canada obligation

On May 7, 2009, ACE intervened into the employment agreement between Air Canada and Mr. Calin Rovinescu, its President and Chief Executive Officer, to guarantee the payments required of Air Canada under the agreement.

In addition, ACE agreed to cause to be issued an irrevocable bank letter of credit to a maximum of $5 million. At December 31, 2009, as agreed by the parties, the letter of credit had not been issued.

Loan receivable from Air Canada

On July 29, 2009, ACE participated in the $600 million Air Canada Credit Facility with several other lenders providing financing of $150 million which represented 25% 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 after the date of issuance.

The terms of the Credit Facility permit, on or before the first anniversary of the Air Canada Credit Facility and subject to satisfaction of certain conditions, Air Canada to request an increase to the facility by up to an additional $100 million by obtaining new commitments from either the existing or new lenders. ACE's pro-rata share of the Credit Facility is repayable in 16 consecutive quarterly installments commencing in August 2010 of $7.5 million with the final installment of $30 million due in July 2014.

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 December 31, 2009). The Credit Facility can be repaid at any time, in whole or in part, with the payments of applicable fees, subject to a minimum repayment of $10 million.

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 million 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 million 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.

Dilution of ACE's investment in Air Canada

Air Canada Pension MOUs

As described above, 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

As described above, 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 million (net proceeds of $249 million after expenses and underwriter fees).

Each Unit was 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 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 10 business days after the Acceleration Event, to accelerate the time of expiry of the Warrants.

Air Canada dilution and resulting loss of control

As a result of the share issuances 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 ceased to control Air Canada. As a result, ACE recorded a dilution loss of $411 million.

As of October 27, 2009, ACE no longer consolidates Air Canada's financial position, operating results and cash flows. ACE's investment in Air Canada has since been 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 and other comprehensive income. An equity loss of $7 million was recorded representing ACE's pro rata share of post-dilution earnings through to December 31, 2009. The proportionate share of Air Canada other comprehensive income of $15 million was recorded representing ACE's pro rata share of post-dilution other comprehensive income through to December 31, 2009.

Carrying value of ACE's investment in Air Canada

In December 2009, ACE recorded a Provision for loss on Air Canada investment of $219 million as a result of adjusting the carrying value due to an other than temporary decline in the value of the Corporation's investment in Air Canada to $99 million based on Air Canada's closing market price as at December 31, 2009 ($1.32 per Class B share) as quoted on the TSX.

Air Canada carrying value prior to the following:	$	721
Air Canada dilution loss		(411)
Air Canada carrying value as at October 27, 2009 subsequent to the dilution loss		310
Proportionate share of loss, subsequent to October 27, 2009		(7)
Proportionate share of other comprehensive income, subsequent to October 27, 2009		15
Provision for loss on Air Canada investment		(219)
Air Canada carrying value as at December 31, 2009	**$**	**99**
Air Canada total assets as at December 31, 2009	$	10,406
Air Canada total liabilities as at December 31, 2009	$	8,759
Air Canada loss for the year ended December 31, 2009	$	(24)

The loss on ACE's investment in Air Canada of $630, included in the consolidated statement of operations, is comprised of the Air Canada dilution loss of $411 and the Provision for loss on Air Canada investment of $219.

ACTS Aero

ACTS LP was a full service aircraft maintenance, repair and overhaul organization competing on a global basis.

ACTS was consolidated up to October 16, 2007. Post-monetization described below, ACE's investment in ACTS Aero is accounted for using the equity method.

Monetization

On October 16, 2007, ACTS LP sold substantially all its assets, liabilities and business to ACTS Aero, a new entity established to purchase the assets of ACTS LP. ACTS Aero owns 100% of Aveos (Aveos Fleet Performance Inc.) which changed its legal name on September 23, 2008 from its previous name of ACTS Aero Technical Support and Services Inc. As a result of the monetization of ACTS, the $200 million intercompany note payable by ACTS to ACE was settled through the issue of additional partnership units of ACTS LP to ACE. After settlement of certain obligations ACE received cash proceeds of $723 million. Subsequent to December 31, 2007, ACE received an additional $40 million in cash proceeds from funds held in escrow that was conditional upon the completion of certain supplier contracts within specified terms. In addition, on closing Air Canada received cash proceeds of $65 million, comprised of $28 million for the sale of a building, $20 million pursuant to the Repair Schemes and Non-compete agreement, and $17 million as repayment of a note.

ACE realized a gain of $565 million on the monetization in 2007, which includes the funds held in escrow received subsequent to closing. ACE continues to own 100% of ACTS LP, which is now a non-operating company, and ACTS Aero conducts the business previously operated by ACTS LP. Following the redemption of the exchangeable share issued to a party related to Grupo TACA as discussed below and the establishment of an initial ACTS Long Term Incentive Plan ("LTIP"), ACE held a 23% (28.4% as at December 31, 2009) equity interest in ACTS Aero. The consolidated statement of financial position does not include the financial position or results of operations of ACTS Aero, as ACTS Aero is equity accounted for subsequent to the monetization. As at October 16, 2007, ACE's net investment in ACTS Aero was $76 million.

The Corporation has various related party transactions after removing ACTS from the consolidation of ACE.

These transactions are recorded at the exchange amount. Refer to section 13 Related Party Transactions for a description of the transactions between the Corporation and ACTS Aero.

Acquisition of Aeroman

On February 13, 2007, ACTS LP, through a wholly-owned subsidiary, acquired 80% of Aeromantenimiento, S.A. ("Aeroman"), the aircraft maintenance division of Grupo TACA Holdings Limited ("Grupo TACA") of El Salvador. Total consideration for this acquisition included cash as well as a right to acquire an equity stake in ACTS LP. The cash component of US$45 million consisted of cash of $50 million (US$43 million) on closing and milestone payments of up to $2 million (US$2 million) in the aggregate, funded by ACTS LP through ACE's available cash resources.

As part of the monetization process, an entity related to Grupo TACA exchanged its exchangeable share and received $31 million cash, a 5% equity stake in ACTS and a put option that allowed it to put its 5% equity interest back to ACE for US$18 million within 12 months. During 2008, the entity related to Grupo TACA exercised its put option and sold its 5% equity interest to ACE for $19 million (US$18 million) increasing ACE's ownership interest in ACTS Aero from 22.8% to 27.8%. The liability related to this redemption obligation, initially recorded, was settled as part of the transaction.

Loss on ACTS Aero investment

In December 2008, the Corporation recorded a loss of $10 million related to its equity investment in ACTS Aero. As at December 31, 2009, the carrying value of the Corporation's investment in ACTS Aero is nil (nil as at December 31, 2008).

On January 22, 2010, ACE entered into a Restructuring and Lockup Agreement with Aveos, ACTS Aero, lenders and other shareholders. Under the terms of the restructuring, which is planned to be completed in Quarter 1, 2010, ACE has agreed on closing to transfer its shares in ACTS Aero to a newly formed company, in which ACE will have no interest, for nil consideration.

Aeroplan

Overview

Aeroplan provides its commercial partners, including Air Canada, with loyalty marketing services designed to stimulate demand for such partners' products and services.

ACE had an indirect ownership interest in Aeroplan Limited Partnership through its holdings in Aeroplan Income Fund ("AIF"). Aeroplan was consolidated until March 14, 2007, the date the Corporation made a special distribution of Aeroplan Income Fund units to the Corporation's shareholders. From March 14, 2007 to May 9, 2008, ACE's investment in Aeroplan was accounted for using the equity method. From May 10, 2008 to June 2, 2008, ACE's investment in Aeroplan was accounted for as an available for sale security. The classification of the investment in Aeroplan as available-for-sale resulted in the investment being carried at fair value. The adjustment to fair value recorded to OCI was $331 million, net of income taxes of $72 million.

Summary of sales of units in 2008

On April 21, 2008, ACE sold a total of 20.4 million units of AIF at a price of $17.50 per unit representing total net proceeds to ACE of $343 million and realized a gain on sale of $413 million ($340 million after tax).

On June 2, 2008, ACE sold its remaining units of AIF for total net proceeds to ACE of $349 million, and realized a gain on sale of $417 million ($344 million after tax). Net realized gains of $331 million, net of tax of $72 million, were taken into income from OCI.

Since June 2, 2008, subsequent to the sale of all remaining AIF units, ACE has no ownership interest in Aeroplan.

Jazz

Overview

Jazz is the largest regional airline and second largest airline in Canada, after Air Canada, based on fleet size and number of routes operated. Jazz provides service to Air Canada's customers in lower density markets and in higher density markets at off-peak times throughout Canada and to certain destinations in the United States under a capacity purchase agreement between Air Canada and Jazz.

ACE had an indirect ownership interest in Jazz Air LP through its holdings in Jazz Air Income Fund ("JAIF"). Jazz was consolidated to May 24, 2007, the date the Corporation made a special distribution of Jazz Air Income Fund units to the Corporation's shareholders. From that date to January 24, 2008, ACE's investment in Jazz was accounted for using the equity method. Subsequent to the sale on January 24, 2008 to February 7, 2008, ACE's investment in Jazz was classified as an available-for-sale investment. The classification of the investment in Jazz as available-for-sale resulted in the investment being carried at fair value. The adjustment to fair value recorded to OCI was $71 million, net of income taxes of ($15) million.

Summary of sales of units in 2008

On January 24, 2008, ACE sold a total of 13 million units of JAIF at a price of $7.45 per unit representing total net proceeds to ACE of $97 million and realized a gain on sale of $89 million ($71 million net of taxes).

On June 2, 2008, ACE sold its remaining units of JAIF for total net proceeds to ACE of $85 million, and realized a gain on sale of $78 million ($62 million net of taxes). Net realized gains of $65 million, net of tax of $14 million, were taken into income from OCI.

Since June 2, 2008, subsequent to the completion of the sale of JAIF units, ACE has no ownership interest in Jazz.

Disposition of Aviation Interests

The table below details the Loss on ACE's investment in Air Canada, Gain on sale of Aeroplan and Jazz units, and Gain (loss) on other assets realized in 2009, 2008, and 2007 as a result of disposition by way of sales of various aviation interests and impairment of investments and assets were as follows:

(Canadian dollars in millions)	2009[1]	2008	2007
Air Canada dilution loss	$ (411)	$ -	$ -
Provision for loss on Air Canada investment	(219)	-	-
Loss on ACE's investment in Air Canada	**$ (630)**	**$ -**	**$ -**
Sale of Aeroplan Income Fund units	$ -	$ 830	$ 539
Sale of Jazz Air Income Fund units	-	167	233
Gain on sale of Aeroplan and Jazz units	**$ -**	**$ 997**	**$ 772**
Gain on ACTS monetization	**$ -**	**$ -**	**$ 565**
US Airways	$ -	$ -	$ 8
POLARIS impairment provision	(68)	-	-
Boeing 767 impairment provision	-	(38)	-
Provision for loss on ACTS Aero investment	-	(10)	-
Other	(2)	(3)	21
Gain (loss) on other assets	**$ (70)**	**$ (51)**	**$ 29**
	$ (700)	**$ 946**	**$ 1,366**

(1) *Effective October 27, 2009, the results, financial position and cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.*

6. Accounting Policies

This MD&A should be read in conjunction with ACE's audited consolidated financial statements and notes for 2009. ACE prepares its financial statements, on a going concern basis of presentation, in accordance with Canadian Generally Accepted Accounting Principles ("GAAP").

ACE's results reflect the consolidation of Air Canada only up to October 27, 2009. After that ACE's investment in Air Canada is accounted for using the equity method. Consequently, ACE's results of operations for 2009 are not directly comparable to its operating results for 2008.

Significant accounting policies and methods used in preparation of ACE's 2009 audited financial statements are described in Note 2 to ACE's 2009 audited consolidated financial statements.

The preparation of ACE's financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent liabilities and reported amounts of revenues and expenses for the period of the financial statements. ACE evaluates these estimates and assumptions on a regular basis, based on historical experience and other relevant factors. Actual amounts could differ materially from those estimates and assumptions. Refer to section 14 of this MD&A for a discussion of ACE's critical accounting estimates.

6.1 Future Accounting Standard Changes

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 the 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.

6.2 International Financial Reporting Standards

The Canadian Accounting Standards Board has confirmed January 1, 2011 as the changeover date for Canadian publicly accountable enterprises to start using International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board. IFRS uses a conceptual framework similar to Canadian GAAP, but there are significant differences in recognition, measurement and disclosures.

As a result, the Corporation developed a plan to convert its consolidated financial statements to IFRS. The plan addresses the impact of IFRS on the Corporation and is progressing as planned.

ACE's Consolidated statement of financial position now reflects the following significant assets as at December 31, 2009:

- Cash and cash equivalents;
- a 27.0% (75 million Class B Voting Shares) ownership interest in Air Canada and
- a secured loan of $150 million to Air Canada.

