MAY 13, 2005

FIRST QUARTER 2005
MANAGEMENT’S DISCUSSION AND ANALYSIS

ACE AVIATION HOLDINGS INC.

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PREFACE

ACE Aviation Holdings Inc. (ACE) was incorporated on June 29, 2004 for the purposes of becoming the parent company of Air Canada and its subsidiaries upon the implementation of the consolidated plan of reorganization, compromise and arrangement (the Plan) on September 30, 2004, as further described in the 2004 Annual Consolidated Financial Statements of ACE.

In accordance with Section 1625 of the CICA Handbook, Comprehensive Revaluation of Assets and Liabilities (CICA 1625), ACE adopted fresh start reporting on September 30, 2004. References to “Predecessor Company” refer to Air Canada and its subsidiaries prior to September 30, 2004. References to “Successor Company” refer to ACE and its subsidiaries on and after June 29, 2004. In accordance with CICA 1625, prior period financial information has not been restated to reflect the impact of fair value adjustments and, accordingly, certain amounts in the Predecessor Company’s results are not directly comparable with those of the Successor Company.

As a result of the application of fresh start reporting, the application of new accounting policies, the effectiveness of certain lease contracts on emergence from creditor protection under the Companies’ Creditors Arrangement Act (CCAA) and the debt and equity transactions that occurred on September 30, 2004, the Successor Company’s financial statements are not directly comparable to those prepared for the Predecessor Company. The presentation of the financial information of ACE for the period ended March 31, 2005 and the financial information of Air Canada for the period ended March 31, 2004 are not directly comparable because the financial statements of Air Canada for periods prior to October 1, 2004 and the financial statements of ACE for periods on and after October 1, 2004 are those of different reporting entities and are prepared using different bases of accounting and different accounting policies.

The consolidated balance sheet as of March 31, 2005 and December 31, 2004 represent the accounts of the Successor Company. The consolidated statement of operations and cash flow for the three months ended March 31, 2005 reflects the results of operations of the Successor Company; the three months ended March 31, 2004 reflects the results of operations of the Predecessor Company.

The Interim Unaudited Consolidated First Quarter 2005 Financial Statements for the Successor Company are based on the accounting policies consistent with those disclosed for the Successor Company in Note 4 to the 2004 Annual Consolidated Financial Statements of ACE with the exception of the adoption of the accounting policies described in Note 1 to the Interim Unaudited Consolidated First Quarter 2005 Financial Statements under "New Accounting Policies" and page 35 of this MD&A under the section entitled "Accounting Policies".

In accordance with Canadian Generally Accepted Accounting Principles (GAAP), the Interim Unaudited Consolidated First Quarter 2005 Financial Statements do not include all of the disclosures required for annual financial statements and should be read in conjunction with the 2004 Annual Consolidated Financial Statements of ACE. All amounts are expressed in Canadian currency unless indicated otherwise. This Management's Discussion and Analysis is as of May 13, 2005.

See Note 1 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements for additional information on the nature of operations and accounting policies.

For further information on ACE's and Air Canada's public disclosure file, please consult www.sedar.com.

CAUTION REGARDING FORWARD-LOOKING INFORMATION

ACE's communications often contain written or oral forward-looking statements which are included in the MD&A and may be included in filings with securities regulators in Canada and the United States. These forward-looking statements are identified by the use of terms and phrases such as "anticipate", "believe", "could", "estimate", "expect", "intend", "may", "plan", "predict", "project", "will", "would", and similar terms and phrases, including references to assumptions. All such statements are made pursuant to the "safe harbour" provisions of the governing US securities legislation. Such statements may involve but are not limited to comments with respect to strategies, expectations, planned operations or future actions.

Forward-looking statements, by their nature, are based on assumptions and are subject to important risks and uncertainties. Any forecasts or forward-looking predictions or statements cannot be relied upon due to, amongst other things, changing external events and general uncertainties of the business. Results indicated in forward-looking statements may differ materially from actual results for a number of reasons, including without limitation, energy prices, general industry, market and economic conditions, war, terrorist attacks, changes in demand due to the seasonal nature of the business, the ability to reduce operating costs and employee counts, employee relations, labour negotiations or disputes, restructuring, pension issues, currency exchange and interest rates, changes in laws, adverse regulatory developments or proceedings, pending litigation and actions by third parties. The forward-looking statements contained in this discussion represent ACE's expectations as of May 13, 2005, 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.

ACE AVIATION HOLDINGS INC.
FIRST QUARTER 2005
MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS

EXPLANATORY NOTES

Glossary of Terms

Revenue Passenger Miles (RPMs)

A measure of passenger traffic calculated by multiplying the total number of revenue passengers carried by the miles they are carried.

Available Seat Miles (ASMs)

A measure of passenger capacity calculated by multiplying the total number of seats available for revenue traffic by the miles flown.

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 Revenue Passenger Mile (yield per RPM)

Average passenger revenue per revenue passenger mile.

Passenger Revenue per Available Seat Mile (RASM)

Average passenger revenue per available seat mile.

"Corporation" refers to, as the context may require, ACE and its subsidiaries collectively, ACE and one or more of its subsidiaries, one or more of ACE's subsidiaries, or ACE itself.

"Subsidiary" or "subsidiaries" refers to, in relation to ACE, any entity, including a corporation or a limited partnership, which is controlled, directly or indirectly, by ACE.

Comparative Figures

Certain of the prior year's figures have been reclassified to conform to the current year's presentation. Short-term investments with original maturities greater than ninety days were previously included in cash and cash equivalents. Because of increased significance, they are now presented separately as short-term investments. Short-term investments have original maturities over 90 days, but not more than one year. These investments can be readily converted to cash and are with institutions that have high credit ratings.

Non-GAAP Financial Measure

EBITDAR (earnings before interest, taxes, depreciation, amortization and obsolescence and aircraft rent) is a non-GAAP financial measure commonly used in the airline industry to view operating results before aircraft rent and ownership costs as these costs can vary significantly among airlines due to differences in the way airlines finance their aircraft and other asset acquisitions.

EBITDAR is not a recognized measure for financial statement presentation under GAAP and does not have a standardized meaning and is therefore not likely to be comparable to similar measures presented by other public companies. EBITDAR, before reorganization and restructuring items, is reconciled to operating income (loss) before reorganization and restructuring items, as follows:

	Successor Company ACE	Predecessor Company Air Canada	
($ millions)	**Three Months ended March 31, 2005**	**Three Months ended March 31, 2004**	**Change**
GAAP operating loss before reorganization and restructuring items (1)	(10)	(145)	135
Add back:			
Depreciation, amortization and obsolescence	120	95	25
Aircraft rent	90	194	(104)
EBITDAR, before reorganization and restructuring items (1)	200	144	56
EBITDAR margin (%) (2)	9.2	6.8	2.4 pp

(1) Reorganization and restructuring items were recorded while Air Canada was under creditor protection from April 1, 2003 through to September 30, 2004. As Air Canada emerged from CCAA proceedings on September 30, 2004, reorganization and restructuring items were not recorded after that date.

(2) EBITDAR margin is calculated as EBITDAR divided by operating revenues.

Loyalty Program

As described in Note 1 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements, ACE implemented a loyalty program accounting policy as of September 30, 2004 that was different from the policy employed by Air Canada, the Predecessor Company.

As a result of the application of fresh start reporting, the outstanding loyalty program mileage credits ("Miles") were adjusted to reflect the estimated fair value of Miles to be redeemed in the future. As a consequence of this fair value adjustment and the evolving nature of the Aeroplan loyalty program, the Successor Company changed the accounting policy as of September 30, 2004 for the recognition of its obligations relating to the loyalty program. The Predecessor Company recognized the obligation related to Miles earned through transportation services based on the incremental cost of providing future transportation services. On a prospective basis from the date of fresh start reporting, Miles earned by members through transportation services provided by the Corporation and the transportation services are treated as multiple elements. Miles are recorded at fair values with the residual allocated to transportation services. Consistent with the accounting policy of the Predecessor Company, the proceeds from the sale of Miles to loyalty program partners are deferred.

