



**2013**  
**Annual Information Form**

**March 28, 2014**

## TABLE OF CONTENTS

EXPLANATORY NOTES.....	- 2 -
CORPORATE STRUCTURE .....	- 3 -
INTERCORPORATE RELATIONSHIP .....	- 4 -
THE BUSINESS.....	- 5 -
STRATEGY .....	- 6 -
ROUTES AND SCHEDULES .....	- 6 -
AIR CANADA'S ENVIRONMENTAL OBJECTIVES .....	- 10 -
FINANCIAL OVERVIEW .....	- 10 -
SIGNIFICANT FINANCING TRANSACTIONS .....	- 12 -
RATINGS.....	- 13 -
PENSION PLAN ARRANGEMENTS.....	- 14 -
FOREIGN EXCHANGE.....	- 14 -
AIRCRAFT FUEL .....	- 14 -
AIRCRAFT FLEET .....	- 14 -
EMPLOYEES AND ARRANGEMENTS WITH UNIONS.....	- 15 -
FACILITIES .....	- 16 -
TRADEMARKS .....	- 17 -
REGULATORY ENVIRONMENT .....	- 17 -
INDUSTRY OVERVIEW AND COMPETITIVE ENVIRONMENT.....	- 23 -
RISK FACTORS.....	- 26 -
MARKET FOR SECURITIES .....	- 27 -
TRANSFER AGENT AND REGISTRAR .....	- 27 -
DIVIDEND RECORD .....	- 27 -
DESCRIPTION OF CAPITAL STRUCTURE .....	- 28 -
DIRECTORS AND OFFICERS .....	- 32 -
AUDIT, FINANCE AND RISK COMMITTEE .....	- 36 -
INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS.....	- 38 -
LEGAL PROCEEDINGS .....	- 38 -
MATERIAL CONTRACTS .....	- 38 -
EXPERTS .....	- 38 -
ADDITIONAL INFORMATION.....	- 39 -
GLOSSARY OF TERMS .....	- 40 -
SCHEDULE A: CHARTER OF THE AUDIT, FINANCE AND RISK COMMITTEE .....	- 43 -

## EXPLANATORY NOTES

The information in this Annual Information Form ("AIF") is stated as at December 31, 2013, unless otherwise indicated.

**Air Canada and the Corporation** – References herein to Air Canada and references to the "Corporation" include references, as the context may require, to Air Canada and its subsidiaries collectively, Air Canada and one or more of its subsidiaries, one or more of Air Canada's subsidiaries, or Air Canada itself.

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

**Defined Terms** – For an explanation of the capitalized terms and expressions and certain defined terms, refer to the section entitled "Glossary of Terms" at the end of this AIF.

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

**Statistical Information** – Market data and certain industry forecasts used throughout this AIF were obtained from internal surveys, market research, publicly available information and industry publications. Industry publications generally state that the information contained therein has been obtained from sources believed to be reliable, but that the accuracy and completeness of such information is not guaranteed. Similarly, internal surveys, industry forecasts, market research and other publicly available information, while believed to be reliable, have not been independently verified, and the Corporation does not make any representation as to the accuracy of such information.

**Caution regarding forward-looking statements** – Air Canada's public communications may include forward-looking statements within the meaning of applicable securities laws. Such statements may be included in this AIF and may be included in other communications, including filings with regulatory authorities and securities regulators. Forward-looking statements may be 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. 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, including those described herein and are subject to important risks and uncertainties. Forward-looking 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, energy prices, currency exchange and interest rates, competition, employee and labour relations, pension issues, war, terrorist acts, epidemic diseases, environmental factors (including weather systems and other natural phenomena and factors arising from man-made sources), 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 Air Canada's public disclosure file available at [www.sedar.com](http://www.sedar.com) and, in particular, those identified in section 18 "Risk Factors" of Air Canada's 2013 Management's Discussion and Analysis of Results of Operations and Financial Condition dated February 12, 2014. The forward-looking statements contained in this AIF represent Air Canada's expectations as of the date of this AIF (or as of the date they are otherwise stated to be made), and are subject to change after such date. However, Air Canada 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.

Assumptions were made by Air Canada in preparing and making forward-looking statements. As part of its assumptions, Air Canada assumes Canadian GDP growth of 2.0% to 3.0% for 2014. In addition, Air Canada expects that the Canadian dollar will trade, on average, at C\$1.10 per U.S. dollar in the first quarter of 2014 and the full year 2014 and that the price of jet fuel will average 93 cents per litre for the first quarter of 2014 and 92 cents per litre for the full year 2014.