Although the review has not been finalized, the Corporation does not expect to identify differences between its current accounting policies and those required or expected to apply in preparing IFRS financial statements. The Corporation will continue to monitor any developments with respect to any new standards.

7. Results of Operations – Quarter 4 2009

The under-noted reconciliation provides supplementary information to separate CIE from Air Canada results included in the consolidated financial statements for Quarter 4 2009.

(Canadian dollars in millions)	Quarter 4 2009 Air Canada (1)	CIE	ACE Total
Operating revenue			
Passenger revenue	$ 727	$ -	$ 727
Cargo revenue	34	-	34
Other revenue	54	-	54
	815	-	815
Operating expenses			
Aircraft fuel	209	-	209
Wages, salaries and benefits	135	-	135
Airport and navigation fees	79	-	79
Capacity purchase with Jazz	79	-	79
Depreciation and amortization	55	-	55
Aircraft maintenance	68	-	68
Food, beverages and supplies	26	-	26
Communications and information technology	26	-	26
Aircraft rent	26	-	26
Commissions	16	-	16
Other operating expenses	100	1	101
	819	1	820
Operating loss	**(4)**	**(1)**	**(5)**
Non-operating income (expense)			
Interest income	-	3	3
Interest expense	(29)	-	(29)
Interest capitalized	-	-	-
Loss on ACE's investment in Air Canada	-	(630)	(630)
Loss on repurchase of ACE convertible senior notes	-	(1)	(1)
Gain on financial instruments recorded at fair value	21	-	21
Equity and other investment loss	-	(7)	(7)
	(8)	(635)	(643)
Loss before the following items	**(12)**	**(636)**	**(648)**
Non-controlling interest	(1)	8	7
Foreign exchange loss	(18)	-	(18)
Recovery of income taxes	-	3	3
Loss for the period	**$ (31)**	**$ (625)**	**$ (656)**

(1) *Effective October 27, 2009, the results, financial position and cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.*

The under-noted reconciliation provides supplementary information to separate CIE from Air Canada results included in the consolidated financial statements for Quarter 4 2008.

	Quarter 4 2008		
(Canadian dollars in millions)	**Air Canada**	**CIE**	**ACE Total**
Operating revenue			
Passenger revenue	$ 2,182	$ -	$ 2,182
Cargo revenue	113	-	113
Other revenue	203	(2)	201
	2,498	(2)	2,496
Operating expenses			
Aircraft fuel	792	-	792
Wages, salaries and benefits	444	2	446
Airport and navigation fees	230	-	230
Capacity purchase with Jazz	237	-	237
Depreciation and amortization	174	(2)	172
Aircraft maintenance	157	-	157
Food, beverages and supplies	70	-	70
Communications and information technology	72	-	72
Aircraft rent	80	-	80
Commissions	40	-	40
Other operating expenses	348	2	350
	2,644	2	2,646
Operating loss	**(146)**	**(4)**	**(150)**
Non-operating income (expense)			
Interest income	11	6	17
Interest expense	(88)	(15)	(103)
Interest capitalized	6	-	6
Loss on other assets	(5)	(10)	(15)
Gain on financial instruments recorded at fair value	32	-	32
Equity and other investment loss	-	(62)	(62)
	(44)	(81)	(125)
Loss before the following items	**(190)**	**(85)**	**(275)**
Non-controlling interest	(4)	180	176
Foreign exchange loss	(527)	-	(527)
Provision for income taxes	(6)	(1)	(7)
Net income (loss) for the period	**$ (727)**	**$ 94**	**$ (633)**

ACE's results from operations include the consolidation of Air Canada's operations up to October 27, 2009 within the Air Canada column. After that date, Air Canada is accounted for using the equity method. Consequently, ACE's results of operations for Quarter 4 2009 are not directly comparable to its operating results for Quarter 4 2008.

ACE recorded operating loss of $5 million in Quarter 4 2009 compared to the operating loss of $150 million in Quarter 4 2008. ACE's consolidated results for Quarter 4 2008 included an operating loss from Air Canada of $146 million.

ACE recorded operating revenues of $815 million and operating expenses of $820 million in Quarter 4 2009. In the same period in 2008, ACE recorded operating revenues of $2,496 million and operating expenses of $2,646 million. As a result of the deconsolidation of Air Canada, ACE's Quarter 4 2009 operating revenues and expenses are not directly comparable to Quarter 4 2008.

Non-operating expense amounted to $643 million in Quarter 4 2009 compared to non-operating expense of $125 million in Quarter 4 2008. Included in Quarter 4 2009 non-operating expense was a loss on ACE's investment in Air Canada of $630 million which is comprised of the Air Canada dilution loss of $411 million and the Provision for loss on Air Canada investment of $219 million. In Quarter 4 2008, a provision for loss on the investment in ACTS Aero was recorded in the amount of $10 million. Quarter 4 2009 also included an equity loss of $7 million related to the investment in Air Canada, subsequent to October 27, 2009, compared to an equity loss of $62 million in Quarter 4 2008, related to the investment in ACTS Aero.

In Quarter 4 2009, $7 million of the net loss was allocated to non-controlling interest compared to $176 million of the net loss being allocated to non-controlling interest in Quarter 4 2008.

Losses on foreign exchange amounted to $18 million in Quarter 4 of 2009 compared to losses of $527 million in Quarter 4 2008.

The loss in Quarter 4 2009 amounted to $656 million or $(18.38) per diluted share. In Quarter 4 2008, ACE recorded a loss of $633 million or $(18.12) per diluted share.

7.1 Air Canada

The following discussion is based upon Air Canada's Quarter 4 2009 published results.

Air Canada recorded a net loss of $56 million or $(0.25) per diluted share in the fourth quarter of 2009 compared to a net loss of $727 million or $(7.27) per diluted share in the fourth quarter of 2008. The net loss recorded in the fourth quarter of 2009 included foreign exchange gains of $108 million. The foreign exchange gains were primarily attributable to a stronger Canadian dollar at December 31, 2009 versus September 30, 2009. The December 31, 2009 noon day exchange rate was US$1 = C$1.0466 while the September 30, 2009 noon day exchange rate was US $1 = C$1.0722. The fourth quarter 2008 included a foreign exchange loss of $527 million.

In the fourth quarter of 2009, operating revenues of $2,348 million decreased $150 million or 6% from the operating revenues of $2,498 million recorded in the fourth quarter of 2008. The decrease in operating revenues was mainly due to a passenger revenue decline of $152 million or 7% over the same period in 2008. The passenger revenue decline was due to reduced yields. Yield declined 7.3% from the fourth quarter of 2008. Traffic increased 0.4% on a capacity increase of 2.0%, resulting in a passenger load factor decline of 1.3 percentage point. RASM decreased 8.8% over the same period in 2008, which was due to both the yield decline and the decrease in the passenger load factor.

In the fourth quarter of 2009, operating expenses of $2,431 million decreased $213 million or 8% from the operating expenses of $2,644 million recorded the fourth quarter of 2008. Reduced fuel expense of $191 million versus the same period in 2008 was the main factor in the decrease in operating expenses.

In the fourth quarter of 2009, CASM decreased 9.8% from the fourth quarter of 2008. Excluding fuel expense, CASM decreased 3.2% mainly due to the favourable impact of a stronger Canadian dollar versus the U.S. dollar, and lower wages, salaries, and benefits expense. Partly offsetting these decreases to CASM (excluding fuel expense) was a year-over-year increase in aircraft maintenance expense.

7.2 Corporate Items and Eliminations ("CIE")

CIE includes the corporate, financing and investing activities of ACE. As previously discussed, ACE's investment in Air Canada was changed during Quarter 4 2009 from consolidation to the equity method of accounting reported under the CIE column.

CIE recorded a non-operating expense of $635 million in Quarter 4 2009 compared to a non-operating expense of $81 million in Quarter 4 2008.

Factors contributing to the year-over-year change in Quarter 4 2009 included:

- In Quarter 4 2009, ACE recorded a dilution loss of $411 million as a result of the shares issued by Air Canada which reduced ACE's ownership interest in Air Canada from 75% to 27%. In December 2009 ACE also recorded a Provision for loss on Air Canada investment of $219 as a result of adjusting the carrying value due to an other than temporary decline in the value of the Corporation's investment in Air Canada to $99 million based on Air Canada's closing market price as at December 31, 2009, ($1.32 per Class B share) as quoted on the TSX.

- In Quarter 4 2008, ACE recorded a provision for loss on disposal of $10 million related to its equity investment in ACTS Aero. As at December 31, 2008, and December 31, 2009, ACE's investment in ACTS Aero has a carrying value of nil.

- A reduction in interest expense of $15 million as a result of the purchase for cancellation in January, 2009, of 80% of ACE's convertible senior notes outstanding as at December 31, 2008, the purchase of ACE's convertible preferred shares and the redemption of the remaining convertible senior notes in December 2009.

- ACE's consolidated statement of operations for Quarter 4 2009 reflected $7 million of equity loss from ACE's investment in Air Canada versus Quarter 4 2008 $62 million of equity loss from ACE's investment in ACTS Aero.

In Quarter 4 2009, $8 million of the net loss was allocated to non-controlling interest compared to $180 million of the net loss being allocated to non-controlling interest in Quarter 4 2008. This change is mainly attributed to the change to the equity method of accounting for ACE's investment in Air Canada.

8. Results of Operations – 2009

The under-noted reconciliation provides supplementary information to separate CIE from Air Canada results included in the consolidated financial statements for the year ended December 31, 2009.

	2009		
(Canadian dollars in millions)	Air Canada [1]	CIE	ACE Total
Operating revenue			
Passenger revenue	$ 7,196	$ -	$ 7,196
Cargo revenue	282	-	282
Other revenue	728	-	728
External revenue	8,206	-	8,206
Inter-segment revenue	1	(1)	-
	8,207	(1)	8,206
Operating expenses			
Aircraft fuel	2,056	-	2,056
Wages, salaries and benefits	1,468	4	1,472
Airport and navigation fees	822	-	822
Capacity purchase with Jazz	825	-	825
Depreciation and amortization	550	(5)	545
Aircraft maintenance	625	-	625
Food, beverages and supplies	248	-	248
Communications and information technology	255	-	255
Aircraft rent	276	-	276
Commissions	156	-	156
Other operating expenses	1,162	8	1,170
	8,443	7	8,450
Operating loss	**(236)**	**(8)**	**(244)**
Non-operating income (expense)			
Interest income	12	5	17
Interest expense	(316)	(5)	(321)
Interest capitalized	4	-	4
Loss on ACE's investment in Air Canada	-	(630)	(630)
Loss on other assets	(70)	-	(70)
Loss on repurchase of ACE convertible senior notes and preferred shares	-	(44)	(44)
Gain on financial instruments recorded at fair value	94	-	94
Equity and other investment loss	-	(7)	(7)
Other	(5)	-	(5)
	(281)	(681)	(962)
Loss before the following items	**(517)**	**(689)**	**(1,206)**
Non-controlling interest	(12)	(1)	(13)
Foreign exchange gain	531	-	531
Provision for income taxes	(1)	(3)	(4)
Net income (loss) for the year	**$ 1**	**$ (693)**	**$ (692)**

(1) *Effective October 27, 2009, the results, financial position and cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.*

The under-noted reconciliation provides supplementary information to separate CIE from Air Canada results included in the consolidated financial statements for the year ended December 31, 2008

	2008		
(Canadian dollars in millions)	**Air Canada**	**CIE**	**ACE Total**
Operating revenue			
Passenger revenue	$ 9,713	$ -	$ 9,713
Cargo revenue	515	-	515
Other revenue	851	1	852
External revenue	11,079	1	11,080
Inter-segment revenue	3	(3)	-
	11,082	(2)	11,080
Operating expenses			
Aircraft fuel	3,419	-	3,419
Wages, salaries and benefits	1,877	31	1,908
Airport and navigation fees	1,001	-	1,001
Capacity purchase with Jazz	948	-	948
Depreciation and amortization	694	(8)	686
Aircraft maintenance	659	-	659
Food, beverages and supplies	314	-	314
Communications and information technology	286	-	286
Aircraft rent	279	-	279
Commissions	194	-	194
Other operating expenses	1,450	10	1,460
	11,121	33	11,154
Operating income (loss) before under-noted item	**(39)**	**(35)**	**(74)**
Provision for cargo investigations	(125)	-	(125)
Operating loss	**(164)**	**(35)**	**(199)**
Non-operating income (expense)			
Interest income	57	27	84
Interest expense	(319)	(54)	(373)
Interest capitalized	37	-	37
Gain on sale of Aeroplan and Jazz units	-	997	997
Loss on other assets	(34)	(17)	(51)
Gain on financial instruments recorded at fair value	92	-	92
Equity and other investment loss	-	(64)	(64)
Other	(3)	1	(2)
	(170)	890	720
Income (loss) before the following items	**(334)**	**855**	**521**
Non-controlling interest	(12)	250	238
Foreign exchange loss	(655)	-	(655)
Provision for income taxes	(24)	(200)	(224)
Net income (loss) for the year	**$ (1,025)**	**$ 905**	**$ (120)**

ACE's results from operations include the consolidation of Air Canada's operations up to October 27, 2009 within the Air Canada column. After that date, Air Canada is accounted for using the equity method. Consequently, ACE's results of operations for 2009 are not directly comparable to its operating results for 2008.