Effective September 30, 2004, Miles redeemed for travel on Air Canada and Jazz are included in passenger revenues and Miles redeemed for other than travel are included in other revenues. Under the previous accounting policy in the Predecessor Company, Aeroplan redemption revenues from Miles earned by members through loyalty program partners were included in other revenues.

The sum of passenger revenues from Miles redeemed for air travel on Air Canada and Jazz and the above-noted deferred revenues are referred to as “Aeroplan passenger revenues” in this MD&A. For additional information on the Loyalty Program, refer to the section entitled “Accounting Policies” on page 35 of this MD&A.

In the first quarter of 2005, Aeroplan revenues from Miles redeemed for air travel on Air Canada and Jazz amounted to $101 million, of which $65 million related to Aeroplan redemption revenues from Miles earned by members through the loyalty program partners. These redemption revenues were partly offset by the deferral of revenues of $44 million related to the fair value of Miles earned by members through transportation services provided by the Corporation, resulting in net Aeroplan passenger revenues of $57 million. For the three months

ended March 31, 2004, Aeroplan revenues from Miles earned by members through the loyalty program partners amounted to $70 million.

FIRST QUARTER RESULTS OF OPERATIONS – 2005 VERSUS 2004

The following table sets out the first quarter 2005 results of operations for ACE, the Successor Company, as compared to the first quarter 2004 results of operations for Air Canada, the Predecessor Company.

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

ACE Aviation Holdings Inc.
Consolidated Statement of Operations

($ millions, except per share figures) (Unaudited)	Successor Company ACE Three Months ended March 31, 2005	Predecessor Company Air Canada Three Months ended March 31, 2004	$ Change	% Change
Operating revenues				
Passenger	1,739	1,661	78	5
Cargo	135	126	9	7
Other	303	334	(31)	(9)
	2,177	2,121	56	3
Operating expenses				
Salaries, wages and benefits	613	687	(74)	(11)
Aircraft fuel	415	338	77	23
Aircraft rent	90	194	(104)	(54)
Airport and navigation fees	213	203	10	5
Aircraft maintenance, materials and supplies	94	103	(9)	(9)
Communications and information technology	77	88	(11)	(13)
Food, beverages and supplies	78	79	(1)	(1)
Depreciation, amortization and obsolescence	120	95	25	26
Commissions	65	80	(15)	(19)
Other	422	399	23	6
	2,187	2,266	(79)	(3)
Operating loss before reorganization and restructuring items	(10)	(145)	135	
Reorganization and restructuring items	-	(132)	132	
Non-operating income (expense)				
Interest income	12	4	8	
Interest expense	(75)	(47)	(28)	
Interest capitalized	3	-	3	
Loss on sale of and provisions on assets	-	(3)	3	
Non-controlling interest	(3)	-	(3)	
Other	(3)	3	(6)	
	(66)	(43)	(23)	
Loss before foreign exchange on non-compromised long-term monetary items and income taxes	(76)	(320)	244	
Foreign exchange gain (loss) on non-compromised long-term monetary items	(15)	17	(32)	
Loss before income taxes	(91)	(303)	212	
Recovery of (Provision for) income taxes	14	(1)	15	
Loss	(77)	(304)	227	
Loss per share				
- Basic and diluted	(0.87)	(2.53)		
Operating Statistics				
Revenue Passenger Miles (millions)	10,586	10,057	529	5
Available Seat Miles (millions)	13,566	13,797	(231)	(2)
Passenger Load Factor (%)	78.0	72.9	5.1 pp	

Comparison of First Quarter Results

In the first quarter of 2005, ACE reported an operating loss of $10 million, an improvement of $135 million compared to Air Canada's operating loss before reorganization and restructuring items of $145 million recorded in the same quarter of 2004. EBITDAR improved $56 million over the 2004 quarter. Refer to "Non-GAAP Financial Measure" on page 6 of this MD&A for additional information on EBITDAR.

In the first quarter of 2005, total operating revenues increased $56 million or 3 per cent compared to the first quarter of 2004. Passenger revenues increased $78 million or 5 per cent reflecting increases in all markets with the exception of the US transborder market and the transfer of Aeroplan passenger revenues of $57 million into the passenger revenue category. For additional information on Aeroplan passenger revenues, refer to page 7 of this MD&A.

Operating expenses were reduced by $79 million or 3 per cent compared to the 2004 quarter in spite of an increase in fuel expense of $77 million or 23 per cent. Capacity, as measured in available seat miles (ASM) was reduced by 2 per cent. Unit cost for the first quarter of 2004, as measured by operating expense per ASM, was 2 per cent below the first quarter of 2004. Excluding fuel expense, unit cost was down 6 per cent compared to the 2004 quarter. Unit cost reductions were achieved in essentially all controllable categories including salaries, wages and benefits, aircraft rent, aircraft maintenance, materials and supplies, and communications and information technology.

While under creditor protection from April 1, 2003 through to September 30, 2004, Air Canada recorded significant reorganization and restructuring items directly associated with the rearranging of its business affairs. In the first quarter of 2004, reorganization and restructuring items amounted to $132 million. These mainly non-cash items related primarily to lease deficiency claims, labour-related items, foreign exchange adjustments on compromised debt and professional fees. As Air Canada emerged from CCAA proceedings on September 30, 2004, reorganization and restructuring were not recorded after that date.

Foreign exchange losses on long-term monetary items totaled $15 million in the first quarter of 2005 attributable to a weaker Canadian dollar versus the US dollar at March 31, 2005 compared to December 31, 2004. This compared to foreign exchange gains on non-compromised long-term monetary items of $17 million in the first quarter of 2004.

Net loss for the quarter was $77 million compared to a net loss of $304 million in the first quarter of 2004, an improvement of $227 million. The first quarter of 2004 included reorganization and restructuring items amounting to $132 million.

RASM
Passenger revenue per available seat mile (RASM) is a common industry measure of passenger revenue performance providing a yardstick of revenue generation per unit of capacity offered. RASM is influenced by two key components: • Load factor • Yield per RPM The first component is load factor which represents passenger traffic expressed in relation to the capacity offered (i.e. revenue passenger miles (RPMs) to available seat miles (ASMs)). The second component is the yield per revenue passenger mile (or average fare paid per occupied seat mile flown). If an airline can improve its load factor on a particular flight (i.e. the number of revenue passengers) or its yield per revenue passenger mile (i.e. the average fare per mile paid by each passenger) then the passenger revenue per available seat mile (RASM) will increase leading to greater operating profitability on that flight. Depending on market conditions, airlines may periodically have a greater focus on improving load factor or yield, however, the interaction of both these factors will determine RASM. The higher the RASM, the more revenue is generated by the airline for each available seat. Long-haul flights generally have a lower yield per RPM than short-haul flights. When measured on a per mile basis, the average fare paid on long-haul flights is relatively lower than on short-haul flights. Because the costs of ground handling and fees for take-off and landing are similar for both short and long-haul flights, unit costs per ASM are normally lower for long-haul flights due to the distance flown.

REVENUE PERFORMANCE

Passenger Revenues

As a result of the inclusion of Aeroplan passenger revenues in passenger revenues starting in October 2004 as described on page 7 of this MD&A, passenger revenues, RASM and yield per RPM are not directly comparable to previous years. The following discussion will provide the reader with passenger revenue, RASM and yield per RPM variances that include Aeroplan passenger revenues. However, for comparative purposes, the discussion and tables will also provide passenger revenue, RASM and yield per RPM information excluding Aeroplan passenger revenues.

The table below describes, by major market, the percentage change from the prior year in passenger revenues for the eight most recent quarters.