## CORPORATE STRUCTURE

### Name, Address and Incorporation

Air Canada was continued under the *Canada Business Corporations Act* ("CBCA") on August 25, 1988. Air Canada acquired Canadian Airlines International Ltd. ("Canadian Airlines") on July 6, 2000 and completed a corporate amalgamation with Canadian Airlines effective January 1, 2001, with the amalgamated entity being known as Air Canada. Pursuant to a consolidated plan of reorganization, compromise and arrangement of Air Canada and certain of its subsidiaries made pursuant to the *Companies Creditors Arrangement Act* ("CCAA"), ACE Aviation Holdings Inc. ("ACE") became the parent holding company of the reorganized Air Canada on September 30, 2004.

On November 24, 2006, ACE and Air Canada completed an initial public offering and secondary offering of an aggregate 25 million Class A variable voting shares of Air Canada (the "Variable Voting Shares") and Class B voting shares of Air Canada (the "Voting Shares", together with the Variable Voting Shares, the "Shares") (the "Initial Public Offering"). The Shares trade on the Toronto Stock Exchange ("TSX") under the symbol AC.A for the Variable Voting Shares and the symbol AC.B for the Voting Shares. Through the Initial Public Offering, Air Canada sold an aggregate of 9,523,810 Variable Voting Shares and Voting Shares for gross proceeds of \$200 million to be used for general corporate purposes, including the partial funding of its fleet renewal program. In the secondary offering, ACE reported selling an aggregate of 15,476,190 Variable Voting Shares and Voting Shares for gross proceeds of \$325 million. As at November 24, 2006, ACE reported holding a 75% ownership interest in Air Canada.

On October 27, 2009, Air Canada completed a bought deal public offering pursuant to which it sold to an underwriting syndicate 160,500,000 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 Variable Voting Share or one Voting Share, of Air Canada, and one-half of one share purchase warrant entitling the holder thereof to acquire one Variable Voting Share or one Voting Share at an exercise price of \$2.20 per Share, at any time prior to October 27, 2012. As a result of this public offering, and shares issued by Air Canada to a trust in conjunction with the adoption, in July 2009, of the Air Canada 2009 Pension Regulations and the completion of pension funding agreements with the Corporation's Canadian-based unions, ACE reported that its ownership interest in Air Canada, as at October 27, 2009, was reduced from 75% to 27%.

On December 23, 2010, ACE announced that it had concluded a public secondary offering on a bought deal basis of 44 million Class B voting shares of Air Canada for net proceeds to ACE of \$156 million. Air Canada did not receive any of the proceeds from this offering. As at December 23, 2010, after giving effect to this offering, ACE reported its ownership interest in Air Canada as having been reduced from 27% to approximately 11%.

On February 10, 2012, ACE announced its intention to seek shareholder approval for its winding-up, the distribution of its remaining net assets and, ultimately, its dissolution in the future. On April 25, 2012, ACE announced that its shareholders had approved a special resolution providing for the voluntary liquidation of ACE. On June 28, 2012, ACE announced that the Quebec Superior Court – Commercial Division had appointed Ernst & Young Inc. as liquidator of ACE.

On October 27, 2012, 79,430,300 warrants, which were issued in 2009 with an exercise price of \$2.20, expired.

On November 14, 2012, ACE announced that it had sold to Cormark Securities Inc., an investment dealer, a total of 31 million shares of Air Canada and 2.5 million warrants to purchase Air Canada shares at exercise prices of \$1.51 (1.25 million warrants) and \$1.44 (1.25 million warrants) and that, as a result, ACE no longer held any shares or warrants in the capital of Air Canada.

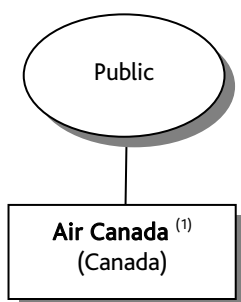
In 2013, Air Canada purchased for cancellation 2,083,333 warrants expiring July 30, 2013. In addition, the outstanding number of Shares increased by 7,916,667 upon exercise of warrants. Air Canada has no warrants left outstanding.

The head office of Air Canada is located at 7373 Côte-Vertu Boulevard West, Saint-Laurent, Québec, H4S 1Z3. Air Canada's website address is [aircanada.com](http://aircanada.com). (For greater certainty, no information contained in Air Canada's website is incorporated in this AIF by reference, unless expressly stated herein).

Additional information is provided in Air Canada's consolidated financial statements for the year ended December 31, 2013 and Air Canada's 2013 Management's Discussion and Analysis of Results of Operations and Financial Condition dated February 12, 2014 ("Air Canada's 2013 MD&A"), both of which are available on Air Canada's website at [aircanada.com](http://aircanada.com) and on SEDAR at [www.sedar.com](http://www.sedar.com).

### INTERCORPORATE RELATIONSHIP

The following chart and accompanying note describes, on a simplified basis, the corporate structure of Air Canada (including jurisdiction of establishment/incorporation of the various entities) as at December 31, 2013.