ACE recorded an operating loss of $244 million in 2009 compared to the operating loss of $74 million, before the provision for cargo investigations, in 2008. In 2008, Air Canada recorded a provision for cargo investigations of $125 million relating to alleged anti-competitive cargo pricing activities.

ACE recorded operating revenues of $8,206 million and operating expenses of $8,450 million in 2009. In the same period in 2008, ACE recorded operating revenues of $11,080 million and operating expenses of $11,154 million. As a result of the deconsolidation of Air Canada, ACE's 2009 operating revenues and operating expenses are not directly comparable to 2008.

Non-operating expense amounted to $962 million in 2009 compared to non-operating income of $720 million in 2008. In 2009, ACE recorded a loss on its investment in Air Canada in the amount of $630 million. ACE recorded a loss on repurchase of the convertible senior notes and preferred shares within Non-operating expense in the amount of $44 million. The repurchase prices of these investments, allocated to the liability components of these compound instruments, exceeded the respective carrying values resulting in a loss of $44 million being recorded. The residual equity components of the instruments amounting to $199 million have been transferred directly to Contributed surplus in the consolidated statement of changes in shareholders' equity. Refer to section 9.5 of this MD&A for additional information. Included in 2008 were gains totalling $997 million on ACE's sale of Aeroplan Income Fund units and Jazz Air Income Fund units.

In 2009, $13 million of net income was allocated to non-controlling interest compared to $238 million of the net loss being allocated to non-controlling interest in 2008.

Gains on foreign exchange amounted to $531 million in 2009 compared to losses of $655 million in 2008.

The net loss in 2009 amounted to $692 million or $(19.56) per diluted share. The net loss in 2008 amounted to $120 million or $(2.59) per diluted share. The net income in 2008 included the significant gains on disposal of the remaining units of Aeroplan Income Fund and Jazz Air Income Fund partially offset by the provision for cargo investigations of $125 million and foreign exchange losses of $655 million recorded by Air Canada. The net loss in 2009 included the loss on ACE's investment in Air Canada of $630 million, partly offset the benefit of foreign exchange gains of $531 million.

8.1 Air Canada

The following discussion is based upon Air Canada's 2009 published results.

Air Canada recorded a loss of $24 million or $(0.18) per diluted share in 2009 compared to a loss of $1,025 million or $(10.25) per diluted share in 2008.

The net income recorded in 2009 included foreign exchange gains of $657 million compared to foreign exchange losses of $655 million in 2008. The gains in 2009 were attributable to a stronger Canadian dollar at December 31, 2009 compared to December 31, 2008. The December 31, 2009 noon day exchange rate was US$1 = C$1.0466 while the December 31, 2008 noon day exchange rate was US$1 = C$1.2246.

In 2009, operating revenues of $9,739 million decreased $1,343 million or 12% from the operating revenues of $11,082 million recorded in 2008. The decrease in operating revenues was mainly due to a passenger revenue decline of $1,214 million or 12% over 2008. The passenger revenue decline was due to lower yield and traffic. Yield declined 7.6% from 2008. Traffic decreased 5.2% on a capacity reduction of 4.4%, resulting in a passenger load factor decrease of 0.7 percentage point. RASM decreased 8.4% over 2008, which was mainly due to the yield decline, but also to the decrease in passenger load factor. A weaker Canadian dollar in 2009 versus 2008 had a positive impact on foreign currency denominated passenger revenues of $184 million.

In 2009, operating expenses of $10,055 million decreased $1,066 million or 10% from the operating expenses of $11,121 million recorded in 2008. Reduced fuel expense of $971 million versus the same period in 2008 was the main factor in the decrease in operating expenses.

In 2009, CASM decreased 5.4% from 2008. Excluding fuel expense, CASM increased 3.3% from 2008. The unfavourable impact of a weaker Canadian dollar versus the US dollar accounted for approximately 44% of the CASM growth (excluding fuel expense) in 2009. In addition to the impact of foreign exchange, other factors included: growth in aircraft maintenance expense, increased Jazz CPA rates, higher unit cost of ownership and the impact of the capacity reduction which disproportionately impacts CASM as Air Canada's cost structure is such that its fixed costs do not fluctuate proportionately with changes in capacity in the short term.

Air Canada's non-operating expense amounted to $355 million in 2009 compared to non-operating expense of $170 million in 2008. Factors contributing to the year-over-year change in non-operating expense included:

- Net interest expense increased $130 million from 2008 due to:
    - A $43 million decrease in interest income which was due to both lower rates of interest and lower cash balances;
    - A $54 million increase in interest expense which was mainly due to the impact of new financing transactions completed in 2009, and the unfavourable impact of foreign exchange on interest expense. These increases were partly offset by the impact of lower average interest rates year-over-year. In addition, in 2009, Air Canada recorded charges amounting to $25 million related to the sale and leaseback transaction of four Boeing 777 aircraft and a charge of $9 million related to the termination of the capital leases of two Airbus A340 aircraft and the subsequent sale of these aircraft. These increases were partly offset by a reduction of interest expense on aircraft pre-delivery payments related to Boeing 777 aircraft versus the same period in 2008;
    - A lower amount of capitalized interest of $33 million compared to 2008.
- In 2009, Air Canada recorded an impairment charge of $68 million 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. In addition, Air Canada recorded a loss on assets of $24 million pertaining to the sale and leaseback of three Boeing 777 aircraft.
- In 2008, Air Canada recorded an impairment charge of $38 million relating to the retirement of its fleet of Boeing 767-200 aircraft and gains amounting to $7 million pertaining to the sale of aircraft-related inventory.
- Gains related to fair value adjustments on derivative instruments amounted to $95 million in 2009 versus gains of $92 million in 2008. The mark-to-market gains on financial instruments recorded in 2009 were mainly related to the change in the fair value of fuel derivatives.

8.2 Corporate Items and Eliminations ("CIE")

CIE includes the corporate, financing and investing activities of ACE.

CIE recorded a non-operating expense of $681 million in 2009 compared to non-operating income of $890 million in 2008.

Factors contributing to the year-over-year change in 2009 included:

- In Quarter 4 2009, ACE recorded a dilution loss of $411 million as a result of the shares issued by Air Canada which reduced ACE's ownership interest in Air Canada from 75% to 27%. In December 2009 ACE also recorded a Provision for loss on Air Canada investment of $219 as a result of adjusting the carrying value due to an other than temporary decline in the value of the Corporation's investment in Air Canada to $99 million based on Air Canada's closing market price as at December 31, 2009, ($1.32 per Class B share) as quoted on the TSX.

- In 2009, ACE recorded a Loss on repurchase of the convertible senior notes and preferred shares within Non-operating expense in the amount of $44 million. The repurchase prices of these investments, allocated to the liability components of these compound instruments, exceeded the respective carrying values resulting in a loss of $44 million being recorded. The residual equity components of the instruments amounting to $199 million have been transferred directly to Contributed surplus in the consolidated statement of changes in shareholders' equity. Refer to section 9.5 of this MD&A for additional information.

- In 2008, gains totalling $997 million were recorded in CIE as a result of ACE's sale of Aeroplan Income Fund units and Jazz Air Income Fund units.

- A reduction in interest expense of $49 million as a result of the purchase for cancellation in January, 2009, of 80% of ACE's convertible senior notes outstanding as at December 31, 2008, the purchase of ACE's convertible preferred shares and the redemption of the remaining convertible senior notes in December 2009.

In 2009, $1 million of the net income was allocated to non-controlling interest compared to $250 million of a net loss being allocated to non-controlling interest in 2008.

9. Financial and Capital Management

Effective October 27, 2009, the results, financial position and cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.

The following table summarizes ACE's consolidated statement of financial position as at December 31, 2009 and as at December 31, 2008.

Condensed Consolidated Statement of Financial Position (Canadian dollars in millions)	**December 31, 2009**	**December 31, 2008**
Assets		
Cash, cash equivalents and short-term investments	$ 71	$ 1,813
Current Assets	3	1,396
Equity investment in Air Canada	99	-
Loan Receivable from Air Canada	150	-
Property and equipment	-	7,469
Intangible assets	-	698
Deposits and other assets	-	495
	$ 323	**$ 11,871**
Liabilities		
Current liabilities	$ 3	$ 3,704
Long-term debt and capital leases	-	4,980
Convertible preferred shares	-	206
Pension and other benefits liabilities	-	1,585
Other long-term liabilities	-	420
	3	**10,895**
Non-controlling interest	**-**	**512**
Shareholders' equity	**320**	**464**
	$ 323	**$ 11,871**

** Refer to Section 12 for Off-balance sheet arrangements.*

9.1 Analysis of Financial Position

The following discussion is based upon ACE's statement of financial position as at December 31, 2009 versus ACE's unconsolidated statement of financial position as at December 31, 2008.

Cash and cash equivalents

As at December 31, 2009, ACE's cash and cash equivalents amounted to $71 million. As at December 31, 2008 ACE's unconsolidated cash and cash equivalents was $808 million. Refer to section 9.2 of this MD&A for a discussion of the change in Cash, and cash equivalents.

Investment in Air Canada

On July 29, 2009, ACE participated in the $600 million Air Canada Credit Facility with several other lenders providing financing of $150 million which represented 25% of the Credit Facility. Since October 27, 2009, ACE no longer consolidates Air Canada's financial position. ACE's investment in Air Canada has since been accounted for using the equity method. In Quarter 4 2009, ACE recorded a dilution loss of $411 million as a result of the shares issued by Air Canada which reduced ACE's ownership interest in Air Canada from 75% to 27%. In December 2009 ACE also recorded a Provision for loss on Air Canada investment of $219 as a result of adjusting the carrying value due to an other than temporary decline in the value of the Corporation's investment in Air Canada to $99 million based on Air Canada's closing market price as at December 31, 2009, ($1.32 per Class B share) as quoted on the TSX.

Convertible senior notes

In January 2009, ACE completed a substantial issuer bid resulting in the purchase for cancellation of 80% of ACE's convertible senior notes outstanding as at December 31, 2008, at a purchase price of $900 in cash for each $1,000 principal amount of notes. The aggregate principal amount of the repurchased convertible senior notes was $259 million. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 million for the notes tendered. On December 14, 2009, the Corporation paid an aggregate purchase price of $64 million for the redemption of the remaining convertible senior notes.

Convertible preferred shares

In January 2009 and March 2009, ACE completed substantial issuer bids resulting in the purchase for cancellation of 9.3 million of ACE's convertible preferred shares at a purchase price of $20.00 per preferred share. In September 2009, ACE purchased for cancellation the remaining 3.2 million convertible preferred shares at a purchase price of $23.00 per share. In Quarter 1 2009, the Corporation paid an aggregate purchase price of $186 million for the shares tendered. In Quarter 3 2009, the Corporation paid an aggregate purchase price of $74 million for the remaining shares.

Shareholders' equity

As at December 31, 2009, ACE's shareholders' equity amounted to $320 million, a decline of $144 million during 2009 mainly as a result of the loss of $692 million offset by other comprehensive income of $556 million.

9.2 Consolidated Cash Flows

Effective October 27, 2009, the results, financial position and also cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.

The following table summarizes ACE's consolidated statement of cash flows for the indicated periods.

	Quarter 4					
(Canadian dollars in millions)	**2009**	**2008**	**$ Change**	**2009**	**2008**	**$ Change**
Cash from (used for) operating activities	$ 19	$ (291)	$ 310	$ (168)	$ (110)	$ (58)
Cash from (used for) financing activities	160	269	(109)	(409)	(2,095)	1,686
Cash from (used for) investing activities	(1,284)	8	(1,292)	(659)	1,212	(1,871)
Net change in cash and cash equivalents during the period	**(1,105)**	**(14)**	**(1,091)**	**(1,236)**	**(993)**	**(243)**
Cash and cash equivalents - Beginning of period	**1,176**	**1,321**	**(145)**	**1,307**	**2,300**	**(993)**
Cash and cash equivalents - End of period	**$ 71**	**$ 1,307**	**$ (1,236)**	**$ 71**	**$ 1,307**	**$ (1,236)**

** Cash and cash equivalents exclude Short-term investments of $506 million as at December 31, 2008.*

ACE

The following summarizes significant transactions or factors which impacted ACE's non-consolidated cash and cash equivalents in 2009:

- 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 in cash for each $1,000 principal amount of notes. The aggregate principal amount of the repurchased convertible senior notes was $259 million. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 million for the notes tendered.