Passenger Revenue % Change Year-over-Year by Quarter

	Predecessor Company Air Canada						Successor Company ACE	
	Quarter 2 2003	**Quarter 3 2003**	**Quarter 4 2003**	**Quarter 1 2004**	**Quarter 2 2004**	**Quarter 3 2004**	**Quarter 4 2004**	**Quarter 1 2005**
Canada (1)	(26)	(17)	(13)	(9)	8	3	0	1
US (1)	(27)	(24)	(19)	(13)	5	(1)	(17)	(13)
Atlantic (1)	(11)	(4)	(5)	(5)	6	6	4	8
Pacific (1)	(63)	(52)	(13)	15	162	113	35	14
Other (1)	(8)	3	18	24	38	25	22	17
System (1) (excluding Aeroplan)	(26)	(19)	(12)	(5)	15	12	1	1
System (including Aeroplan)	(26)	(19)	(12)	(5)	15	12	4	5

(1) The calculation of percentage change year-over-year does not include Aeroplan passenger revenues for the fourth quarter of 2004 and the first quarter of 2005.

The table below describes, by major market, quarter-over-quarter percentage changes in passenger revenues, capacity as measured by available seat miles (ASMs), traffic as measured by revenue passenger miles (RPMs), passenger load factor as measured by RPMs divided by ASMs, yield as measured by passenger revenue per RPM, and RASM as measured by passenger revenue per ASM.

Operating Statistics – Quarter 1, 2005 versus Quarter 1, 2004

	Passenger Revenue % Change	Capacity (ASMs) % Change	Traffic (RPMs) % Change	Passenger Load Factor pp Change	Yield per RPM % Change	RASM % Change
Canada (1)	1	(3)	4	5.1	(3)	4
US (1)	(13)	(12)	(1)	8.4	(12)	(1)
Atlantic (1)	8	(3)	4	4.9	4	11
Pacific (1)	14	5	8	1.8	5	8
Other (1)	17	14	18	3.1	(1)	3
System (1) (excluding Aeroplan)	1	(2)	5	5.1	(4)	3
System (including Aeroplan)	5	(2)	5	5.1	0	7

(1) The calculation of percentage change quarter-over-quarter does not include Aeroplan passenger revenues for the first quarter of 2005.

Passenger revenues were up $78 million or 5 per cent from 2004 and included Aeroplan passenger revenues of $57 million in the first quarter of 2005.

In the first quarter of 2005, system passenger traffic increased 5 per cent on a decrease of 2 per cent in ASM flying capacity producing a 5.1 percentage point improvement in load factor. Passenger traffic is measured by revenue passenger miles which is calculated by multiplying the number of revenue passengers carried by the miles they are carried. Excluding Aeroplan passenger revenues, yield per RPM, as measured by average passenger revenue per revenue passenger mile, decreased 4 per cent. The yield per RPM decrease was mainly due to increased low-cost competition, a weak transborder market and a greater proportion of longer haul flying which has a lower yield per RPM. However, with the major improvement in load factor, system RASM, excluding Aeroplan passenger revenues, rose 3 per cent over the first quarter of 2004.

First quarter domestic passenger revenues were up $30 million or 5 per cent and included Aeroplan passenger revenues of $24 million in the 2005 quarter. Domestic passenger

traffic was up 4 per cent and capacity was reduced by 3 percent resulting in a passenger load factor improvement of 5.1 percentage points. Domestic yield per RPM decreased 3 per cent, excluding Aeroplan passenger revenues, mainly due to increased price discounting in the domestic market. However, reflecting the improvement in passenger load factor, excluding Aeroplan passenger revenues, domestic RASM rose 4 per cent above the 2004 level.

US transborder passenger revenues were down $36 million or 9 per cent and included Aeroplan passenger revenues of $18 million in the 2005 quarter. In response to increased capacity from US carriers, US transborder ASM capacity was reduced by 12 per cent. In spite of the ASM capacity reduction, traffic declined only 1 per cent resulting in a passenger load factor improvement of 8.4 percentage points. Excluding Aeroplan passenger revenues, yield per RPM declined 12 per cent reflecting the introduction of transborder flights by Canadian low-cost carriers and an aggressive pricing environment resulting from increased capacity in the US transborder market, as well as the weakening of the US dollar for sales denominated in US dollars. As part of its new business model to compete more effectively, Air Canada introduced a simplified fare structure progressively in 2004 consistent with Air Canada's domestic fare strategy. Excluding Aeroplan passenger revenues, US transborder RASM was down only 1 per cent as the significant improvement in passenger load factor almost offset the yield decrease.

Atlantic revenues, including Aeroplan passenger revenues of $3 million, increased $23 million or 9 per cent. This reflected a 4 per cent increase in yield per RPM, excluding Aeroplan passenger revenues, reflecting in part growth in higher-yield business traffic. Traffic increased 4 per cent on a capacity reduction of 3 per cent resulting in a passenger load factor improvement of 4.9 percentage points over the 2004 quarter. Excluding Aeroplan passenger revenues, RASM increased 11 per cent reflecting both the yield per RPM increase and the passenger load factor improvement. Pacific revenues were up $25 million or 15 per cent and included Aeroplan passenger revenues of $2 million in the 2005 quarter. Excluding Aeroplan passenger revenues, yield per RPM increased 5 per cent over the first quarter of 2004, reflecting in part strong premium traffic due to the introduction of non-stop Toronto-Hong Kong and Toronto-Narita services. Traffic increased 8 per cent on 5 per cent increase in ASM capacity resulting in a passenger load factor improvement of 1.8 percentage points. As a result of the yield increase and, to a lesser extent, the passenger load factor improvement, RASM increased 8 per cent, excluding Aeroplan passenger revenues. South Pacific, Caribbean, Mexico and South America revenues increased $36 million or 22 per cent and included Aeroplan passenger revenues of $10 million in the 2005 quarter. Traffic increased 18 per cent on an ASM capacity increase of 14 per cent resulting in a passenger load factor improvement of

3.1 percentage points. Excluding Aeroplan passenger revenues, yield per RPM decreased 1 per cent over the first quarter of 2004 and RASM increased 3 per cent due to the passenger load factor improvement. The growth in these markets is mainly from increased capacity to traditional leisure destinations such as Cuba as well as the addition of new routes to South America such as Lima, Bogota and Caracas as well as other destinations.

Cargo Revenues

Cargo revenues, including revenues from freighter operations, increased $9 million or 7 per cent due to both an increase in the volume of cargo carried and higher yield mainly in the non-North American markets. Cargo freighter operations commenced in the domestic market in June 2004 and in the international market in November 2004 following the retirement of the Boeing 747-400 Combi aircraft.

Other Revenues

Other non-transportation revenues were down $31 million mainly as a result of the change in accounting policy for the loyalty program (Aeroplan) as described on page 7 of this MD&A. For the three months ended March 31, 2004, Aeroplan revenues from miles earned by members through the loyalty program partners amounted to $70 million and were recorded in other revenues. For the three months ended March 31, 2005, Aeroplan revenues from Miles redeemed for air travel on Air Canada and Jazz are recorded in passenger revenues. Partly offsetting the reduction from the change in accounting policy for the loyalty program is an increase in other revenues from Air Canada Vacations primarily as a result of a stronger presence in the Latin Caribbean market such as Cuba and Mexico as well as a higher unit selling price for vacation packages. In addition, higher revenues were recorded from cancellation and change fees.

As a result of the restructuring, effective September 30, 2004, the Corporation's businesses are operated through four reportable segments: transportation services, loyalty program, technical services and regional operations. In the Predecessor Company, there was one reportable segment. Refer to Note 5 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements and to page 33 of this MD&A for additional information.

COST PERFORMANCE

Impact of the Adoption of AcG 15

Effective January 1, 2005, the Corporation adopted Accounting Guideline 15 – Consolidation of Variable Interest Entities (AcG 15). Prior to the adoption of AcG 15, Air Canada entered into aircraft and engine lease transactions with a number of special purpose entities that are referred to as variable interest entities (VIEs) under AcG 15. As a result of the adoption of AcG 15 and Air Canada being the primary beneficiary of these VIEs, the Corporation consolidated leasing entities covering 51 aircraft and 22 engines previously accounted for as operating leases.