(1) *Air Canada directly and indirectly holds all of the issued and outstanding shares of certain subsidiaries, including Air Canada Capital Ltd. and Simco Leasing Ltd., which are incorporated under the laws of the province of Alberta. Air Canada holds all the issued and outstanding limited partner units of Touram Limited Partnership (doing business as Air Canada Vacations), a limited partnership formed under the laws of the province of Quebec. Touram General Partner Inc., a corporation incorporated under the laws of Canada, is the general partner of, and holds a 0.00001% interest in Touram Limited Partnership and Air Canada holds a 100% interest in Touram General Partner Inc. Air Canada also holds all the issued and outstanding limited partner units of Air Canada rouge LP (doing business as Air Canada rouge™), a limited partnership formed under the laws of the province of Quebec. Air Canada rouge General Partner Inc., a corporation incorporated under the laws of Canada, is the general partner of, and holds a 0.00001% interest in Air Canada rouge LP, and Air Canada holds a 100% interest in Air Canada rouge General Partner Inc.*

Subsidiaries of Air Canada, each of which represents not more than 10% of the consolidated assets and not more than 10% of the consolidated sales and operating revenues of Air Canada, and all of which, in the aggregate, represent not more than 20% of the total consolidated assets and the total consolidated sales and operating revenues of Air Canada at December 31, 2013, have been omitted.

## THE BUSINESS

### Overview

Air Canada is Canada's largest domestic, U.S. transborder and international airline and the largest provider of scheduled passenger services in the Canadian market, the Canada-U.S. transborder market and in the international market to and from Canada. In 2013, Air Canada, together with Jazz and other airlines operating flights on behalf of Air Canada under commercial agreements with Air Canada (which operate under the brand name "Air Canada Express" and which are referred to in this AIF as "Contracted Carriers") operated scheduled flights to 181 direct destinations on five continents.

At December 31, 2013, Air Canada operated a mainline fleet of 183 aircraft comprised of 81 Airbus narrow-body aircraft, 57 Boeing and Airbus wide-body aircraft and 45 Embraer 190 regional jets. In 2013, all of Air Canada's 15 Embraer 175 aircraft were transferred from the mainline fleet to Sky Regional Airlines, a lower cost regional provider.

The Air Canada Leisure Group was created in 2012 with a goal of improving the airline's earnings capabilities and strengthening its competitive position. This leisure travel group represents a coordinated strategy which leverages the strengths of Air Canada, Air Canada *rouge*, which launched its operations on July 1, 2013, and Air Canada Vacations. Air Canada Vacations is a leading Canadian tour operator. Based in Montreal and Toronto, Air Canada Vacations operates its business in the outbound leisure travel market (Caribbean, Mexico, U.S., Europe, Central and South America, South Pacific, Australia and Asia) by developing, marketing and distributing vacation travel packages. Air Canada Vacations also offers cruise packages in North America, Europe and the Caribbean.

The Air Canada Leisure Group is positioning itself in the highly competitive leisure market, with a strong value proposition and competitive cost structure, while benefiting from Air Canada's widely-recognized and respected brand, operational expertise, extensive global network, strong airport infrastructure and world-class loyalty program. Through Air Canada *rouge*, Air Canada expects to improve margins on leisure routes previously operated by the mainline fleet and pursue opportunities in international leisure markets made viable by Air Canada *rouge*'s more competitive cost structure.

Air Canada enhances its domestic and transborder network through capacity purchase agreements ("CPAs") with regional airlines, namely Jazz, Sky Regional, Air Georgian Limited ("Air Georgian") and Exploits Valley Air Services Ltd. ("EVAS"), which operate flights on behalf of Air Canada under the Air Canada Express banner. At December 31, 2013, the Air Canada Express fleet was comprised of 41 Bombardier regional jets, 86 Dash-8 turboprop aircraft, 15 Embraer 175 regional jets and 17 Beech 1900 aircraft.

Air Canada is a founding member of the Star Alliance® network. Through Star Alliance® network's 28 member airlines, Air Canada is able to offer its customers access to approximately 1,328 destinations in 195 countries, as well as reciprocal participation in frequent flyer programs and use of airport lounges and other common airport facilities.

Air Canada participates in a transatlantic joint venture with United Airlines and Deutsche Lufthansa AG through which the carriers provide customers with more choice and streamlined service on routings between North and Central America, and Africa, India, Europe and the Middle East. This transatlantic joint venture, including its revenue share structure, was implemented effective January 1, 2010. Air Canada also has the ability to create a transborder joint venture with United Airlines.