- In January 2009, ACE completed a substantial issuer bid to purchase for cancellation 8.3 million of its convertible preferred shares at a purchase price of $20.00 per preferred share. On January 21, 2009, the Corporation paid an aggregate purchase price of $166 million for the shares tendered.

- In March 2009, ACE completed a substantial issuer bid to purchase for cancellation 1.0 million of its convertible preferred shares at a purchase price of $20.00 per preferred share. On March 23, 2009, the Corporation paid an aggregate purchase price of $20 million for the shares tendered.

- In July 2009, ACE participated in the Air Canada credit facility providing financing of $150 million, which represents 25% of the $600 million Credit Facility. The Credit Facility is a five-year facility repayable in sixteen (16) consecutive quarterly installments commencing in August 2010 with the final balloon installment due in July 2014. 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% at December 31, 2009).

- In September 2009, ACE entered into an agreement with Morgan Stanley Canada Limited pursuant to which ACE indirectly purchased for cancellation all of its remaining 3.2 million preferred shares at a price of $23.00 per share for an aggregate purchase price of $74 million.

- In December 2009, ACE redeemed the remaining convertible senior notes for an aggregate purchase price of $64 million.

The following summarizes significant transactions or factors which impacted ACE's unconsolidated cash and cash equivalents in 2008:

- On January 10, 2008, ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares at $30.00 per share for an aggregate purchase price of $1,498 million, in accordance with the terms of a substantial issuer bid.

- ACE received cash proceeds of $40 million representing the full balance of funds held in escrow on closing of the monetization of ACTS on October 16, 2007.

- ACE received net proceeds of $97 million related to the sale of Jazz Air Income Fund units on January 24, 2008.

- On April 21, 2008, ACE completed the sale of 20,400,000 units of Aeroplan Income Fund at a price of $17.50 per unit, for total net proceeds to ACE of $343 million.

- On June 2, 2008, ACE completed the sale in the market of a total of 11,726,920 units of Jazz Air Income Fund for total net proceeds to ACE of $85 million.

- On June 2, 2008, ACE completed the sale in the market of a total of 19,892,088 units of Aeroplan Income Fund for total net proceeds to ACE of $349 million.

- On June 18, 2008, ACE accepted for purchase and cancellation a total of 12,537,084 Class A variable voting shares and 10,190,187 Class B voting shares at $22.00 per share for an aggregate purchase price of $500 million, in accordance with the terms of a substantial issuer bid.

- In June 2008, an entity related to Grupo TACA exercised its put option and sold its 5% equity interest in ACTS Aero to ACE for $19 million.

Air Canada

The following discussion is based upon Air Canada's 2009 published results.

During 2009, Air Canada entered into the following significant transactions in an effort to mitigate liquidity risks:

- Completed a share and warrant public offering for net proceeds of $249 million.

- Completed a secured term credit facility (the "Credit Facility") for financing proceeds of $600 million, less fees of $20 million. The Credit Facility is a five-year facility, with the first principal repayment due in August 2010, and currently bears interest at 12.75%. Under the Credit Facility, 10 million warrants were also issued which entitle the debt holders to acquire up to 10 million shares in Air Canada. ACE provided financing of $150 million with respect to the Credit Facility, as further described below.

- 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 million, $175 million, and $225 million 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 (in both cases 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.

- Total cash flows to Air Canada during the full year 2009 from borrowing, including the Credit Facility described above, amounted to $926 million, proceeds from sale of assets amounted to $103 million, proceeds from sale-leaseback transactions amounted to $552 million and proceeds from contractual commitments amounted to $230 million. Reductions of long-term debt during 2009, which include repayments as a result of certain of the above financings and sale-leasebacks, amounted to $1,237 million.

At December 31, 2009, Air Canada had Cash and cash equivalents and Short-term investments of $1,407 million ($1,005 million as at December 31, 2008).

9.3 Contractual Obligations

On November 5, 2009, the Board of Directors authorized the redemption for cash of ACE's senior convertible notes. The notes were redeemed on December 14, 2009 for an aggregate purchase price of $64 million.

9.4 Capital Management

ACE views capital as the sum of parent company capital consisting of convertible senior notes, convertible preferred shares, non-controlling interest and shareholders' equity. This definition of capital used by management may not be comparable to measures presented by other public companies. Capital managed by ACE, summarized from the consolidated statement of financial position follows:

(Canadian dollars in millions)	2009	2008
Convertible senior notes	$ -	$ 289
Convertible preferred shares	-	206
Non-controlling interest	-	512
Shareholders' equity	320	464
Capital	**$ 320**	**$ 1,471**

As at December 31, 2009, ACE's capital amounted to $320 million, a decline of $1,151 million during 2009. As at December 31, 2009, ACE cash and cash equivalents amounted to $71 million ($808 million as at December 31, 2008).

ACE's business strategy, to surface shareholder value and to return capital to its shareholders, has influenced its capital management objectives. Consistent with those objectives, during 2008 and 2009, the ACE Board of Directors authorized the return of capital to its shareholders and the redemption of its convertible senior notes and convertible preferred shares, as further described below. Going forward, the Board will continue to review alternatives to maximize the return to its shareholders.

Convertible Senior Notes

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 in cash for each $1,000 principal amount of notes. The aggregate principal amount of the repurchased convertible senior notes was $259 million. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 million for the convertible senior notes tendered. On December 14, 2009, the Corporation redeemed the remaining convertible senior notes for an aggregate purchase price of $64 million.

Convertible Preferred Shares

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 $20.00 per preferred share. In Quarter 1 2009, the Corporation paid an aggregate purchase price of $186 million 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 preferred shares at a price of $23.00 per share for an aggregate purchase price of $74 million.

Non-controlling Interest

Effective October 27, 2009, ACE no longer consolidates Air Canada's financial position, operating results and cash flows. As a result, as at December 31, 2009 ACE's Non-controlling interest is nil.

Shareholders' equity

As at December 31, 2009, ACE's shareholders' equity amounted to $320 million, a decline of $144 million during 2009.

9.5 Share Information

At January 31, 2010, the issued and outstanding common shares of ACE, along with common shares potentially issuable, pursuant to convertible preferred shares, convertible senior notes and stock options were as follows:

Number of shares (000)	January 31, 2010	December 31, 2009
Issued and outstanding common shares		
Class A variable voting shares	24,223	25,643
Class B voting shares	8,242	10,048
Total issued and outstanding common shares (1)	**32,465**	**35,691**
Common shares potentially issuable		
Convertible preferred shares (2)	-	-
Convertible senior notes (3)	-	-
Stock options (4)	48	48
Total common shares potentially issuable	**48**	**48**
Total outstanding and potentially issuable common shares	**32,513**	**35,739**

(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 million 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.

In January 2010, the Corporation completed a substantial issuer bid to purchase for cancellation a total of 1,401,094 Class A Variable Voting Shares and 1,824,711 Class B Voting shares at $6.20 per share for an aggregate purchase price of $20 million.

(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 $20.00 per preferred share. In Quarter 1 2009, the Corporation paid an aggregate purchase price of $186 million 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 preferred shares at a price of $23.00 per share for an aggregate purchase price of $74 million.

(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 in cash for each $1,000 principal amount of notes. The aggregate principal amount of the repurchased convertible senior notes was $259 million. On January 21, 2009, the Corporation paid an aggregate purchase price of $233 million for the notes tendered. In November 2009, the Board of Directors authorized the redemption for cash of ACE's remaining senior convertible notes. On December 14, 2009, the Corporation redeemed the remaining convertible senior notes for an aggregate purchase price of $64 million.

(4) The Corporation's stock option plan is described in Note 13 to the 2008 annual consolidated financial statements. At January 31, 2010, a total of 47,812 stock options with a weighted exercise of $14.61 were outstanding (61,230 stock options with a weighted exercise of $14.11 outstanding as at December 31, 2008). The decrease of 13,418 stock options since December 31, 2008 is due to forfeitures experienced throughout 2009.

10. Quarterly Financial Information

The quarterly information presented below is not directly comparable as a result of ACE's investment in Air Canada being changed on October 27, 2009 from consolidation to the equity method of accounting.

($ millions, except per share amounts)	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1 2009	Q2 2009	Q3 2009	Q4[(1)] 2009
Operating revenues	$ 2,726	$ 2,783	$ 3,075	$ 2,496	$ 2,391	$ 2,330	$2,670	$815
Operating expenses	(2,753)	(2,785)	(2,970)	(2,646)	(2,583)	(2,445)	(2,602)	820
Operating income (loss) before under-noted item	**(27)**	**(2)**	**105**	**(150)**	**(192)**	**(115)**	**68**	**(5)**
Provision for cargo investigations[(2)]	(125)	-	-	-	-	-	-	-
Operating income (loss)	**(152)**	**(2)**	**105**	**(150)**	**(192)**	**(115)**	**68**	**(5)**
Total non-operating income (expense), non-controlling interest, foreign exchange gain (loss) and income tax[(3)]	(30)	832	(240)	(483)	(152)	225	130	(651)
Net income (loss)	**$ (182)**	**$ 830**	**$ (135)**	**$ (633)**	**$ (344)**	**$ 110**	**$ 198**	**$ (656)**
Earnings (loss)[(4)]								
Per share – basic	**$ (2.96)**	**$ 15.46**	**$ (3.86)**	**$ (18.12)**	**$ (9.87)**	**$ 3.16**	**$5.57**	**$(18.38)**
Per share – diluted	**$ (2.96)**	**$ 10.76**	**$ (3.86)**	**$ (18.12)**	**$ (9.87)**	**$ 2.68**	**$5.15**	**$(18.38)**

(1) *The results, financial position and cash flows of Air Canada are not consolidated with ACE effective October 27, 2009.*

(2) *Air Canada recorded a provision for cargo investigations of $125 million in Quarter 1 2008.*

(3) *Quarter 1 2008 includes a gain of $89 million ($71 million, net of tax) on ACE's sale of 13,000,000 units of Jazz Air Income Fund and an impairment provision of $38 million recorded by Air Canada related to its fleet of Boeing 767-200 aircraft. Quarter 2 2008 includes a gain of $413 million ($340 million, net of tax) on ACE's sale of 20,400,000 units of Aeroplan Income fund, a gain of $417 million ($344 million, net of tax) on ACE's sale of 19,892,088 units of Aeroplan Income Fund and a gain on of $78 million ($62 million, net of tax) on ACE's sale of 11,726,920 units of Jazz Air Income Fund. Quarter 1 2009 includes a loss on repurchase of the convertible senior notes and preferred shares of $33 million relating to the substantial issuer bids completed in January 2009 and March 2009. Quarter 3 2009 includes a loss on repurchase of the preferred shares of $10 million relating to the acquisition for cancellation of the remaining preferred shares in September 2009. Quarter 4 2009 includes a dilution loss of $411 million as a result of the shares issued by Air Canada reducing ACE's ownership interest from 75% to 27% and includes a provision for loss on ACE's Air Canada investment of $219 million as a result of adjusting the carrying value of ACE's investment in Air Canada to $99 million based on Air Canada's market price as at December 31, 2009.*

(4) *Earnings (loss) per share includes the impact of a substantial issuer bid completed by ACE on January 10, 2008 whereby ACE accepted for purchase and cancellation a total of 40,023,427 Class A variable voting shares and 9,894,166 Class B voting shares and a substantial issuer bid completed by ACE on June 18, 2008 whereby ACE accepted for purchase and cancellation a total of 12,537,084 Class A variable voting shares and 10,190,187 Class B voting shares.*

11. Financial Instruments and Risk Management

Effective October 27, 2009, the results, financial position and also cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.

Risk Management

As a result, as at December 31, 2009, ACE's financial instruments are limited to cash and cash equivalents in the amount of $71 million, a secured loan of $150 million to Air Canada, interest receivable of $3 million from Air Canada and accounts payable of $3 million. The risk exposure related to these holdings is described below.

Interest Rate Risk
Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Corporation is exposed to interest rate risk from its holding in cash and cash equivalents of $71 million in addition to its secured loan receivable and related interest receivable from Air Canada of $150 million and $3 million, respectively. The loan receivable from Air Canada bears interest at a rate based upon the greater of the bankers' acceptance rate or 3.00% plus 9.75% (12.75% as at December 31, 2009), which mitigates risk to nil.

The weighted average interest rate on ACE's cash and cash equivalents at December 31, 2009, is 0.22%, which results in limited downside risk.

Liquidity risk
Liquidity risk is the risk that the Corporation will encounter difficulty in meeting obligations associated with its financial liabilities. This risk is mitigated by the fact that as at December 31, 2009, the Corporation had Cash and cash equivalents of $71 million and current financial liabilities of $3 million.

Credit Risk
Credit risk is the risk of loss due to a counterparty's inability to meet its obligations. The Corporation is exposed to credit risk from its cash and cash equivalents and its secured loan receivable from Air Canada and related interest receivable from Air Canada. The maximum exposure of which is represented by the carrying amounts reported on the balance sheet.