In the first quarter of 2005, the net impact of adopting AcG 15 on the Corporation's results was a pre-tax charge of $30 million ($0.34 per share, diluted). The impact of the adoption of AcG 15 was a reduction to aircraft rent expense of $28 million, an increase to depreciation expense of $25 million, an increase to net interest expense of $24 million, a foreign exchange loss of $6 million and non-controlling interest of $3 million compared to financial results had AcG 15 not been effective.

The adoption of AcG 15 and the consolidation of the variable interest entities (VIEs) does not alter the underlying contractual arrangements between Air Canada, as lessee, and its lessors, nor the cash payments from Air Canada to the lessors. Over the life of the lease, the accounting expense is consistent between an operating lease and an aircraft leasing entity consolidated under AcG 15. However, there may be timing differences in any given period between net expense recorded under an operating lease versus an aircraft leasing entity consolidated under AcG 15. The main reason for the difference is due to the fact that lease expense under operating leases is straight-lined over the term of the lease whereas the interest expense under the debt obligation in the variable interest entities is based on the effective interest rate method. The effective interest rate method results in interest expense being recorded proportionate to the amount of the outstanding debt, which declines over time. In addition, foreign currency adjustments are recorded on the outstanding debt obligations of the VIEs; changes in foreign exchange rates are straight-lined over the term of the lease under operating lease accounting.

Refer to Note 1 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements or page 36 of this MD&A for additional information on the adoption of AcG 15.

Operating Expenses

In the first quarter of 2005, total operating expenses decreased $79 million or 3 per cent compared to the first quarter of 2004 in spite of an increase in fuel expense of $77 million or 23 per cent. Unit cost decreased 2 per cent from the 2004 level (excluding fuel expense, unit cost declined 6 per cent). Excluding fuel expense, operating expenses decreased $156 million or 8 percent from the first quarter of 2004.

Salaries and wage expense totaled $469 million in the first quarter of 2005, a decrease of $25 million or 5 per cent from the first quarter of 2004. This mainly reflected a reduction of an average of 1,362 full-time equivalent (FTE) employees or 4 per cent from the first quarter of 2004 as well as salary reductions for unionized and non-unionized labour groups. This decrease was partly offset by the expense of $12 million relating to an employee profit sharing program. No expenses related to this program were recorded in 2004. Salaries and wages expense per ASM was reduced 3 per cent from the first quarter of 2004.

Employee benefits expense amounted to $144 million in the first quarter of 2005, a decrease of $49 million or 25 per cent from the first quarter of 2004. The decrease was largely due to lower pension expense as a result of the elimination of unamortized actuarial losses and prior service costs resulting from fresh start reporting which accounted for approximately $30 million of the decrease.

Despite an ASM capacity decrease of 2 per cent, fuel expense increased $77 million or 23 per cent reflecting record high fuel prices. The average base fuel price increase of $114 million or 35 per cent was partially offset by a reduction of $33 million due to the favourable impact of a stronger Canadian dollar versus the US dollar during the quarter. On a unit cost basis, fuel expense per ASM increased 25 per cent.

Aircraft rent expense decreased $104 million or 54 per cent. As discussed above, as a result of the adoption of AcG 15, aircraft rent expense decreased $34 million versus the same period last year. Other factors in the remaining decrease to aircraft rent expense included the impact of fair value adjustments as a result of fresh start reporting, the net reclassification of certain aircraft leases from operating to capital leases, lease re-negotiations and terminations, as well as a stronger Canadian dollar versus the US dollar for leases denominated in US dollars.

Airport and navigation fees increased $10 million or 5 per cent on a 7 per cent decrease in aircraft frequencies. Higher fees for air navigation services as a result of a 10 per cent average unit rate increase which came into effect in September 2004 and higher landing and general terminal fees, primarily at Toronto's Pearson International Airport, were the main reasons for the increase.

Aircraft maintenance, materials and supplies expense declined $9 million or 9 per cent. Most of the decline was due to decreased maintenance activities on the Canadair Regional Jets as well as the retirement of the British Aerospace Bae146, Boeing 737-200 and Boeing 747-400 fleets.

Communications and information technology expense was down $11 million or 13 per cent largely due to renegotiated contract rates for communication services for web and Global Distribution System (GDS) and for information technology services. The impact of a stronger Canadian dollar versus the US dollar was also a factor in the decrease.

Food, beverage and supplies expense decreased $1 million or 1 per cent despite an increase of 5 per cent in passenger traffic as measured by RPMs. The decrease was mainly due to the impact of cost reduction initiatives and renegotiated contract rates.

Depreciation, amortization and obsolescence expense increased $25 million or 26 per cent. As discussed above, as a result of the adoption of AcG 15, depreciation expense increased $25 million. Amortization of intangible assets amounted to $26 million compared to $13 million in the same period last year, reflecting the impact of fresh start on the amortization of intangible assets. Amortization of intangible assets prior to fresh start related mainly to the systems development projects. Partially offsetting this increase is lower depreciation expense as a result of certain fair value adjustments and extending the useful lives on buildings.

Commission expense was down $15 million or 19 per cent on passenger and cargo revenue growth of 5 per cent. In the first quarter of 2005, the Corporation recorded a favorable adjustment of $11 million relating to changes in estimates on commission expense on corporate contracts. Lower international commission rates as well as the impact of a new commission structure introduced in July 2004 for web and GDS bookings more than offset the volume-related increase.

The other operating expense category increased $23 million or 6 per cent largely as a result of higher Aeroplan non-air redemption expenses, increased expenses relating to a higher volume and an increase in the cost of tour packages by Air Canada Vacations as well as other factors.

Non-Operating Expense

Non-operating expense amounted to $66 million in the first quarter of 2005, a $23 million increase from the first quarter of 2004. Net interest expense amounted to $60 million, an increase of $17 million from the 2004 quarter. As discussed above, as a result of the adoption of AcG 15, interest expense increased $24 million. Also contributing to the increase is interest expense relating to the ACE preferred shares as well as to the GE Exit Facility, partially offset by higher interest income and the capitalization of interest. In the first quarter of 2004, Air Canada did not record interest expense on unsecured debt subject to compromise.

Foreign Exchange Gains

Losses from foreign exchange on long-term monetary items amounted to $15 million in the first quarter of 2005 attributable to a weaker Canadian dollar versus the US dollar at March 31, 2005 compared to December 31, 2004. The foreign exchange losses recorded in the 2005 quarter included $7 million related to capital lease obligations and $6 million resulting from the adoption of AcG 15. This compared to foreign exchange gains on non-compromised long-term monetary items of $17 million in the first quarter of 2004.

Future Income Taxes

Recovery of income taxes amounted to $14 million versus a provision of $1 million in the same period last year. The Corporation has recorded a future income tax asset of $17 million as at March 31, 2005. This asset is expected to reverse in subsequent quarters in 2005.

BALANCE SHEET ANALYSIS

ACE Aviation Holdings Inc.
Consolidated Statement of Financial Position

Unaudited ($ millions)	March 31, 2005	December 31, 2004
ASSETS		
Current		
Cash, cash equivalents and short-term investments	1,785	1,632
Other current assets	1,080	1,063
	2,865	2,695
Property and equipment	5,056	3,696
Deferred charges	125	167
Intangible Assets	2,678	2,691
Other assets	246	137
	10,970	9,386
LIABILITIES		
Current liabilities	2,790	2,491
Long-term debt and capital lease obligations	3,499	2,328
Convertible preferred shares	135	132
Future income taxes	243	243
Pension and other benefit liabilities	2,336	2,344
Non-controlling interest	192	-
Other long-term liabilities	1,506	1,645
	10,701	9,183
SHAREHOLDERS' EQUITY	269	203
	10,970	9,386

As a result of the adoption of AcG 15 effective January 1, 2005, the Corporation consolidated the financial statements of certain aircraft and engine leasing entities and fuel facilities corporations. As at March 31, 2005, additional property and equipment of $1,392 million, long-term debt, including current portion, of $1,255 million, other assets of $105 million, and non-controlling interest of $192 million are consolidated under AcG 15. The impact of the adoption of this guideline on the Consolidated Statement of Financial Position is described in further detail under the section entitled “Accounting Policies” on page 35 of this MD&A.