Through its long-term relationship with Aimia Canada Inc. (formerly Aeroplan Canada Inc. and referred to as "Aeroplan" in this AIF), Air Canada's loyalty program provider, Air Canada is able to build customer loyalty by offering those customers who are Aeroplan® members the opportunity to earn Aeroplan® Miles when they fly with Air Canada and with the 27 other Star Alliance® member airlines. Aeroplan is also Air Canada's single largest customer. The relationship with Aeroplan is designed to provide a stable and recurring source of revenue from the purchase of Air Canada seats by Aeroplan, which in turn are provided to Aeroplan® members who choose to redeem their Aeroplan® Miles for travel on Air Canada. Additionally, Aeroplan® members may also choose to redeem their Aeroplan® Miles for travel with the Star Alliance® member airlines. Furthermore, Aeroplan® members who are among Air Canada's most frequent flyers are recognized and rewarded through Air Canada Altitude™, a recognition program delivering a range of premium travel privileges and benefits depending on the status level they have reached.

Air Canada also generates revenue from its Air Canada Cargo division. Air Canada Cargo provides direct cargo services to over 150 Canadian, U.S. transborder and international destinations and has sales representation in over 50 countries. Air Canada Cargo is Canada's largest provider of air cargo services as measured by cargo capacity. Air cargo services are provided on domestic and U.S. transborder flights and on international flights on routes between Canada and major markets in Europe, Asia, South America and Australia.

Over the last several years, Air Canada has made significant progress in positioning itself to improve services to customers, create value for shareholders and transform its corporate culture to one that embraces leadership, accountability and entrepreneurship among its employees. The airline has been taking concrete, aggressive and targeted actions to successfully improve its earnings and lower the overall risk profile of the company through the execution of strategic initiatives designed to lower its cost structure, improve its balance sheet, increase its return on invested capital, further improve its market-leading customer service programs, de-risk its pension plans and provide a more stable and positive environment to its employees.

## STRATEGY

### Key Priorities

Air Canada's global strategy for sustained value creation and profitability is based on the following four key priorities:

- Cost transformation and revenue improvement
- International growth
- Customer engagement
- Culture change

Air Canada's key priorities and key achievements in 2013 are discussed in section 4 "Strategy" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by reference.

## ROUTES AND SCHEDULES

### Air Canada

In 2013, Air Canada, together with its Contracted Carriers, operated, on average, 1,498 daily scheduled flights, comprised of 60 Canadian cities, 54 destinations in the United States and a total of 67 cities in Europe, the Middle East, Asia, Australia, the Caribbean, Mexico and South America. Domestic, U.S. transborder and international departures accounted for approximately 67%, 25% and 8%, respectively, of the 1,498 average daily departures.

In 2013, Air Canada, together with its Contracted Carriers, carried 35.8 million revenue passengers and provided passenger service to 181 direct destinations on five continents.

Air Canada's hubs are located in Toronto, Vancouver, Montreal and Calgary, each of which provides extensive access to domestic, transborder and international markets. Toronto Pearson International Airport ("Toronto Pearson Airport") is the largest hub in Canada and a significant airline origin and destination market in North America. Vancouver International Airport is the second largest hub in Canada and is Air Canada's gateway to the Pacific Rim. Montreal's Pierre Elliott Trudeau International Airport ("Montreal Trudeau Airport") is the third most important hub in Air Canada's network and Calgary International Airport is Air Canada's fourth largest hub. For the year ended December 31, 2013, Air Canada, together with its Contracted Carriers, operated, on average:

- 326 daily departures from Toronto;
- 144 daily departures from Vancouver;
- 134 daily departures from Montreal, and
- 105 daily departures from Calgary.

#### Domestic Services

In 2013, Air Canada, together with its Contracted Carriers, provided the largest network and most extensive product offering in Canada, with scheduled direct passenger service to 60 Canadian destinations. The most important Canadian routes, in terms of operating revenues, are the transcontinental routes linking Toronto, Montreal and Ottawa with major western Canadian cities, including Vancouver, Calgary, Edmonton and Winnipeg. On a combined basis, Air Canada, together with its Contracted Carriers, operates a large number of short-haul routes, including Rapidair® routes, linking Toronto, Montreal and Ottawa. Air Canada, together with its Contracted Carriers, also offers frequent service linking major centres within western Canada, and operates numerous flights between Calgary, Edmonton and Vancouver. In addition to transcontinental and commuter routes, Air Canada, together with its Contracted Carriers, provides service between and within Central Canada, the Prairies and the Atlantic provinces.

#### Transborder Services

With the most non-stop destinations and flights from Canada to the United States, Air Canada, together with its Contracted Carriers, carries more passengers between Canada and the United States than any other airline. Air Canada, together with its Contracted Carriers, directly served 54 U.S. destinations in 2013. Air Canada's network reach is also enhanced through its extensive connections to, and code sharing flights with United Airlines, its Star Alliance™ partner.

#### International Services

Air Canada is well positioned as Canada's largest scheduled international airline. In 2013, Air Canada provided scheduled service directly to 67 destinations in Europe, the Middle East, Asia, Australia, the Caribbean, and Central and South America.