This risk is mitigated by the fact that:

- Cash and cash equivalents are held by credit worthy institutions only. The Corporation's target is that no one financial institution hold more than 25% of the total cash balance;
- 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).

Summary of gain (loss) on financial instruments recorded at fair value

	2009 (1)	2008
Ineffective portion of fuel hedges	$ -	$ 83
Fuel derivatives not under hedge accounting	98	(9)
Cross currency interest rate swaps	-	4
Other	(4)	14
Gain on financial instruments recorded at fair value	**$ 94**	**$ 92**

(1) *Effective October 27, 2009, the results and financial position of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.*

12. Off-Balance Sheet Arrangements

Effective October 27, 2009, the results, financial position and also cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.

Guarantees

On May 7, 2009, ACE intervened into the employment agreement between Air Canada and Mr. Calin Rovinescu, its President and Chief Executive Officer, to guarantee the payments required of Air Canada under the agreement.

In addition, ACE agreed to cause to be issued an irrevocable bank letter of credit to a maximum of $5 million. At December 31, 2009, as agreed by the parties, the letter of credit had not been issued.

13. Related Party Transactions

At February 11, 2009 ACE held a 27% ownership interest in Air Canada. On October 16, 2007, ACTS LP sold substantially all its assets, liabilities and business to ACTS Aero, a new entity established to purchase the assets of ACTS LP. ACTS Aero owns 100% of Aveos (Aveos Fleet Performance Inc.) which changed its legal name on September 23, 2008 from its previous name of ACTS Aero Technical Support and Services Inc. As at February 11, 2009 ACE held a 28.4% interest in ACTS Aero. Air Canada has various related party transactions with Aveos, an ACE related entity. Subsequent to the sale of Jazz units on January 24, 2008 and the termination of the Securityholders' Agreement on February 7, 2008, ACE no longer exercised significant influence over Jazz. Subsequent to the sale on April 24, 2008 and the termination of the Securityholders' Agreement on May 9, 2008, ACE no longer exercised significant influence over Aeroplan.

On January 22, 2010, ACE entered into a Restructuring and Lockup Agreement with Aveos, ACTS Aero, lenders and other shareholders. Under the terms of the restructuring, which is planned to be completed in Quarter 1, 2010, ACE has agreed on closing to transfer its shares in ACTS Aero to a newly formed company, in which ACE will have no interest, for nil consideration.

Summary of significant related party agreements

The Relationship between Air Canada and ACE

Credit Facility
ACE is a participant lender in the Credit Facility as described in Section 5. ACE's participation in the Credit Facility represents $150 million of the outstanding loan of $600 million as at February 11, 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 paid by Air Canada on February 1, 2010, amounts to $4.8 million.

Master Services Agreement
Air Canada provides certain accounting and administrative services to ACE in return for a fee. ACE terminated the majority of these service agreements in 2009.

Guarantee of Air Canada obligation
Refer to Section 12 for Off-balance sheet arrangements.

The Relationship between the Air Canada and Aveos

Pension and Benefits Agreement
Air Canada, ACTS and ACTS Aero entered into a Pension and Benefits Agreement effective as of October 16, 2007, as amended ("Pension and Benefits Agreement"), relating to pension and benefits arrangements pertaining to (i) the non-unionized employees of Air Canada who were previously assigned to the ACTS operation and who became employees of Aveos on October 16, 2007 and (ii) those unionized employees of Air

Canada who were assigned to ACTS Aero operation pursuant to general services agreements between Air Canada and ACTS for the assignment of unionized employees from Air Canada to ACTS (these agreements were assigned to ACTS Aero (i.e. Aveos) upon closing of the monetization). Under the Pension and Benefits Agreement, Aveos is required to establish new defined benefit and defined contribution pension plans as well as other employee and retiree benefit arrangements (including health, life and disability) (the "ACTS Benefit Arrangements").

Upon receipt of regulatory approval where required and based upon valuations of the relevant pension and benefit arrangements of Air Canada (the "Air Canada Benefit Arrangements") as at October 16, 2007, the assets and obligations under the Air Canada Benefit Arrangements pertaining to the transferring non-unionized employees are to be transferred to ACTS Aero or the ACTS Benefit Arrangements, as applicable. Amounts with a present value equal to the solvency deficiency in the defined benefit pension plans as at October 16, 2007 related to transferring non-unionized employees will be paid by Air Canada through quarterly payments to Aveos until 2014. Amounts with a present value equal to the accounting liability as at October 16, 2007 in respect of retiree and disability benefits related to transferring non-unionized employees are to be paid by Air Canada through quarterly payments to Aveos until 2012. The present value of these quarterly payments is also referred to as the compensation amount. Until such future time as the assets and obligations under the Air Canada Benefit Arrangements pertaining to non-unionized employees are to be transferred to Aveos, the current service pension cost and the current service and interest costs for other employee benefits are expensed by Air Canada with a full offset recorded as an amount charged to affiliates (Aveos).

In addition, the Pension and Benefits Agreement contemplates similar asset and liability transfer and compensation arrangements in respect of unionized employees, which arrangements would take effect at such future time as those unionized employees may commence employment with Aveos pursuant to the Transition Memorandum of Agreement ("the Transition MOA"), as described further below. However, the solvency deficiencies in respect of transferring unionized employees for which the future quarterly compensation payments would be made are determined as at October 16, 2007, subject to certain adjustments, and the discount rate used to compute the accounting liability for the unionized employees' retiree and disability benefits is fixed as at October 16, 2007. The compensation payments in respect of these solvency deficiencies and accounting liabilities will be made quarterly during the five years beginning after the unionized employees are transferred to Aveos, but only if such a transfer occurs. Until such future time as the assets and obligations under the Air Canada Benefit Arrangement pertaining to unionized employees may be transferred to Aveos, the current service pension cost and the current service and interest costs for other employee benefits in respect of Air Canada employees providing services to Aveos are charged by Air Canada to Aveos.

The Pension and Benefits Agreement also required that Air Canada provide letters of credit to Aveos on October 16, 2007, to secure the above-described payment obligations in respect of the solvency deficiencies of the defined benefit pension plans and accounting liabilities for other retiree and disability benefit arrangements. The letters of credit initially totaled $101 million, subject to adjustment once the exact amounts of the relevant solvency deficiencies and accounting liabilities as at October 16, 2007 were determined by actuarial valuations. The face amount of the letter of credit in respect of the unionized solvency deficiency is also adjusted annually to recognize past service costs paid by Air Canada to the plan in respect of unionized employees assigned to ACTS Aero. The face amount of the letters of credit decreases as the related quarterly funding payments described above are made. During 2008, as described below under "Agreement with Aveos on Revised Payment Terms", Air Canada and Aveos also agreed to temporarily cancel certain letters of credit in the amount of $40 million. Aveos may call the letters of credit in whole or in part, in the event of a default as defined in the Pension and Benefits Agreement. Collateral equal to the amount of the letters of credit was paid in cash with the asset recorded in deposits and other assets.

In 2008, Air Canada, Aveos, and the union representing the employees assigned to Aveos continued discussions regarding the options under which certain unionized employees would commence employment directly with Aveos and the creation of a separate bargaining unit for those employees at Aveos. On January 8, 2009, these same parties entered into the Transition MOA in order to resolve certain remaining issues and in order to (i) facilitate the orderly transition of certain Air Canada employees to Aveos and (ii) to establish terms and conditions of employment that will apply to those Air Canada employees who elect to become employees of Aveos. In relation to the Transition MOA, Air Canada and Aveos also entered into certain ancillary agreements (the "Ancillary Transition Agreements") to address commercial issues relating to the transition of employees contemplated by the Transition MOA. On March 5, 2009, Air Canada received the decision of the arbitrator seized with resolving five issues which remained outstanding following the execution of the Transition MOA. Air Canada and the IAMAW subsequently amended the Transition MOA, by establishing timelines for the steps for the transition and by providing for a date on which the employees who will transition to Aveos will become employees of Aveos, namely, April 1, 2011.

Non-Compete and Repair Schemes Transfer Agreement
Aveos and Air Canada are parties to a Non-Compete and Repair Schemes Transfer Agreement, effective as of October 16, 2007. Generally described, repair schemes are processes and methods which may be used in the maintenance and repair of aircraft and related equipment. The Non-Compete and Repair Schemes Transfer Agreement confirmed an arrangement and provides for the sale from Air Canada to ACTS Aero (as successor to ACTS LP) of an undivided joint ownership interest in repair schemes owned by Air Canada or approved under Air Canada's airworthiness engineering organization as well as the sale from Aveos to Air Canada of an undivided joint ownership interest in the repair schemes owned or developed by Aveos and applicable to airframe heavy maintenance services provided by ACTS to Air Canada under the parties' airframe heavy maintenance services agreement. However, in September 2004 as part of the implementation of Air Canada's plan of arrangement under the CCAA, Air Canada had already granted ACTS full and exclusive right to these schemes on a royalty free basis.

The Non-Compete and Repair Schemes Transfer Agreement also restricts Air Canada's ability to own any equity interest in an entity (other than entities in which Air Canada previously held interests), or to carry on a business activity, related to the following commercial maintenance, repair and overhaul services in the airline industry, namely, airframe heavy maintenance and paint services, engine and auxiliary power unit ("APU") overhaul maintenance services, and component maintenance services. The applicable non-compete periods are as follows:

- With respect to airframe heavy maintenance services and paint services, the non-compete period ends one year after the current heavy maintenance services agreement is terminated or expires (the current term of the heavy maintenance services agreement expires October 1, 2011);

- With respect to engine and APU overhaul maintenance services, the non-compete period ends on October 1, 2015; and

- With respect to component maintenance services, the non-compete period ends on October 1, 2016.

The Non-Compete and Repair Schemes Transfer Agreement does not restrict Air Canada from holding interests in any entities in which it held interests at the time of concluding the agreement nor does it limit Air Canada's line maintenance activities which it continues to operate.

Agreement with Aveos on Revised Payment Terms
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 above, were cancelled. The cancellation of the letters of credit provided cash to Air Canada of approximately $40 million and was offset by the impact of extended payment terms to Aveos of $22 million, for a net cash flow benefit of $18 million to Air Canada. 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, the payment terms were extended. The extended payment terms to Aveos will be reduced starting in February 2010, with the expiration of the extended terms to be completed over the following six months. By July 2010, following expiration of the extended payment terms, the letters of credit would be reinstated to the levels then required under the Pension and Benefits Agreement between the two parties.

Maintenance Agreements
Aveos and Air Canada are parties to a general terms and related services agreements effective October 1, 2006, pursuant to which Aveos provides technical services to Air Canada including engine and auxiliary power unit maintenance services, aircraft heavy maintenance services (excluding line and cabin maintenance services which are provided by Air Canada), and component maintenance. Aveos serves as Air Canada's exclusive repair agency in respect of aircraft heavy maintenance, engine maintenance, auxiliary power unit maintenance services as well as for maintenance services relating to certain components. The services agreement relating to aircraft heavy maintenance services, which expires in October 2011, will be extended to June 2013 conditional upon the issuance of an order of the Canada Industrial Relations Board establishing that Aveos is a distinct employer, bound by separate collective agreements and providing for the transition of employees from Air Canada to Aveos which are fully within the scope of the Transition MOA and the Ancillary Transition Agreements mentioned above. The services agreement relating to engine maintenance expires in October 2013, except in respect of certain engine types, for which the parties have agreed to extend the term to December 31, 2018. Each of the other maintenance agreements referred to above expire in October 2013.

Master Services Agreement (MSA)
Aveos and Air Canada are parties to an amended and restated master services agreement (the "Aveos MSA"), effective January 1, 2007, pursuant to which Air Canada provides Aveos with services including infrastructure support and services which are mostly administrative in nature, including information technology, human resources, finance and accounting services in return for fees paid by Aveos to Air Canada. Aveos may elect to terminate any services under the Aveos MSA or the entire Aveos MSA upon six months' prior written notice, with the exception of services relating to information technology which Aveos cannot terminate prior to the expiry of the Aveos MSA. Air Canada may elect to terminate any services under the Aveos MSA or the entire Aveos MSA upon 18 months' prior written notice. These amounts are recorded in the above table summarizing related party revenues and expenses under Revenues from corporate services and other.

General Services Agreements
Aveos and Air Canada are parties to an amended and restated general services agreement (the "Aveos GSA"), effective as of June 22, 2007, pursuant to which Air Canada provides Aveos with the services of a group of unionized employees for which Air Canada is reimbursed by Aveos for all costs, including salary and benefits, on a fully allocated basis. The Aveos GSA may be terminated by either party at any time upon 30 days' prior written notice.