Share Capital and Other Equity

As at March 31, 2005, the issued and outstanding common shares of ACE, along with other equity instruments, were as follows:

	Authorized (000)	March 31, 2005	December 31, 2004
		Outstanding (000)	
Issued and outstanding common shares			
Class A variable voting shares	unlimited	72,195	74,813
Class B voting shares	unlimited	11,431	8,813
Shares held in escrow		5,189	5,189
Total issued and outstanding common shares		88,815	88,815

	March 31, 2005	December 31, 2004
Issued and outstanding		
Convertible preferred shares	9,259	9,259
Stock options	2,960	3,028
	12,219	12,287

On April 6, 2005, ACE completed the public offering of an aggregate of 11,350,000 Class A Variable Voting Shares and Class B Voting Shares (collectively the "Shares") at a price of $37.00 per share for gross proceeds of approximately $420 million, and $300 million of 4.25 per cent Convertible Senior Notes due 2035. Aggregate gross proceeds were approximately $720 million with ACE receiving net proceeds of approximately $693 million, after commissions and expenses. In addition, ACE granted the underwriters over-allotment options to purchase up to an additional 10 per cent of each of the offerings, until May 5, 2005. ACE used approximately $557 million of the aggregate net cash proceeds of the offerings to repay all of its outstanding debt under the exit credit facility with General Electric Capital Corporation (GECC), including $17 million for early payment and legal fees. The Corporation expects to record a charge of $29 million for this transaction in the second quarter of 2005, including $12 million for the write-off of deferred financing charges.

On April 11, 2005, the Corporation announced that it had received written notice from the underwriters that they had elected to exercise in full their over-allotment options to purchase an additional 1,135,000 Class A Variable Voting Shares at $37.00 per share and $30 million of 4.25 per cent convertible senior notes due 2035. On April 13, 2005, the aggregate gross proceeds approximately $72 million were received from the exercise of the over-allotment options. Proceeds will be used for general corporate purposes and have brought the aggregate

gross proceeds of the ACE financial offerings to approximately $792 million ($762 million net of commissions and expenses).

Debt Obligations

As at March 31, 2005, ACE had long-term debt and capital lease obligations of $3.8 billion, including current portion, with a cash, cash equivalents and short-term investments of $1.8 billion. These long-term debt obligations included $1.3 billion recorded as a result of the adoption of AcG 15. Refer to Note 3 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements and to the table on page 29 of this MD&A for additional information on ACE's principal repayment requirements as at March 31, 2005 on long-term debt, capital lease obligations, and aircraft, engine and fuel facility debt consolidated as variable interest entities (VIEs) under AcG 15.

Lease Obligations

As a result of the adoption of AcG 15, the Corporation has consolidated leasing entities covering aircraft and engine leasing agreements previously accounted for as operating leases. The consolidation of these aircraft leasing agreements impacts the operating lease commitments previously disclosed in the 2004 Annual Consolidated Financial Statements of ACE. Future minimum lease payments under existing operating leases of aircraft, excluding leases accounted for as VIEs, amounted to $2.2 billion as at March 31, 2005 compared to $3.0 billion at December 31, 2004. Refer to Note 6 of the Interim Unaudited First Quarter 2005 Consolidated Financial Statements and to the table on page 29 of this MD&A for additional information on ACE's future minimum lease payments under existing operating leases.

Guarantees

As a result of the adoption of AcG 15 as further described in Note 7 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements, the Corporation no longer has any residual value guarantees under any of its aircraft leasing agreements accounted for as operating leases. The entire debt balance under these leasing agreements is now on the consolidated balance sheet of the Corporation, and as a result the residual value support previously disclosed in the 2004 Annual Consolidated Financial Statements of ACE is no longer a guarantee of the Corporation.

FINANCIAL MANAGEMENT

ACE Aviation Holdings Inc.
Consolidated Statement of Cash Flow

Unaudited (in millions of Canadian dollars)	Successor Company ACE Three months ended March 31, 2005	Predecessor Company Air Canada Three months ended March 31, 2004
Cash flows from (used for)		
Operating		
Loss for the period	(77)	(304)
Adjustments to reconcile to net cash provided by operations		
Reorganization and restructuring items	-	109
Depreciation, amortization and obsolescence	120	95
Loss on sale of and provisions on assets	-	3
Foreign exchange	15	(17)
Future income taxes	(17)	(2)
Employee future benefit funding (more than) less than expense	(8)	60
Decrease (Increase) in accounts receivable	(91)	(54)
Decrease (increase) in spare parts, materials and supplies	14	(3)
Increase in accounts payable and accrued liabilities	100	62
Increase in advance ticket sales, net of restricted cash	219	140
Aircraft lease payments in excess of rent expense	(4)	(44)
Other	43	18
	314	63
Financing		
GE DIP financing	-	300
Credit facility borrowings	-	80
Reduction of long-term debt and capital lease obligations	(140)	(214)
	(140)	166
Investing		
Short-term investments	(675)	186
Additions to capital assets	(38)	(36)
Proceeds from sale of assets	37	1
Cash collaterization of letters of credit	(20)	-
	(696)	151
Increase (decrease) in cash and cash equivalents	(522)	380
Cash and cash equivalents, beginning of period	1,481	1,101
Cash and cash equivalents, end of period	959	1,481
Cash payments of interest	38	35
Cash payments of income taxes	4	-

Cash and cash equivalents exclude short-term investments of $826 million as at March 31, 2005 ($151 million as at December 31, 2004).

Cash Flows from (used for) Operations

The first quarter of 2005 cash flows from operations amounted to $314 million. This compared to cash flows from operations of $63 million in the first quarter of 2004, an improvement of $251 million. Improved operating results contributed significantly to the cash flow improvement. Further components of the cash flow change are described below:

- Advance ticket sales was a source of funds of $219 million partially offset by a use of funds of $91 million from an increase in accounts receivable, largely reflecting the seasonal increase in passenger sales into the second quarter (2004 - $140 million source and $54 million use respectively).

- Accounts payable and accrued liabilities was a source of funds of $100 million in the first quarter of 2005. This compared to a source of funds of $62 million in the first quarter of 2004, an increase of $38 million.

- Aircraft lease payments in excess of rent expense was a use of funds of $4 million in the first quarter of 2005 versus a use of funds of $44 million in the first quarter of 2004, an improvement of $40 million. In the first quarter of 2005, as a result of the adoption of AcG 15 on January 1, 2005 and the consolidation of certain lease structures previously accounted for as operating leases, payments of $56 million previously recorded in "aircraft lease payments in excess of rent expense" were reclassified under cash flows used for financing activities.

- Employee future benefit funding was a use of funds of $8 million in the first quarter of 2005, an increase of $68 million from the first quarter of 2004. This increase was mainly as a result of pension funding of $61 million in the quarter following the implementation of the Plan and the adoption of the Air Canada Pension Plan Solvency Deficiency Funding Regulations, as well as the application of fresh start reporting on September 30, 2004. Refer to Note 15 to the 2004 Annual Consolidated Financial Statements for additional information.

- the change in spare parts, materials and supplies was a source of funds of $14 million in the first quarter of 2005 versus a use of funds of $3 million in the first quarter of 2004, an improvement of $17 million. This change was largely due to lower fuel inventories in the first quarter of 2005.

- other cash from operations was $43 million in the first quarter of 2005 versus a source of funds of $18 million in the first quarter of 2004. A decrease in prepaid expenses related to vacation packages at Air Canada Vacations accounted for approximately $25 million of the source of funds.

Cash Flows used for Financing Activities

In the first quarter of 2005, reduction of long-term debt and capital lease obligations amounted to $140 million. As a result of the adoption of AcG 15 on January 1, 2005, payments of $56 million previously recorded in "aircraft lease in excess of rent expense" under cash flows from (used for) operating activities were reclassified under cash flows used for financing activities. In the first quarter of 2005, proceeds of $29 million resulting from the sale of one Boeing 747-400 aircraft were used to repay the General Electric Capital Corporation (GECC) Limited Recourse Loan as disclosed in Note 3 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements. In addition, repayments of $32 million were made on capital lease obligations and repayments of $18 million were made on the credit facility with Amex Bank of Canada (Amex).