Air Canada offers transatlantic services to the United Kingdom, Germany, France, Switzerland, Israel, Ireland, Italy, Spain, Belgium, Denmark, Greece and Turkey. In 2014, Air Canada plans on expanding its international services to Europe from Toronto, Montreal, Vancouver and Calgary. The airline's summer 2014 schedule includes the introduction of year-round, non-stop service from Toronto to Milan, Italy with up to five weekly flights, offering the only non-stop service between Canada and Milan. In addition, Air Canada will increase its year-round Toronto-Istanbul non-stop service to daily flights from three times weekly. Air Canada will also deploy larger aircraft from its international wide-body fleet on flights from Calgary to London Heathrow and Frankfurt, as well as from Montreal to Brussels and Geneva in order to meet travel and cargo demand during the peak summer season.

As discussed in the section entitled "The Business" of this AIF, Air Canada participates in a transatlantic joint venture with United Airlines and Deutsche Lufthansa AG through which the carriers provide customers with more choice and streamlined service on routings between North and Central America, and Africa, India, Europe and the Middle East.

Air Canada also offers services to the Asia-Pacific market via its Vancouver, Calgary and Toronto hubs. Air Canada operates non-stop flights to Japan (Vancouver, Calgary and Toronto to Tokyo), China (Vancouver and Toronto to Beijing, Shanghai and Hong Kong) and Korea (Vancouver to Seoul). In 2014, Air Canada will continue to bolster its Asia-Pacific presence. Beginning on July 1, 2014, Air Canada will operate daily flights between Toronto-Pearson and Tokyo International Airport using the Boeing 787 Dreamliner. The new year-round service will be both the only non-stop flight between eastern Canada and Tokyo International Airport, located less than 30 minutes from downtown Tokyo, and the first daytime flight to Tokyo International Airport from North America. This will be the first deployment of Air Canada's Dreamliner aircraft in the Asian market and will feature the airline's new seating and cabin amenities. The new route will complement Air Canada's existing service to Tokyo Narita International Airport from Toronto, Calgary and Vancouver, which Air Canada will continue to offer. Both Japanese airports offer a wealth of onward domestic and international connections through All Nippon Airways and other Star Alliance™ partners.



Air Canada provides service directly to six destinations in South America, one in Australia, nine in Mexico/Central America and 29 in the Caribbean.

### **The Air Canada Leisure Group**

As discussed in the section entitled “The Business” of this AIF, the Air Canada Leisure Group was created in 2012 with a goal of improving the airline’s earnings capabilities and strengthening its competitive position. This leisure travel group represents a coordinated strategy which leverages the strengths of Air Canada, Air Canada *rouge* and Air Canada Vacations.

### **Air Canada Vacations**

Air Canada Vacations is a leading Canadian tour operator. Based in Montreal and Toronto, Air Canada Vacations operates its business in the outbound leisure travel market (Caribbean, Mexico, U.S., Europe, Central and South America, South Pacific, Australia and Asia) by developing, marketing and distributing vacation travel packages. Air Canada Vacations also offers cruise packages in North America, Europe and the Caribbean. Air Canada Vacations offers its products through its website at [vacations.aircanada.com](http://vacations.aircanada.com) and a network of independent travel agencies across Canada.

### **Air Canada *rouge***

Air Canada *rouge* launched its operations on July 1, 2013 with a start-up fleet of four aircraft transferred from the mainline fleet – two Boeing 767-300ER and two Airbus A319 aircraft. By the end of 2013, the Air Canada *rouge* fleet was comprised of eight Airbus A319 and two Boeing 767 aircraft. In 2014, additional Airbus A319 and Boeing 767-300 aircraft will be transferred from Air Canada’s mainline fleet to Air Canada *rouge*, with the expectation that Air Canada *rouge* will have up to 33 aircraft in its fleet by the end of 2014. As new Boeing 787 aircraft enter the mainline fleet, additional Boeing 767 aircraft are expected to be transferred to Air Canada *rouge*. Air Canada *rouge* may operate up to 20 Boeing 767 and 30 Airbus A319 aircraft, for a total of 50 aircraft.