Real Estate Agreements
Aveos and Air Canada are parties to a master lease agreement, effective as of October 1, 2006, pursuant to which Aveos leases space from Air Canada at the Vancouver, Winnipeg, Toronto and Montreal airports.

14. Critical Accounting Estimates

Effective October 27, 2009, the results, financial position and also cash flows of Air Canada are not consolidated with ACE. Refer to Section 5 "Investments" in this MD&A.

Critical accounting estimates are those that are most important to the portrayal of the Corporation's financial condition and results of operations. They require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Actual results could differ from those estimates under different assumptions or conditions.

The Corporation has identified the following areas that contain critical accounting estimates utilized in the preparation of its consolidated financial statements:

Passenger and Cargo Revenues
Airline passenger and cargo advance sales are deferred and included in current liabilities. Advance sales also include the proceeds from the sale of flight tickets to Aeroplan, a corporation that provides loyalty program services to Air Canada and purchases seats from Air Canada pursuant to the Aeroplan Commercial Participation and Services Agreement between Aeroplan and Air Canada (the "CPSA"). Passenger and cargo revenues are recognized when the transportation is provided, except for revenue on unlimited flight passes which is

recognized on a straight-line basis over the period during which the travel pass is valid. Air Canada has formed alliances with other airlines encompassing loyalty program participation, code sharing and coordination of services including reservations, baggage handling and flight schedules. Revenues are allocated based upon formulas specified in the agreements and are recognized as transportation is provided.

Air Canada performs regular evaluations on the deferred revenue liability which may result in adjustments being recognized as revenue. Due to the complex pricing structures, the complex nature of interline, and other commercial agreements used throughout the industry, historical experience over a period of many years, and other factors including refunds, exchanges and unused tickets, certain relatively small amounts are recognized as revenue based on estimates. Events and circumstances may result in actual results that are different from estimates.

Income Taxes

The Corporation utilizes the assets and liability method of accounting for income taxes under which future income tax assets and liabilities are recognized for the estimated future income tax consequences attributable to differences between the financial statement carrying value amount and the tax basis of assets and liabilities. Management uses judgment and estimates in determining the appropriate rates and amounts in recording future taxes, giving consideration to timing and probability. Actual taxes could significantly vary from these estimates as a result of future events, including changes in income tax law or the outcome of reviews by tax authorities and related appeals. The resolution of these uncertainties and the associated final taxes may result in adjustment to the Corporation's tax assets and tax liabilities.

Future income tax assets are recognized to the extent that realization is considered more likely than not. The Corporation considers past results, current trends and outlooks for future years in assessing realization of income tax assets.

Cash Tax Projections

As at December 31, 2009, the Corporation has substantial tax attributes largely in the form of loss carry forwards and other tax attributes to shelter future taxable income. The Corporation does not forecast having any significant current taxes payable within the foreseeable future.

15. Risk Factors

The risks described herein may not be the only risks faced by the Corporation. Other risks which the Corporation is not aware of or which the Corporation currently deems to be immaterial may surface and have a material adverse impact on the Corporation's business, results from operations and financial condition.

Risks Related to ACE

Exposure to Air Canada

ACE's principal investments are equity and debt interests in Air Canada. The value of ACE's equity interest in Air Canada is subject to market conditions based on the financial performance of Air Canada, movements in the price of publicly-traded airline stocks and general market conditions. Any decrease in the market price of Air Canada shares will reduce the value of these shares which can be realized. The value of ACE's debt interest is dependent on the performance of Air Canada and the value of the security for the Air Canada Credit Facility in which ACE participates. Detailed risk factors for Air Canada are set out below.

A Substantial Portion of ACE's Cash is Invested in Cash Equivalents

A substantial portion of ACE's cash is invested in cash equivalents which are subject to credit exposure and interest rate fluctuations which could change the value of these investments. These investments are made in accordance with an investment policy approved by the Board of Directors. Although ACE's investment policy is designed to provide for short-term liquidity and low levels of risk, such investments are subject to credit exposure and interest rate fluctuations. Consequently, the value of such investments could increase or decrease accordingly. Any decrease in the fair value of these investments would reduce the amount available for distribution to stakeholders.

Going Concern

On July 29, 2009, ACE announced that its participation in the $600 million Air Canada Credit Facility amounted to $150 million. Given ACE's participation in the facility, it is not management's intention to liquidate at this time.

If ACE subsequently proceeds with the liquidation of its net assets, ACE will again adopt a liquidation basis of presentation which will result in net assets in liquidation being presented on a net realizable basis.

Risks Relating to Air Canada

Operating Results

Prior to emergence from its restructuring under the Companies Creditors Arrangement Act, as amended ("CCAA") on September 30, 2004, Air Canada had sustained significant losses and Air Canada may sustain significant losses in the future. In 2008, Air Canada recorded an operating loss before a provision for cargo investigations and proceedings of $39 million. During 2009, Air Canada recorded an operating loss of $316 million. Current economic conditions may result in significant losses for Air Canada. Despite ongoing business initiatives and efforts at securing cost reductions, revenue improvements and additional sources of financing, Air Canada may not be able to successfully achieve positive net profitability or realize the objectives of any or all of its initiatives, including those which seek to improve yield or offset or mitigate risks facing Air Canada, including those relating to economic conditions, liquidity, pension funding, unexpected volatility in fuel costs and other expenses.

Leverage

Air Canada has, and is expected to continue to have and incur, a significant amount of indebtedness, including substantial fixed obligations under aircraft leases and financings, and as a result of challenging economic or other conditions affecting Air Canada, Air Canada may incur greater levels of indebtedness than currently exist. The amount of indebtedness that Air Canada currently has and which it may incur in the future could have a material adverse effect on Air Canada, for example, by (i) limiting Air Canada's ability to obtain additional financing, (ii) requiring Air Canada to dedicate a substantial portion of its cash flow from operations to payments on its indebtedness and fixed cost obligations, thereby reducing the funds available for other purposes, (iii) making Air Canada more vulnerable to economic downturns, and (iv) limiting Air Canada's flexibility in planning for, or reacting to, competitive pressures or changes in its business environment.

The ability of Air Canada to make scheduled payments under its indebtedness will depend on, among other things, its future operating performance and its ability to refinance its indebtedness, if necessary. In addition, as Air Canada incurs indebtedness which bears interest at fluctuating interest rates, to the extent these interest rates increase, its interest expense will increase. There can be no assurance that Air Canada will be able to generate sufficient cash from its operations to pay its debts and lease obligations. Each of these factors is, to a large extent, subject to economic, financial, competitive, regulatory, operational and other factors, many of which are beyond Air Canada's control.

Need for Additional Capital and Liquidity

Air Canada faces a number of challenges in its business, including in relation to economic conditions, pension plan funding, volatile fuel prices, contractual covenants which could require Air Canada to deposit cash collateral with third parties, foreign exchange rates and increased competition from international, transborder and low-cost domestic carriers. Air Canada's liquidity levels may be adversely impacted by these as well as by other factors and risks identified in this MD&A. As part of Air Canada's efforts to meet such challenges and to support Air Canada's business strategy, significant liquidity and significant operating and capital expenditures are, and will in the future be, required. There can be no assurance that Air Canada will continue to be able to obtain on a timely basis sufficient funds on terms acceptable to Air Canada to provide adequate liquidity and to finance the operating and capital expenditures necessary to overcome challenges and support its business strategy if cash flows from operations and cash on hand are insufficient.

Failure to generate additional funds, whether from operations or additional debt or equity financings, could require Air Canada to delay or abandon some or all of its anticipated expenditures or to modify its business strategy and could have a material adverse effect on Air Canada, its business, results from operations and financial condition. Furthermore, competitors with greater liquidity or their ability to raise money more easily and on less onerous terms could create a competitive disadvantage for Air Canada.

Air Canada's credit ratings influence its ability to access capital markets and its liquidity. There can be no assurance that Air Canada's credit ratings will not be downgraded, which would add to Air Canada's borrowing and insurance costs, hamper its ability to attract capital, adversely impact its liquidity, and limit its ability to operate its business, all of which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Economic and Geopolitical Conditions

Airline operating results are sensitive to economic and geopolitical conditions which can have a significant impact on Air Canada. For example, economic and geopolitical conditions may impact demand for air transportation in general or to or from certain destinations, as well as Air Canada's operating costs, pension plan contributions and costs and availability of capital and supplies required by Air Canada. Especially in light of Air Canada's substantial fixed cost structure, any prolonged or significant impact arising from economic and geopolitical conditions, including weakness of the Canadian, U.S. or world economies could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Airline fares and passenger demand have fluctuated significantly in the past and are likely to fluctuate significantly in the future. Air Canada is not able to predict with certainty market conditions and the fares that Air Canada may be able to charge. Customer expectations can change rapidly and the demand for lower fares may limit revenue opportunities. Travel, especially leisure travel, is a discretionary consumer expense. Depressed economic conditions in North America and other areas served by Air Canada, as well as geopolitical instability in various areas of the world, concerns about the environmental impacts of air travel and tendencies towards "green" travel initiatives where consumers reduce their travel activities, could have the effect of reducing demand for air travel in Canada and abroad and could materially adversely impact Air Canada's profitability.

Pension Plans

Canadian federal pension legislation requires that the funded status of registered pension plans be determined periodically, on both a going concern basis (essentially assuming indefinite plan continuation) and a solvency basis (essentially assuming immediate plan termination).

Pension plan solvency valuations are influenced primarily by long-term interest rates and by the investment return on plan assets, which in turn may be dependent on a variety of factors, including economic conditions.

The interest rate used to calculate benefit obligations for solvency purposes is a prescribed rate derived from the interest rates on long-term Government of Canada bonds. Deteriorating economic conditions may result in significant increases in Air Canada's funding obligations, which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

In particular, as of 2014, the Air Canada 2009 Pension Regulations will cease to have effect and Air Canada's pension funding obligations may vary significantly based on several factors, including regulatory developments, assumptions and methods used and changes in the economic conditions (mainly the return on fund assets and changes in interest rates). Underfunded pension plans or a failure or inability by Air Canada to make required cash contributions to its registered pension plans could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Fuel Costs

Fuel costs constituted the largest percentage of the total operating costs of Air Canada in 2009. Fuel prices fluctuate widely depending on many factors including international market conditions, geopolitical events and the Canada/U.S. dollar exchange rate. Air Canada cannot accurately predict fuel prices. During 2006, 2007 and 2008, fuel prices increased and fluctuated near or at historically high levels. Should fuel prices fluctuate significantly or increase significantly above current levels, fuel costs could have a material adverse effect on Air Canada, its business, results from operations and financial condition. Due to the competitive nature of the airline industry, Air Canada may not be able to pass on increases in fuel prices to its customers by increasing its fares. Based on 2009 volumes, Air Canada estimates that a US$1 per barrel movement in the average price of WTI crude oil would have resulted in an approximate $25 million change in 2009 fuel expense for Air Canada (excluding any impact of fuel surcharges, foreign exchange rates and fuel hedging), assuming flying capacity remained unchanged and that refining spreads between WTI crude oil and jet fuel as well as foreign exchange rates remained constant.

Foreign Exchange

Air Canada's financial results are sensitive to the fluctuating value of the Canadian dollar. In particular, Air Canada has a significant annual net outflow of U.S. dollars and is affected by fluctuations in the Canada/U.S. dollar exchange rate. Air Canada estimates that during 2009, a $0.01 increase in the Cdn/U.S. dollar exchange rate (i.e., $1.09 to $1.08 per U.S. dollar) would have had an estimated $23 million favourable impact on operating income and a $57 million favourable impact on pre-tax income. Conversely, an opposite change in the exchange rate would have had the opposite effect. Air Canada incurs significant expenses in U.S. dollars for such items as fuel, aircraft rental and maintenance charges, interest payments, debt servicing and computerized reservations system fees, while a substantial portion of its revenues are generated in Canadian dollars. A significant deterioration of the Canadian dollar relative to the U.S. dollar would increase the costs of Air Canada relative to its U.S. competitors and could have a material adverse effect on Air Canada, its business, results from operations and financial condition. In addition, Air Canada may be unable to appropriately hedge the risks associated with fluctuations in exchange rates.