Cash Flows used for Investing Activities

In the first quarter of 2005, cash used for the purchase of short-term investments amounted to $675 million. Short-term investments with original maturities greater than ninety days were previously included in cash and cash equivalents. Short-term investments have original maturities over 90 days, but not more than one year. These investments can be readily converted to cash and are with institutions that have high credit ratings.

In the first quarter of 2005, additions to capital assets amounted to $38 million and related mainly to spare engines and aircraft betterments, system developments costs, ground equipment and facilities. In addition, proceeds from sale of assets totaled $37 million of which $29 million related to the sale of one Boeing 747-400 aircraft. These proceeds were used to repay the GECC Limited Recourse Loan.

Liquidity

As at March 31, 2005, ACE had cash, cash equivalents and short-term investments of $1.8 billion and positive working capital of $75 million. As at March 31, 2004, Air Canada had cash and cash equivalents of $864 million and a working capital deficiency of $669 million.

On April 6, 2005, Air Canada entered into a senior secured syndicated revolving credit facility in an aggregate amount of up to $300 million or the US dollar equivalent. The revolving credit facility has a two-year term which can be extended at Air Canada's option for additional one-year periods on each anniversary of closing, subject to prior approval by a majority of the lenders. Included in the aggregate amount is a swing line facility of up to $20 million provided for cash management and working capital purposes. The amount available to be drawn by Air Canada under the revolving credit facility is limited to the lesser of $300 million and the amount of a borrowing base determined with reference to certain eligible accounts receivable of Air Canada and certain eligible owned and leased real property of Air Canada. The credit facility is secured by a first priority security interest and hypothec over the present and after-acquired property of Air Canada, subject to certain exclusions and permitted encumbrances. The revolving credit facility provides Air Canada with a certain amount of flexibility to dispose of, finance and otherwise deal with its assets and property other than accounts receivable and certain leased real property of Air Canada.

As at May 11, 2005, ACE's consolidated cash balance, measured on the basis of unrestricted cash in its bank accounts, and short-term investments amounted to approximately $2.1 billion.

The Corporation is expected to have positive cash flows from operations in 2005 and, as described above, has a senior secured syndicated revolving credit facility in an aggregate amount of up to $300 million or the US dollar equivalent. Debt repayment obligations in the future are expected to be met from cash flows from operations. Future aircraft deliveries have committed financing from the manufacturers or a third party.

The Corporation could potentially realize additional funding through the monetization of or sale of interests in certain divisions or subsidiaries.

Summary of Principal Repayment and Future Minimum Lease Payment Requirements as at March 31, 2005

The table below summarizes ACE's principal repayment requirements on long-term debt, capital lease obligations, and aircraft, engine and fuel facility debt consolidated as variable interest entities under AcG 15 through to 2009, as well as the Corporation's future minimum lease payments under existing operating leases as at March 31, 2005, as further described in Notes 3 and 6 to the Interim Unaudited First Quarter 2005 Consolidated Financial Statements.

($ millions) (1)	Remainder of 2005	2006	2007	2008	2009
Long-Term Debt and Capital Lease Obligations (Note 3)					
Long-term debt principal obligations excluding GECC Exit Financing	54	32	32	51	28
Capital lease principal obligations	138	147	182	179	88
Debt consolidated under AcG 15	44	74	118	117	57
Total excluding GECC Exit Financing	236	253	332	347	173
GECC Exit Financing	-	-	96	128	128
Total Long-Term Debt and Capital Lease Obligations	236	253	428	475	301
Operating Leases (excluding leases accounted for as VIEs under AcG 15)					
-Future minimum lease payments under existing operating leases of aircraft (Note 6)	292	370	320	257	210
-Future minimum lease payments under existing leases for other property	71	57	48	46	33
	363	427	368	303	243

Long-term debt and capital lease obligations as at March 31, 2005 combined with the estimated present value of committed future aircraft lease payments for the period to the end of the lease term and estimated future purchase options, net of cash and short term investments, amounted to approximately $4 billion compared to approximately $12 billion at December 31, 2002, prior to filing for creditor protection under CCAA.

Projected Aircraft Expenditures, Net of Aircraft Financing

The table below provides projections for aircraft expenditures for firm Bombardier and Embraer aircraft orders, net of aircraft financing, over the next five years:

($ millions) (1)	Remainder of 2005	2006	2007	2008	2009
Projected committed capital expenditures (1)					
Projected aircraft expenditures – Bombardier and Embraer aircraft	949	529	767	30	0
Projected aircraft financing	(879)	(450)	(697)	(30)	0
Projected committed aircraft expenditures, net of aircraft financing	70	79	70	0	0

(1) US dollar amounts are converted using the March 31, 2005 noon day rate of CDN$1.2096. Projected aircraft expenditures are based on escalated aircraft delivery prices.

As disclosed in ACE's 2004 Management's Discussion and Analysis of Results, in 2004, Air Canada signed definitive purchase agreements with Empresa Brasileira de Aeronautica S.A. (Embraer) and Bombardier Inc. (Bombardier). The agreement with Embraer covers firm orders for 45 Embraer 190 series aircraft as well as 15 Embraer 175 series aircraft. The purchase agreement also contains rights to exercise options for up to 60 additional Embraer 190 series aircraft as well as providing for conversion rights to other Embraer models. Deliveries of the Embraer 175 series aircraft are scheduled to begin in July 2005, with the Embraer 190 series deliveries scheduled to commence in November 2005. The agreement with Bombardier covers firm orders for 15 Bombardier CRJ700 Series 705 aircraft and 30 Bombardier CRJ200 aircraft of which 15 of the Bombardier CRJ200 may be cancelled without penalty. The purchase agreement also contains options for an additional 45 aircraft. Deliveries of the 50-seat Bombardier CRJ200 firm aircraft orders have been completed, with the 75-seat CRJ700 Series 705 deliveries scheduled to begin in May 2005. The Corporation has received financing commitments from the manufacturers and a third party covering all firm orders.

On April 24, 2005, Air Canada and The Boeing Company (Boeing) signed an agreement for a wide-body fleet renewal plan that includes firm orders for 18 Boeing 777 aircraft, plus purchase rights for an additional 18 aircraft, in a yet-to-be-determined mix of the Boeing 777 family's newest models: the Boeing 777-300ER aircraft, the Boeing 777-200LR Worldliners, and the Boeing 777 Freighter aircraft. Air Canada's Boeing 777 deliveries are scheduled to begin with the arrival of three Boeing 777-300ER aircraft in 2006. The renewal plan also includes firm orders for 14 new Boeing 787 Dreamliners, plus options and purchase rights for an additional 46 aircraft. Air Canada's first Boeing 787 is scheduled for delivery in 2010. The order is subject to several conditions including final documentation. The Corporation expects the agreement to be finalized by mid-year 2005. Air Canada will receive a financing commitment for the firm aircraft deliveries from the manufacturer.