Air Canada *rouge*’s lower cost structure enables Air Canada to compete on a more cost effective basis in the leisure market. While the Airbus A319 aircraft operated by Air Canada *rouge* are being used to provide service to leisure destinations previously operated by Air Canada mainline, the Boeing 767-300ER aircraft operated by Air Canada *rouge* are being used to provide service to certain European and high volume North American leisure destinations previously operated by the mainline fleet as well as to new leisure destinations in Europe. As part of the 2014 summer schedule, Air Canada *rouge* plans to launch seasonal non-stop flights to Barcelona, Dublin, Lisbon, Manchester, Nice and Rome and to continue to operate its summer routes to Athens, Edinburgh and Venice. In addition, beginning in the spring of 2014, routes previously operated by Air Canada from Toronto and Montreal to Cuba, Dominican Republic, Bahamas, Barbados, Haiti, Cancun and Tampa, Florida, are being converted to Air Canada *rouge* service. In addition, Air Canada *rouge* will expand to Western Canada to serve a number of predominantly leisure markets from Vancouver and Calgary to Los Angeles, San Francisco, Las Vegas and Anchorage. Existing service from San Diego to Toronto and from Calgary and Toronto to Phoenix will also be converted to Air Canada *rouge* service. The airline also plans to introduce new seasonal non-stop service operated by Air Canada *rouge* between Vancouver and Phoenix beginning December 17, 2014. Air Canada continues to evaluate future market opportunities as new aircraft are introduced in the mainline fleet and existing aircraft are released for operation by Air Canada *rouge* as market demand warrants. As of the date of this AIF, Air Canada *rouge* plans to operate a total of 54 routes.

### **Contracted Carriers**

As discussed in the section entitled “The Business” of this AIF, Air Canada enhances its domestic and transborder network through capacity purchase agreements with regional airlines, namely Jazz, Sky Regional, Air Georgian and EVAS, which operate flights on behalf of Air Canada under the Air Canada Express banner.

Jazz is an integral part of Air Canada’s North American strategy. Jazz operates both domestic and transborder services for Air Canada under the Jazz CPA. Jazz operates scheduled passenger service on behalf of Air Canada with approximately 723 departures per day to 55 destinations in Canada and 27 destinations in the United States as at December 31, 2013. Approximately 39% of Jazz’s traffic connects to Air Canada’s mainline network. In 2013, Jazz contributed approximately 20% of Air Canada’s consolidated domestic ASM capacity and approximately 14% of Air Canada’s consolidated transborder ASM capacity.

Sky Regional operates 15 daily non-stop return flights between downtown Toronto and Montreal Trudeau Airport for Air Canada under a capacity purchase agreement. In 2013, Air Canada transferred its 15 Embraer 175 aircraft from the

mainline fleet to Sky Regional who operates these aircraft on Air Canada's behalf under an amended capacity purchase agreement. These aircraft continue flying on U.S. short-haul routes, primarily from Toronto and Montreal to destinations in the Northeast U.S.

In December 2013, Air Canada concluded a memorandum of understanding to expand its relationship and amend its capacity purchase agreement with Air Georgian. Air Georgian has been selected to operate a number of regional routes starting in mid-2014, including transborder routes, using Canadair regional jet aircraft.

### **Star Alliance™**

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

Since its inception in 1997, the Star Alliance™ network has grown to include the following 28 airlines: Adria Airways, Aegean Airlines, Air Canada, Air China, Air New Zealand, ANA, Asiana Airlines, Austrian, Avianca, Brussels Airlines, Copa Airlines, Croatia Airlines, EGYPTAIR, Ethiopian Airlines, EVA Air, LOT Polish Airlines, Lufthansa, Scandinavian Airlines, Shenzhen Airlines, Singapore Airlines, South African Airways, SWISS, TAM Airlines, TAP Portugal, THAI, Turkish Airlines, United Airlines and US Airways. TAM Airlines and US Airways are expected to exit Star Alliance™ at the end of March 2014.

Through Air Canada's strategic and commercial arrangements with Star Alliance™ members and other airlines, Air Canada's customers have access to over 1,328 destinations in 195 countries, with reciprocal participation in frequent flyer programs and use of airport lounges. The Star Alliance™ is an alliance that brings together networks, lounge access, check-in services, ticketing and dozens of other services to improve the travel experience for customers. The airlines have implemented initiatives, such as common utilization of facilities, and are focusing on capturing potential synergies in additional areas. Air Canada code shares with all Star Alliance™ members, except for Adria Airways, Aegean Airlines, Copa Airlines, Croatia Airlines, Ethiopian Airlines, Eva Air and Shenzhen Airlines.

### **Cargo**

Air Canada Cargo provides direct cargo services to over 150 Canadian, U.S. transborder and international destinations and has sales representation in over 50 countries. The network is extended through interline agreements with other air carriers and through ground trucking services offered in selected markets.

Air Canada Cargo is Canada's largest provider of air cargo services as measured by cargo capacity. Its primary customers are large freight forwarding companies and businesses whose products require the use of air services to expedite their time sensitive cargo shipments. With safety and customer service at the heart of the business, Air Canada Cargo offers customers a unique set of business solutions tailored to meet their needs efficiently and cost-effectively. There are services for high priority shipments (AC Priority1™) and a service for standard air freight services (AC Standard™). In addition there are seven solutions including one for high value secure items, one for dangerous goods and one for temperature sensitive cargo such as those shipped by the pharmaceutical industry.