Labour Costs and Labour Relations

Labour costs constitute one of Air Canada's largest operating cost items. There can be no assurance that Air Canada will be able to maintain such costs at levels which do not negatively affect its business, results from operations and financial condition. There can be no assurance that future agreements with employees' unions or the outcome of arbitrations will be on terms consistent with Air Canada's expectations or comparable to agreements entered into by Air Canada's competitors. Any future agreements or outcome of negotiations, mediations or arbitrations including in relation to wages or other labour costs or work rules may result in increased labour costs or other charges which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Most of Air Canada's employees are unionized. The collective agreements representing the majority of the unionized workforce were renewed or extended in 2009 and will now expire in 2011. No strikes or lock-outs may lawfully occur during the term of the collective agreements, nor during the negotiations of their renewal until a number of pre-conditions, in respect of the unions for Canadian-based employees, prescribed by the Canada Labour Code, have been satisfied. There can be no assurance that collective agreements will be further renewed without labour conflict or action or that there will not be a labour conflict that could lead to a dispute or to an interruption or stoppage in Air Canada's service or otherwise adversely affect the ability of Air Canada to conduct its operations, any of which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

If there is a labour disruption or work stoppage by any of the unionized work groups of Jazz, there would also likely be a material adverse effect on Air Canada, its business, results from operations and financial condition. In addition, labour conflicts at Star Alliance® partners could result in lower demand for connecting traffic with Air Canada and, ultimately, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Airline Industry Characterized by Low Gross Profit Margins and High Fixed Costs

The airline industry is characterized by low gross profit margins and high fixed costs. The costs of operating any particular flight do not vary significantly with the number of passengers carried and, therefore, a relatively small change in the number of passengers or in fare pricing or traffic mix would have a significant effect on Air Canada's operating and financial results. This condition has been exacerbated by aggressive pricing by low-cost carriers, which has had the effect of driving down fares in general. Accordingly, a shortfall from expected revenue levels could have a material adverse effect on Air Canada, its business, results from operations and financial condition. Air Canada incurs substantial fixed costs which do not meaningfully fluctuate with overall capacity. As a result, should Air Canada be required to reduce its overall capacity or the number of flights operated, it may not be able to successfully reduce certain fixed costs in the short term and may be required to incur important termination or other restructuring costs, which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Competition

Air Canada operates within a highly competitive industry. Over the past few years, several carriers have entered or announced their intention to enter or expand into the domestic, the U.S. transborder and international markets in which Air Canada operates.

Canadian low-cost and other carriers have entered and/or expanded or announced their intention to compete in many of Air Canada's key domestic markets and, along with some U.S. carriers have also entered and/or expanded their operations in the U.S. transborder and leisure-oriented markets. Carriers against which Air Canada may compete, including U.S. carriers, may undergo (and some of whom who have undergone) substantial reorganizations (including by way of merger with or acquisition by another carrier), creating reduced levels of indebtedness and lower operating costs and may be in a position to more effectively compete with Air Canada. Air Canada is also facing increasing competition in international markets as carriers increase their international capacity, both by expansion and by shifting existing domestic capacity to international operations to avoid low-cost domestic competition.

If Canadian low-cost and other carriers are successful in entering or expanding into Air Canada's domestic and the U.S. transborder markets, if additional U.S. or other carriers against which Air Canada competes are successful in entering Air Canada's transborder market or if carriers are successful in their expansion in international markets of Air Canada, Air Canada's business results from operations and financial condition could be materially adversely affected.

Air Canada also encounters substantial price competition. The expansion of low-cost carriers in recent years, along with the advent of Internet travel websites and other travel products distribution channels, has resulted in a substantial increase in discounted and promotional fares initiated by Air Canada's competitors. The decision to match competitors' fares to maintain passenger traffic, results in reduced yields which, in turn, could have a material adverse effect on Air Canada, its business, results from operations and financial condition. Furthermore, Air Canada's ability to reduce its fares in order to effectively compete with other carriers is dependent on Air Canada's ability to achieve acceptable operating margins and may also be limited by government policies to encourage competition. Likewise, competitors continue to pursue commission/incentive actions and, in many cases, increase these payments. The decision to modify Air Canada's current programs in order to remain competitive and maintain passenger traffic could result in increased costs to Air Canada's business.

In addition, consolidation in the airline industry could result in increased competition as some airlines emerging from such consolidations may be able to compete more effectively against Air Canada which could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Limitations Due to Restrictive Covenants
Some of the financing and other major agreements to which Air Canada is a party contain restrictive, financial (including in relation to liquidity, minimum EBITDAR, fixed charge coverage ratio and debt coverage ratios) and other covenants which affect and, in some cases, significantly limit or prohibit, among other things, the manner in which Air Canada may structure or operate its business, including by reducing Air Canada's liquidity, limiting Air Canada's ability to incur indebtedness, create liens, sell assets, pay dividends, make capital expenditures, and engage in acquisitions, mergers or restructurings or a change of control. Future financing and other major agreements may also be subject to similar covenants which limit Air Canada's operating and financial flexibility, which could materially and adversely affect Air Canada's ability to operate its business and its profitability.

A failure by Air Canada to comply with its contractual obligations (including restrictive, financial and other covenants), or to pay its indebtedness and fixed costs could result in a variety of material adverse consequences, including the acceleration of its indebtedness, the withholding of credit card proceeds by the credit card service providers and the exercise of remedies by its creditors and lessors, and such defaults could trigger additional defaults under other indebtedness or agreements. In such a situation, it is unlikely that Air Canada would be able to repay the accelerated indebtedness or fulfill its obligations under certain contracts, make required aircraft lease payments or otherwise cover its fixed costs. Also, the lenders under the financing arrangements could foreclose upon all or substantially all of the assets of Air Canada which secure Air Canada's obligations.

Airport User Fees and Air Navigation Fees
With the privatization of airports and air navigation authorities over the last decade in Canada, new airport and air navigation authorities have imposed significant increases in their fees. Though certain authorities have implemented some fee reductions, if authorities in Canada or elsewhere were to increase their fees Air Canada, its business, results from operations and financial condition could be materially adversely affected.

Strategic, Business, Technology and Other Important Initiatives
In order to operate its business, achieve its goals and remain competitive, Air Canada continuously seeks to identify and devise, invest in and implement strategic, business, technology and other important initiatives, such as those relating to the aircraft fleet restructuring program, business process initiatives, information technology initiatives and others. These initiatives, including activities relating to their development and implementation, may be adversely impacted by a wide range of factors, many of which are beyond Air Canada's control. Such factors include the performance of third parties, including suppliers, the implementation and integration of such initiatives into Air Canada's other activities and processes as well as the adoption and acceptance of initiatives by Air Canada's customers, suppliers and personnel. A delay or failure to sufficiently and successfully identify and devise, invest in or implement these initiatives could adversely affect Air Canada's ability to operate its business, achieve its goals and remain competitive and could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

For instance, a key component of Air Canada's business plan is the completion of Air Canada's fleet restructuring program through the acquisition of new and more efficient Boeing 787 aircraft. A delay or failure in the completion of Air Canada's fleet restructuring, including further delays by the manufacturers in the delivery of the wide-body aircraft, or an inability to remove, as planned, certain aircraft from the fleet in coordination with the planned entry into service of new aircraft, could adversely affect the implementation of Air Canada's business plan which may, in turn, have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Dependence on Technology
Air Canada relies heavily on technology, including computer and telecommunications equipment and software and Internet-based systems, to operate its business, increase its revenues and reduce its costs. These systems include those relating to Air Canada's telecommunications, websites, computerized airline reservations and airport customer services and flight operations.

These technology systems may be vulnerable to a variety of sources of failure, interruption or misuse, including by reason of third party suppliers' acts or omissions, natural disasters, terrorist attacks, telecommunications failures, power failures, computer viruses, unauthorized or fraudulent users, and other operational and security issues. While Air Canada continues to invest in initiatives, including security initiatives and disaster recovery plans, these measures may not be adequate or implemented properly. Any such technology systems failure, interruption or misuse could materially and adversely affect Air Canada's operations and could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Key Supplies and Suppliers

Air Canada is dependent upon its ability to source, on favourable terms and costs, sufficient quantities of goods and services in a timely manner, including those available at airports or from airport authorities or otherwise required for Air Canada's operations such as fuel, aircraft and related parts and aircraft maintenance services (including maintenance services obtained from Aveos). In certain cases, Air Canada may only be able to access goods and services from a limited number of suppliers and transition to new suppliers may take significant amounts of time and require significant resources. A failure, refusal or inability of a supplier may arise as a result of a wide range of causes, many of which are beyond Air Canada's control. In addition, in the context of the current economic climate, there can be no assurance as to the continued viability of any of Air Canada's suppliers. Any failure or inability of Air Canada to successfully source goods and services, including by reason of a failure, refusal or inability of a supplier, or to source goods and services on terms and pricing and within the timeframes acceptable to Air Canada, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Aeroplan

Through its commercial agreement with Aeroplan LP ("Aeroplan"), Air Canada is able to offer its customers who are Aeroplan® members the opportunity to earn Aeroplan® Miles. Based on customer surveys, Air Canada believes that rewarding customers with Aeroplan® Miles is a significant factor in customers' decision to travel with Air Canada and Jazz and contributes to building customer loyalty. The failure by Aeroplan to adequately fulfill its obligations towards Air Canada under the Aeroplan Commercial Participation and Services Agreement and in connection with the Aeroplan program®, or other unexpected interruptions of Aeroplan services which are beyond Air Canada's control, could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Jazz

Under the CPA, Jazz provides Air Canada's customers service in lower density markets and higher density markets at off-peak times throughout Canada and to and from certain destinations in the United States and also provides valuable traffic feed to Air Canada's mainline routes. Pursuant to the terms of the Jazz CPA, Air Canada pays Jazz a number of fees which are determined based upon certain costs incurred by Jazz. Air Canada also reimburses Jazz, without mark-up, for certain pass-through costs incurred directly by Jazz, such as fuel, navigation, landing and terminal fees and certain other costs. Significant increases in such pass-through costs, the failure by Jazz to adequately fulfill its obligations towards Air Canada under the Jazz CPA, or other unexpected interruptions or cessation of Jazz's services which are beyond Air Canada's control could have a material adverse effect on Air Canada, its business, results from operations and financial condition. In addition, the Jazz CPA requires that Jazz maintain a minimum fleet size and contains a minimum average daily utilization guarantee which requires that Air Canada make certain minimum payments to Jazz regardless of the amount of flying done on its behalf by Jazz.

Star Alliance®

The strategic and commercial arrangements with Star Alliance® members provide Air Canada with important benefits, including codesharing, efficient connections and transfers, reciprocal participation in frequent flyer programs and use of airport lounges from the other members. Should a key member leave Star Alliance® or otherwise fail to meet its obligations thereunder, Air Canada, its business, results from operations and financial condition could be materially adversely affected.

Interruptions or Disruptions in Service

Air Canada's business is significantly dependent upon its ability to operate without interruption at a number of hub airports, including Toronto Pearson International Airport. Delays or disruptions in service, including those due to security or other incidents, weather conditions, labour conflicts with airport workers, baggage handlers, air traffic controllers and other workers not employed by Air Canada or other causes beyond the control of Air Canada could have a material adverse impact on Air Canada, its business, results from operations and financial condition.

Current Legal Proceedings

The European Commission, the United States Department of Justice and the Competition Bureau in Canada are investigating alleged anti-competitive cargo pricing activities, including the levying of certain fuel surcharges, of a number of airlines and cargo operators, including Air Canada. Competition authorities have sought or requested information from Air Canada as part of their investigations. Air Canada is cooperating with these investigations, which are likely to lead, or have led, to proceedings against Air Canada and a number of airlines and other cargo operators in certain jurisdictions including in the European Union where all formal procedural steps preceding a decision have been completed. Air Canada is also named as a defendant in a number of class action lawsuits that have been filed before the United States District Court and in Canada in connection with these allegations.

During 2008, Air Canada recorded a provision of $125 million as a preliminary estimate. This is only an estimate 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 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 and such provisions could have a material adverse effect on Air Canada's financial position.

In February 2006, Jazz commenced proceedings before the Ontario Superior Court of Justice against Porter Airlines Inc. ("Porter") and other defendants (collectively the "Porter Defendants") after Jazz became aware that it would be excluded from operating flights from Toronto City Centre (Island) Airport (the "TCCA"). On October 26, 2007, the Porter Defendants counter-claimed against Jazz and Air Canada alleging various violations of competition law, including that Jazz and Air Canada's commercial relationship contravenes Canadian competition laws, and claiming $850 million in damages. Concurrently with the Ontario Superior Court of Justice proceedings, Jazz commenced judicial review proceedings against the Toronto Port Authority ("TPA") before the Federal Court of Canada relating to Jazz's access to the TCCA. The Porter Defendants were granted intervener and party status in these proceedings. In January of 2008, Porter filed a defence and counterclaim against Jazz and Air Canada making allegations and seeking conclusions similar to those in the Ontario Superior Court counterclaim. On October 16, 2009, Jazz discontinued its suit in the Ontario Superior Court against Porter. However, Jazz is continuing its proceedings in the Federal Court of Canada against the TPA, to which Porter intervened. The counterclaim filed by Porter in the Ontario Court against Jazz and Air Canada has been stayed pending the outcome of the mirror counterclaim in the Federal Court. Air Canada views Porter's counterclaims in both jurisdictions as being without merit.