QUARTERLY RESULTS

The table below describes quarterly financial results of Air Canada for the last three quarters of 2003 and the first three quarters of 2004 and the financial results of ACE for the fourth quarter of 2004 and the first quarter of 2005 as well as major operating statistics:

Quarterly Financial Data – Condensed Consolidated

$ millions (except per share figures)	Predecessor Company Air Canada						Successor Company ACE	
	---------------2003---------------			-------------------------2004-------------------------				2005
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Passenger revenues	1,597	1,901	1,615	1,661	1,844	2,123	1,681	1,739
Cargo revenues	122	122	131	126	137	142	151	135
Other revenues	235	207	231	334	240	231	230	303
Operating revenues	1,954	2,230	1,977	2,121	2,221	2,496	2,062	2,177
Operating expenses	2,225	2,212	2,054	2,266	2,199	2,253	2,065	2,187
Operating income (loss) before reorganization and restructuring items	(271)	18	(77)	(145)	22	243	(3)	(10)
Reorganization and restructuring items	(216)	(274)	(560)	(132)	(426)	(313)	-	-
Non-operating income (expense)	(68)	(21)	(132)	(43)	(72)	(133)	(67)	(66)
Loss before foreign exchange on non-compromised long-term monetary items and income taxes	(555)	(277)	(769)	(320)	(476)	(203)	(70)	(76)
FX gain (loss) on non-compromised long-term monetary items	(5)	17	(7)	17	(34)	123	98	(15)
Income (loss) before income taxes	(560)	(260)	(776)	(303)	(510)	(80)	28	(91)
Recovery of (provision for) income taxes	(6)	(3)	8	(1)	-	(1)	(13)	14
Net income (loss)	(566)	(263)	(768)	(304)	(510)	(81)	15	(77)
Earnings (loss) (1) Per share - basic and diluted	(4.70)	(2.18)	(6.39)	(2.53)	(4.24)	(0.67)	0.17	(0.87)
Revenue passenger miles (millions)	9,073	11,617	9,289	10,057	10,836	12,853	9,681	10,586
Available seat miles (millions)	12,579	15,156	13,115	13,797	13,931	15,993	12,815	13,566
Passenger load factor (%)	72.1	76.6	70.8	72.9	77.8	80.4	75.5	78.0
Operating expense per available seat mile (CASM) (cents)	17.7	14.6	15.7	16.4	15.8	14.1	16.1	16.1
Operating expense per available seat mile excl. fuel expense (cents)	15.4	12.5	13.5	14.0	13.1	11.2	12.7	13.1

(1) Pursuant to the Plan as further described in Note 2 to the 2004 Annual Consolidated Financial Statements, all issued and outstanding options of Air Canada and warrants were cancelled without payment or consideration. In addition, a new share capital was established under ACE, as further described in Notes 19 and 20 to the 2004 Annual Consolidated Financial Statements.

SEGMENT INFORMATION

As a result of the corporate restructuring, the Corporation's businesses are operated through four reporting segments: transportation services, loyalty program, technical services, and regional operations. In the Predecessor Company, Technical Services was a cost centre within Air Canada and discrete financial information is not available. A capacity purchase agreement between Air Canada and Jazz Limited Partnership (Jazz) came into effect on September 30, 2004. The Regional Operations segment information in the Successor Company is not comparable to that of the Predecessor Company as a result of this new agreement.

As described in Note 4 to the 2004 Annual Consolidated Financial Statements, the Corporation changed the accounting policy as of September 30, 2004 for the recognition of its revenues relating to the Loyalty Program. As a result, Loyalty Program results are not directly comparable to prior periods.

Segment financial information has been prepared consistent with how financial information is produced internally for the purposes of making operating decisions. Segments negotiate transactions with each other as if they were unrelated parties. A reconciliation of the total amounts reported by each segment to the applicable amounts in the consolidated financial statements follows:

Successor Company
Three months ended March 31, 2005

($ Millions)	Transportation Services (1)	Loyalty Program (2)	Technical Services	Regional Operations (3)	Inter-Segment Elimination	ACE Consolidated Total
Passenger revenue	1,739	-	-	-	-	1,739
Cargo revenue	135	-	-	-	-	135
Other revenue	93	169	39	2	-	303
External revenue	1,967	169	39	2	-	2,177
Inter-segment revenue	50	3	141	211	(405)	-
Total revenue	2,017	172	180	213	(405)	2,177
Operating expenses, before the following:	1,996	149	149	178	(405)	2,067
Amortization of capital assets	105	2	8	5	-	120
Total operating expenses	2,101	151	157	183	(405)	2,187
Operating income (loss)	(84)	21	23	30	-	(10)
Net interest expense	(54)	-	(3)	(3)	-	(60)
Foreign exchange on long-term monetary items	(15)	-	-	-	-	(15)
Income tax expense	14	-	-	-	-	14
Other non-operating items	(6)	-	-	-	-	(6)
	(61)	-	(3)	(3)	-	(67)
Segment Results	(145)	21	20	27	-	(77)
Total Assets	10,053	234	308	375	-	10,970
Capital Expenditures	32	2	-	4	-	38

(1) Includes revenues and costs for Air Canada Mainline operations, Jazz transportation revenues and fees to Air Canada Mainline for Jazz operations under the CPA as well as Air Canada Cargo Limited Partnership (doing business as Air Canada Cargo), Destina.ca Inc., AC Online Limited Partnership, ACGHS Limited Partnership (doing business as Air Canada Ground Handling), Touram Inc. (doing business as Air Canada Vacations) and ACE. Inter-segment revenue includes management fees and cost and operating services charged to other segments. Foreign exchange on long-term monetary items is included by management in the Transportation Services segment. Interest expense in the Transportation Services segment represent interest on third party debt. Interest expense included in other segments represent interest on inter-company and third party debt. Management reflects all income taxes within the Transportation Services segment including any income taxes that may be applicable to amounts earned in the other segments because the activities of the other segments are carried out as limited partnerships and the income is taxable in one of the entities included in Transportation Services.

(2) Other revenue of $169 million includes revenue recognized on redemption of points accumulated through both air and third party contracts. Inter-segment revenue of $3 million represents the management fee charged to Air Canada by Aeroplan relating to the redemption of points accumulated prior to January 1, 2002. The value of points earned through air travel, charged by Aeroplan to Air Canada, is recorded in Aeroplan's accounts as deferred revenues.

(3) Includes Jazz operations under the CPA effective September 30, 2004.

ACCOUNTING POLICIES

The Interim Unaudited Consolidated First Quarter 2005 Financial Statements for the Successor Company are based on the accounting policies consistent with those disclosed in Note 4 to the 2004 Annual Consolidated Financial Statements of ACE with the exception of the adoption of the accounting policies as further described below under “New Policies”: The accounting policies of the Successor Company were consistent with those of the Predecessor Company, with the exception of the fair value adjustments applied under fresh start reporting and the accounting policies noted below.

Property and Equipment

On the application of fresh start accounting effective September 30, 2004, the estimated useful lives of buildings was extended to periods not exceeding 50 years. The Predecessor Company depreciated buildings over their useful lives not exceeding 30 years.

Air Transportation Revenues and Loyalty Program

As a result of the application of fresh start reporting, the outstanding loyalty program mileage credits ("Miles") were adjusted to reflect the estimated fair value of Miles to be redeemed in the future. As a consequence of this fair value adjustment and the evolving nature of the Aeroplan loyalty program, the Successor Company changed the accounting policy as of September 30, 2004 for the recognition of its obligations relating to the loyalty program. The Predecessor Company recognized the obligation related to Miles earned through transportation services based on the incremental cost of providing future transportation services. On a prospective basis from the date of fresh start reporting, Miles earned by members through transportation services provided by the Corporation and the transportation services are treated as multiple elements. Miles are recorded at fair values with the residual allocated to transportation services. Consistent with the accounting policy of the Predecessor Company, the proceeds from the sale of Miles to loyalty program partners are deferred.

Effective September 30, 2004, Miles redeemed for travel on Air Canada and Jazz are included in passenger revenue and Miles redeemed for other than travel are included in other revenues. Under the previous accounting policy in the Predecessor Company, Aeroplan redemption revenues from Miles earned by members through loyalty program partners were included in other revenues. These revenues amounted to $70 million for the three months ended March 31, 2004. For the three months ended March 31, 2005, Aeroplan revenues from Miles redeemed for air travel on Air Canada and Jazz amounted to $101 million of which $65 million

related to Miles earned by members through loyalty program partners and are included in passenger revenues.

Non-transportation Revenues

Non-transportation revenue includes certain loyalty program revenues, as described in Loyalty Program, as well as revenues from technical services maintenance and other airline related services. The Predecessor Company recorded all loyalty program revenues under non-transportation revenues prior to September 30, 2004.