Air Canada Cargo uses e-business to drive value in the supply chain. The company offers e-freight and e-air waybills (which remove the need to carry paper documents) and is taking steps to assist customers in adapting to the positive changes supported by technology.

Air Canada Cargo is also actively involved in Cargo 2000 and several other industry initiatives to promote efficient cargo operations and improved service performance. This attention to quality raises their standing amongst their customers and maintains their competitiveness.

Air Canada Cargo's freight management system, AC Lynx™, offers customers a number of services including on-line tracking of cargo shipments. In addition, Air Canada Cargo is a founding member of Cargo Portal Services which offers customers a web-based booking and an air cargo management tool that facilitates the movement and tracking of air cargo globally.

In November 2013, Air Canada signed a Letter of Intent with Cargojet Airways Ltd. to explore strategic opportunities in both cargo and airline operations within Canada and internationally. The execution of related definitive agreements is expected to commence in the second quarter of 2014.

Air Canada Cargo continues to work with the various regulatory authorities worldwide and has shown its commitment to cargo security with the implementation of state of the art equipment and training.

### **AIR CANADA'S ENVIRONMENTAL OBJECTIVES**

Air Canada is mindful of the impact that its use of energy and natural resources has on the environment. To minimize the generation of waste as well as the emission of carbon dioxide and other greenhouse gases, Air Canada has developed an environmental management system based on principles of the International Organization for Standardization standard ISO 14000. Providing a continual cycle of planning, implementation and review, Air Canada's environmental management system is designed to ensure continuous improvement in its efforts towards meeting its environmental objectives.

Air Canada's main environmental objectives are as follows:

- Optimize energy consumption and minimize emissions resulting from air and ground operations including aircraft maintenance;
- Ensure efficient use of resources, minimize waste generation and effectively manage waste disposal;
- Minimize noise from aircraft operations;
- Seek opportunities to include in the supply chain suppliers that demonstrate a respect for the environment; and
- Promote sound environmental management policies and practices throughout the Corporation.

Air Canada measures and discloses its greenhouse gas emissions and climate change strategies through annual reporting to the Carbon Disclosure Project ("CDP"). The CDP is an organization based in the United Kingdom which works with shareholders and corporations to disclose the greenhouse gas emissions of major corporations. Air Canada is also monitoring its CO<sub>2</sub> emissions for flights to and from EU destinations in accordance with the EU ETS. Refer to section entitled "Regulatory Environment" of this AIF for additional information.

### **FINANCIAL OVERVIEW**

In 2011, Air Canada recorded operating income of \$179 million and EBITDAR of \$1,242 million. On a GAAP basis, Air Canada recorded a net loss of \$249 million. In 2009, Air Canada launched a comprehensive company-wide cost transformation program ("CTP") to improve unit revenue and cost productivity with the objective of achieving annualized revenue improvements and cost savings of \$530 million by the end of 2011. By September 30, 2011, Air Canada had surpassed its CTP target. The airline has now transitioned to a more permanent approach to business transformation. Refer to section 4 "Strategy" of Air Canada's 2013 MD&A for additional information, which section is incorporated into this AIF by reference.

In 2012, strong passenger demand, a disciplined approach to capacity management and ongoing focus on cost transformation and revenue enhancement resulted in Air Canada recording adjusted net income of \$55 million and EBITDAR, excluding the impact of benefit plan amendments, of \$1,320 million. On a GAAP basis, Air Canada recorded a net loss of \$136 million in 2012.

In 2013, Air Canada generated adjusted net income of \$340 million, the highest in Air Canada's history and an improvement of \$285 million from 2012. EBITDAR (excluding benefit plan amendments) amounted to \$1,433 million compared to EBITDAR (excluding benefit plan amendments) of \$1,320 million in 2012, an increase of \$113 million. Operating income of \$619 million reflected an improvement of \$177 million. In 2012 and 2013, Air Canada recorded operating expense reductions related to benefit plan amendments of \$127 million and \$82 million, respectively, as a result of amendments to defined benefit pension plans determined in accordance with new collective agreements concluded in 2011 and 2012 and changes to non-unionized employee pension plans. On a GAAP basis, Air Canada reported net income of \$10 million or \$0.02 per diluted share in 2013 compared to a net loss of \$136 million or \$0.51 per diluted share in 2012, an improvement of \$146 million or \$0.53 per diluted share.