The Canadian Union of Public Employees ("CUPE"), which represents Air Canada's flight attendants, has filed a complaint before the Canadian Human Rights Commission where it alleges gender-based wage discrimination. CUPE claims the predominantly female flight attendant group should be paid the same as the predominantly male pilot and mechanics groups because their work is of equal value. The complaint dates from 1991 but has not been investigated on the merits because of a legal dispute over whether the three groups work in the same "establishment" within the meaning of the Canadian Human Rights Act. On January 26, 2006, the Supreme Court of Canada ruled that they do work in the same "establishment" and sent the case back to the Canadian Human Rights Commission, which may now proceed to assess the merits of CUPE's complaint. On March 16, 2007, the Canadian Human Rights Commission referred the complaint against Air Canada for investigation. Air Canada considers that any investigation will show that it is complying with the equal pay provisions of the Canadian Human Rights Act, however, Air Canada has determined that it is not possible at this time to predict with any degree of certainty the final outcome of the Commission's investigation.

Air Canada is engaged in a number of proceedings involving challenges to the mandatory retirement provisions of certain of its collective agreements, including the Air Canada-Air Canada Pilots Association collective agreement which incorporate provisions of the pension plan terms and conditions applicable to pilots requiring them to retire at age 60.

Air Canada is defending these challenges. At this time, it is not possible to determine with any degree of certainty the extent of any financial liability that may arise from Air Canada being unsuccessful in its defense of these proceedings, though any such financial liability, if imposed, would not be expected to be material.

Future Legal proceedings
Airlines are susceptible to various claims and litigation, including class action claims, in the course of operating their business or with respect to the interpretation of existing agreements. Any future claims or litigation could also have a material adverse effect on Air Canada, its business and results from operations.

Key Personnel
Air Canada is dependent on the experience and industry knowledge of its executive officers and other key employees to execute its business plan. If Air Canada were to experience a substantial turnover in its leadership or other key employees, Air Canada's business, results from operations and financial condition could be materially adversely affected. Additionally, Air Canada may be unable to attract and retain additional qualified key personnel as needed in the future.

Risks Relating to the Airline Industry

Terrorist Attacks and Security Measures
The September 11, 2001 terrorist attacks and subsequent terrorist activity, notably in the Middle East, Southeast Asia, Europe and the U.S., causes uncertainty in the minds of the traveling public. The occurrence of a terrorist attack (or attempted attacks) (whether domestic or international and whether involving Air Canada or another carrier or no carrier at all) and increasingly restrictive security measures, such as current restrictions on the content of carry-on baggage, current or proposed passenger identification document requirements, and passenger screening procedures could have a material adverse effect on passenger demand for air travel and on the number of passengers traveling on Air Canada's flights. It could also lead to a substantial increase in insurance, airport security and other costs. Any resulting reduction in passenger revenues and/or increases in insurance, security or other costs could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Epidemic Diseases (Severe Acute Respiratory Syndrome (SARS), H1N1 Influenza or Other Epidemic Diseases)
The international outbreaks of Severe Acute Respiratory Syndrome (SARS) in 2003 and the resulting actions tabled by the World Health Organization (the "WHO"), including a travel advisory against non-essential travel to Toronto, Canada, had a significant adverse effect on passenger demand for air travel in Air Canada's markets and resulted in a major negative impact on traffic on the entire network. 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 its operations to the extent this risk does materialize. An outbreak of influenza, SARS, H1N1 influenza virus or of another epidemic disease (whether domestic or international) or any WHO travel advisories (whether relating to Canadian cities or regions or other cities, regions or countries) could have a material adverse effect on passenger demand for air travel. Any resulting reduction in traffic in the markets served by Air Canada could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Casualty Losses
Due to the nature of its core operating business, Air Canada may be subject to liability claims arising out of accidents or disasters involving aircraft on which Air Canada's customers are traveling or involving aircraft of other carriers maintained or repaired by Air Canada, including claims for serious personal injury or death. There can be no assurance that Air Canada's insurance coverage will be sufficient to cover one or more large claims and any shortfall may be material. Additionally, any accident or disaster involving one of Air Canada's aircraft or an aircraft of another carrier receiving line maintenance services from Air Canada may significantly harm Air Canada's reputation for safety, which would have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Seasonal Nature of the Business, Other Factors and Prior Performance
Air Canada has historically experienced considerably greater demand for its services in the second and third quarters of the calendar year and significantly lower demand in the first and fourth quarters of the calendar year. This demand pattern is principally a result of the preference of a high number of leisure travelers to travel during the spring and summer months. Air Canada has substantial fixed costs that do not meaningfully fluctuate with passenger demand in the short term.

As described elsewhere, demand for and cost of air travel is also affected by factors such as geopolitical and economic conditions, war or the threat of war or terrorist attacks, fare levels and weather conditions. Due to these and other factors, operating results for an interim period are not necessarily indicative of operating results for an entire year, and operating results for a historical period are not necessarily indicative of operating results for a future period.

Regulatory Matters

The airline industry is subject to extensive Canadian and foreign government regulations relating to, among other things, security, safety, privacy, licensing, competition, environment (including noise levels and carbon emissions) and, in some measure, pricing.

For example, new and proposed legislation have been considered or adopted concerning carbon emissions emanating from the aviation industry; such legislative initiatives include, for example, market-based mechanisms called emissions trading systems which are being proposed and implemented to reduce the amount of carbon emissions through the setting of emissions allowances and charging aircraft operators for a certain percentage of these allowances. The implementation of additional regulations or decisions, including those relating to carbon emissions, and others, whether by Transport Canada, the Competition Bureau and/or the Competition Tribunal, the Canadian Transportation Agency or other domestic or foreign governmental entities, may have a material adverse effect on Air Canada, its business, results from operations and financial condition.

The European Union passed legislation for an Emissions Trading System which will include carbon emissions from aviation commencing in January 2012, including for flights operated between Canada and countries within the European Union. The legislation would require aircraft operators to monitor and report on fuel use and emissions data. While this legislation would be expected to result in increased costs relating to the purchase of emissions allowances, the net financial impact would, in part, depend upon how much of such cost, if any, would be recoverable in the form of higher passenger and cargo fares.

The availability of international routes to Canadian air carriers is regulated by agreements between Canada and foreign governments. Changes in Canadian or foreign government aviation policy could result in the alteration or termination of these agreements and could adversely affect Air Canada, its international operations.

Air Canada is subject to domestic and foreign laws regarding privacy of passenger and employee data, including advance passenger information and access to airline reservation systems, which are not consistent in all countries in which Air Canada operates. The need to comply with these regulatory regimes is expected to result in additional operating costs and could have a material adverse effect on Air Canada, its business, results from operations and financial condition.

There can be no assurances that new laws, regulations or revisions to same, or decisions, will not be adopted or rendered, from time to time, and these could impose additional requirements or restrictions, which may adversely impact Air Canada's business, results from operations and financial condition.

Increased Insurance Costs

Since September 11, 2001 the aviation insurance industry has been continually re-evaluating the terrorism risks that it covers, and this activity may adversely affect some of Air Canada's existing insurance carriers or Air Canada's ability to obtain future insurance coverage. To the extent that Air Canada's existing insurance carriers are unable or unwilling to provide it with insurance coverage, and in the absence of measures by the Government of Canada to provide the required coverage, Air Canada's insurance costs may increase further and may result in Air Canada being in breach of regulatory requirements or contractual arrangements requiring that specific insurance be maintained, which may have a material adverse effect on Air Canada, its business, results from operations and financial condition.

Third Party War Risk Insurance

There is a risk that the Government of Canada may not continue to provide an indemnity for third party war risk liability coverage, which it currently provides to Air Canada and certain other carriers in Canada. In the event that the Government of Canada does not continue to provide such indemnity or amends such indemnity, Air Canada and other industry participants would have to turn to the commercial insurance market to seek such coverage. Air Canada estimates that such coverage would cost Air Canada approximately $5 million per year. Alternative solutions, such as those envisioned by the International Civil Aviation Organization ("ICAO") and the International Air Transport Association ("IATA"), have not developed as planned, due to actions taken by other countries and the recent availability of supplemental insurance products. ICAO and IATA are continuing their efforts in this area, however, the achievement of a global solution is not likely in the immediate or near future. The U.S. federal government has set up its own facility to provide war risk coverage to U.S. carriers, thus removing itself as a key component of any global plan.

16. Controls and Procedures

Disclosure Controls and Procedures and Internal Controls over Financial Reporting

Disclosure controls and procedures within the Corporation have been designed to provide reasonable assurance that all relevant information is identified to its Disclosure Policy Committee to ensure appropriate and timely decisions are made regarding public disclosure.

Internal controls over financial reporting have been designed by management, with the participation of the Corporation's Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), to provide reasonable assurance regarding the reliability of the Corporation's financial reporting and its preparation of financial statements for external purposes in accordance with GAAP.

The Corporation will file certifications, signed by the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), with the Canadian Securities Administrators ("CSA") upon filing of the Corporation's 2010 Annual Information Form. In those filings, the Corporation's CEO and CFO will certify, as required by National Instrument 52-109, the appropriateness of the financial disclosure, the design and effectiveness of the Corporation's disclosure controls and procedures and the design and effectiveness of internal controls over financial reporting. The Corporation's CEO and CFO also certify the appropriateness of the financial disclosures in the Corporation's interim filings with securities regulators. In those interim filings, the Corporation's CEO and CFO also certify the design of the Corporation's disclosure controls and procedures and the design of internal controls over financial reporting.

Management's Report on Disclosure Controls and Procedures

Management, with the participation of the Corporation's CEO and CFO, concluded, as at December 31, 2009, that such disclosure controls and processes were designed to provide reasonable assurance that:

(i) material information relating to the Corporation was made known to its Disclosure Policy Committee by others; and

(ii) information required to be disclosed by the Corporation in its annual filings, interim filings and other reports filed or submitted by the Corporation under securities legislation was recorded, processed, summarized and reported within the time periods specified in securities legislation.

In addition, the evaluation covered the Corporation's processes, systems and capabilities relating to regulatory filings, public disclosures and the identification and communication of material information.

Management's Report on Internal Controls over Financial Reporting

Management, with the participation of the Corporation's CEO and CFO, assessed the effectiveness of the Corporation's internal controls over financial reporting. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in Internal Control - Integrated Framework. Based on that evaluation, management and the CEO and CFO have concluded that, as at December 31, 2009, the Corporation's internal controls over financial reporting were effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. This evaluation took into consideration the Corporation's Corporate Disclosure Policy and the functioning of its Disclosure Policy Committee.

Changes in Internal Controls over Financial Reporting

There have been no changes to the Corporation's internal controls over financial reporting during the year ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, its internal controls over financial reporting.

17. Selected Annual Information

The following table provides selected annual information for ACE for the years 2009, 2008 and 2007. The information provided below may not be directly comparable as a result of changes in accounting policies relating to Air Canada, Aeroplan, Jazz and ACTS.

($ millions, except per share figures)	2009 (1)	2008	2007 (2)
Operating revenues	$ 8,206	$ 11,080	$ 10,826
Operating expenses	(8,450)	(11,154)	(10,373)
Operating income (loss) before the provision for cargo investigations	**(244)**	**(74)**	**453**
Provision for cargo investigations (3)	-	(125)	-
Operating income (loss)	**(244)**	**(199)**	**453**
Total non-operating income (expense), non-controlling interest, foreign exchange gain (loss) and income tax (4)	(448)	79	945
Net income (loss)	**$ (692)**	**$ (120)**	**$ 1,398**
Earning (loss) per share			
- Basic	**$(19.56)**	**$ (2.59)**	**$ 13.51**
- Diluted	**$(19.56)**	**$ (2.59)**	**$ 11.44**
Cash, cash equivalents and short-term investments	**$ 71**	**$ 1,813**	**$ 3,139**
Total assets	**$ 323**	**$ 11,871**	**$ 13,754**
Total long-term liabilities (5)	**$ -**	**$ 7,804**	**$ 7,181**

(1) The results, financial position and cash flows of Air Canada are not consolidated with ACE effective October 27, 2009.

(2) The results and financial position of Aeroplan, Jazz and ACTS are not consolidated with ACE effective March 14, 2007, May 24, 2007 and October 16, 2007, respectively.

(3) Air Canada recorded a provision for cargo investigations of $125 million in 2008.

(4) Non-operating income (expense) includes losses on ACE's investment in Air Canada of $630 million in 2009, includes gains on assets which amounted to $946 million in 2008, $1,366 million in 2007. Also included are net gains on foreign exchange of $531 million in 2009; net losses on foreign exchange of $655 million in 2008; net gains on foreign exchange of $313 million in 2007.

(5) Total long-term liabilities include long-term debt (including current portion) and capital leases, convertible preferred shares, pension and other benefit liabilities and other long-term liabilities.

18. Glossary of Terms

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.

CASM — Operating expense per ASM.

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

Passenger Revenue per Available Seat Mile or RASM — Average passenger revenue per ASM.

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.

Yield — Average passenger revenue per RPM.