Segment Reporting

As a result of the corporate restructuring, the segment reporting structure for the Successor Company reflects four reportable segments consistent with the current management of the business: transportation services, loyalty program, technical services, and regional operations. In the Predecessor Company, there was one reportable segment.

New Policies

Consolidation of Variable Interest Entities

Accounting Guideline 15 – Consolidation of Variable Interest Entities (AcG 15) is effective for periods beginning on or after November 1, 2004; as a result, ACE adopted this standard effective January 1, 2005. AcG 15 relates to the application of consolidation principles to certain entities that are subject to control on a basis other than ownership of voting interests. The purpose of AcG 15 is to provide guidance for determining when an enterprise includes the assets, liabilities and results of activities of such an entity (a "variable interest entity") in its consolidated financial statements. Restatement of comparative financial information is not required under AcG 15.

An entity falls under the guidance in AcG 15 and is classified a variable interest entity ("VIE") if it has (1) equity that is insufficient to permit the entity to finance its activities without additional subordinated financial support from other parties; or (2) equity investors that cannot make significant decisions about the entity's operations, or that do not absorb the expected losses or receive the expected returns of the entity. A VIE is consolidated by its primary beneficiary, which is the party involved with the VIE that will absorb a majority of the expected losses or will receive the majority of the expected residual returns or both, as a result of ownership, contractual or other financial interests in the VIE.

Aircraft and Engine Leasing Transactions

Prior to the adoption of AcG 15, Air Canada entered into aircraft and engine lease transactions with a number of special purpose entities that are referred to as VIEs under AcG 15. As a result of the adoption of AcG 15 and Air Canada being the primary beneficiary of these VIEs, the Corporation consolidated in its financial statements leasing entities covering 51 aircraft and 22 engines previously accounted for as operating leases. The following adjustments to the consolidated statement of financial position as at January 1, 2005 result from consolidating these lease structures on initial adoption of AcG 15:

$ Millions	Assets	Liabilities and Shareholders' Equity
Increase to property and equipment	1,304	
Decrease to deferred charges	(45)	
Decrease to intangible assets	(6)	
Increase to other assets	113	
Increase to current portion of long-term debt		77
Increase to long-term debt		1,173
Increase to non-controlling interest		181
Decrease to other long-term liabilities		(155)
Increase to retained earnings as result of the cumulative effect of this change in accounting policy		90
	1,366	1,366

The increase to other assets represents restricted cash held in the VIEs and the fair value of a currency swap arrangement of $7 million in favour of the Corporation, taking into account foreign exchange rates in effect as at December 31, 2004. This currency swap was put in place on the inception of the leases for 11 Canadair Regional Jet aircraft. This currency swap has not been designated as a hedge for accounting purposes.

Fuel Facilities Arrangements

Air Canada and Jazz participate in fuel facilities arrangements, along with other airlines to contract for fuel services at various domestic airports. The fuel facilities corporations are organizations incorporated under federal or provincial business corporations acts in order to acquire, finance and lease assets used in connection with the fuelling of aircraft and ground support equipment. The fuel facilities corporations operate on a cost recovery basis.

Under AcG 15, the Corporation is the primary beneficiary of certain of the fuel facilities corporations. On January 1, 2005 the Corporation consolidated in its financial statements three fuel facilities corporations, resulting in the following adjustments:

$ Millions	Assets	Liabilities and Shareholders' Equity
Increase to property and equipment	113	
Increase to long-term debt		51
Increase to non-controlling interest		8
Increase to other long-term liabilities		2
Increase to retained earnings as result of the cumulative effect of this change in accounting policy		52
	113	113

The remaining five fuel facilities corporations in Canada that have not been consolidated have assets recorded of approximately $103 million and debt of approximately $90 million, which is the Corporation's maximum exposure to loss without taking into consideration any cost sharing that would occur amongst the other contracting airlines and any value of the assets. The Corporation views this loss potential as remote.

Effect in Current Period

In the first quarter of 2005, the net impact on the Corporation's results of adopting AcG 15 was a pre-tax charge of $30 million ($0.34 per share, diluted). The impact of the adoption of AcG 15 was a reduction to aircraft rent expense of $28 million, an increase to depreciation expense of $25 million, an increase to net interest expense of $24 million, a foreign exchange loss of $6 million and non-controlling interest of $3 million compared to financial results prior to the adoption of AcG 15.

Prior Periods

Restatement of comparative financial information is not required by AcG 15. The cumulative effect to retained earnings on the adoption of AcG 15 as at January 1, 2005 is an increase of $142 million.

The adoption of AcG 15 and the consolidation of the variable interest entities (VIEs) does not alter the underlying contractual arrangements between Air Canada, as lessee, and its lessors, nor the cash payments from Air Canada to the lessors. Over the life of the lease, the accounting expense is consistent between an operating lease and an aircraft leasing entity consolidated under AcG 15. However, there may be timing differences in any given period between net expense recorded under an operating lease versus an aircraft leasing entity consolidated under AcG 15. The main reason for the difference is due to the fact that lease expense under operating leases is straight-lined over the term of the lease whereas the interest expense under the debt obligation in the variable interest entities is based on the effective interest rate method. The effective interest rate method results in interest expense being recorded proportionate to the amount of the outstanding debt, which declines over time. In addition, foreign currency adjustments are recorded on the outstanding debt obligations of the VIEs; changes in foreign exchange rates are straight-lined over the term of the lease under operating lease accounting.

Foreign Currency Translation of Financial Statements of Integrated Foreign Operations

The majority of the VIEs are not Canadian based entities and monetary assets and liabilities of the VIEs are denominated in foreign currencies, principally US dollars. The Corporation applies the temporal method for the translation of the financial statements of the VIEs denominated in foreign currencies. Monetary assets and liabilities of the VIEs are translated at rates of exchange in effect at the date of the consolidated statement of financial position. Non monetary items are translated at historical exchange rates. Expense items are translated at the average rate of exchange for the period, which results in substantially the same reporting currency amounts that would have resulted had the underlying transactions been translated on the dates they occurred. Depreciation of assets translated at historical exchange rates are translated at the same exchange rates as the assets to which they relate.

Asset Retirement Obligations

As a result of the consolidation of certain Fuel Facilities Corporations, the Corporation has applied the Canadian Institute of Chartered Accountants Section 3110, “Accounting for Asset Retirement Obligations”, which requires the Corporation to record an asset and related liability for the costs associated with the retirement of long-lived tangible assets when a legal liability to retire such assets exists. Under Section 3110, the fair value of a liability for an asset retirement obligation is recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying

amount of the long-lived asset and then amortized over its estimated useful life. In subsequent periods, the asset retirement obligation is adjusted for the passage of time and any changes in the amount of the underlying cash flows through charges to earnings. A gain or loss may be incurred upon settlement of the liability.

Under the terms of its land leases, the Fuel Facilities Corporations have the obligation to restore the land to vacant condition at the end of the lease and to rectify any environmental damage for which is it responsible. If it was found that the Fuel Facilities Corporations had to contribute to any remediation costs, each contracting airline would share pro rata, based on system usage, in the costs. For Fuel Facilities Corporations that are consolidated under AcG 15, the Corporation has recorded an obligation of $2 million ($12 million undiscounted) representing the present value of the estimated decommissioning and remediation obligations at the end of the lease, with lease term expiry dates ranging from 2032 to 2039. This estimate is based on numerous assumptions including the overall cost of decommissioning and remediation and the selection of alternative decommissioning and remediation approaches.

MATERIAL CHANGES

There have been no material changes in debt and lease obligations with the exception of the impact of the adoption of AcG 15 and the transactions completed in April 2005 as described herein. In addition, there have been no material changes in critical accounting estimates, tax, risk management and outlook from the disclosures included in ACE’s 2004 Management’s Discussion and Analysis of Results dated March 18, 2005.

RISK FACTORS

For a detailed description of the possible risk factors associated with ACE and/or its subsidiaries, refer to the section entitled “Risk Factors” in ACE’s 2004 Management’s Discussion and Analysis of Results dated March 18, 2005. There have been no material changes to the risk factors disclosed at that time.