The table below sets forth certain of Air Canada's financial results for the years ended December 31, 2013 and December 31, 2012:

(Canadian dollars in millions)	Year ended December 31, 2013	Year ended December 31, 2012
Passenger revenue	\$ 11,021	\$ 10,737
Cargo revenue	474	488
Other revenue <sup>(1)</sup>	887	889
<b>Total operating revenues</b>	<b>12,382</b>	<b>12,114</b>
<b>Total operating expenses <sup>(2)</sup></b>	<b>11,763</b>	<b>11,672</b>
<b>Operating income</b>	<b>619</b>	<b>442</b>
Non-operating expense <sup>(3)</sup>	(617)	(522)
<b>Income (loss) before income taxes and discontinued operations</b>	<b>2</b>	<b>(80)</b>
Income taxes	8	(1)
<b>Net income (loss) from continuing operations</b>	<b>10</b>	<b>(81)</b>
<b>Net loss from discontinued operations – Aveos <sup>(4)</sup></b>	<b>-</b>	<b>(55)</b>
<b>Net income (loss)</b>	<b>\$ 10</b>	<b>\$ (136)</b>

(1) Other revenues consist primarily of revenues from the sale of the ground portion of vacation packages, ground handling services and other airline-related services, as well as revenues related to the lease or sublease of aircraft to third parties.

(2) In 2013, Air Canada recorded an operating expense reduction of \$82 million related to amendments to defined benefit pension plans. In 2012, Air Canada recorded an operating expense reduction of \$127 million related to the terms of the ACPA collective agreement pertaining to retirement age. In 2013, Air Canada recorded an impairment charge of \$30 million.

(3) In 2013, Air Canada recorded an interest charge of \$95 million related to the purchase of its senior secured notes which were to become due in 2015 and 2016.

(4) In 2012, Air Canada recorded a loss on its investment in Aveos' parent holding company as a result of Aveos' filing for court protection pursuant to the CCAA and ceasing operations in March 2012. As a result, Air Canada reduced the carrying value of its investment in Aveos' parent holding company as well as the carrying value of a long term note receivable from Aveos to nil, and recorded an aggregate loss on investments of \$65 million in Non-operating expense. Air Canada also recorded a liability of \$55 million, which was charged to Discontinued operations, related to Air Canada's commitment under an employee separation program.

The table below sets forth the proportions of passenger revenues derived from domestic, transborder and international services of Air Canada for the years ended December 31, 2013 and December 31, 2012:

(in percent)	Year ended December 31, 2013	Year ended December 31, 2012
Domestic	38	39
Transborder	20	20
International	42	41
<b>Total</b>	<b>100 %</b>	<b>100 %</b>

For additional information on Air Canada's financial results for 2013, refer to Air Canada's consolidated financial statements for the year ended December 31, 2013, and Air Canada's 2013 MD&A, both of which are available on Air Canada's website at [aircanada.com](http://aircanada.com) or on SEDAR at [www.sedar.com](http://www.sedar.com).

Refer to section 20 "Non-GAAP Financial Measures" of Air Canada's 2013 MD&A, which can be found on Air Canada's website at [aircanada.com](http://aircanada.com) or on SEDAR at [www.sedar.com](http://www.sedar.com) and which section is hereby incorporated by reference in this AIF, for a reconciliation of adjusted net income (loss), and for a reconciliation of EBITDAR and EBITDAR, excluding the impact of benefit plan amendments, to operating income (loss).

## SIGNIFICANT FINANCING TRANSACTIONS

Air Canada entered into the following significant financing transactions in the years 2011 through to 2013:

- In 2013, Air Canada completed a private offering of three tranches of enhanced equipment trust certificates ("EETCs") with a combined aggregate face amount of US\$715 million, in connection with the financing of five new Boeing 777-300ER aircraft. Four of these five Boeing 777 aircraft were delivered in 2013 and the remaining aircraft was delivered in February 2014. The trust certificates have a weighted average interest rate of approximately 4.7% per annum.
- In 2013, Air Canada completed private offerings of senior secured notes, consisting of (i) US\$400 million principal amount of 6.750% senior secured first lien notes due 2019 and \$300 million principal amount of 7.625% senior secured first lien notes due 2019 (the "New Senior First Lien Notes") and (ii) US\$300 million principal amount of 8.750% senior secured second lien notes due 2020 (the "New Senior Second Lien Notes" and together with the New Senior First Lien Notes, the "New Senior Notes"). In conjunction with the completion of the offering of the New Senior Notes, Air Canada also completed the closing of its US\$400 million new senior secured (first lien) credit facility, comprised of a US\$300 million term loan maturing in 2019 and a US\$100 million revolving credit facility (collectively, the "New Credit Facility"). As at December 31, 2013, Air Canada had not drawn on the revolving credit facility. The weighted average interest rate of the new financing arrangements is approximately 7% per annum. Air Canada received, in total, net proceeds of approximately \$1,300 million from the sale of the New Senior Notes and from term loan borrowings under the New Credit Facility (in each case, after deduction of the applicable transaction costs, fees and expenses). Air Canada applied a portion of such net proceeds and borrowings to purchase all of its outstanding 9.250% Senior Secured Notes due 2015, 10.125% Senior Secured Notes due 2015 and 12.000% Senior Second Lien Notes due 2016 (collectively, the "Existing Notes") that were validly tendered on or before the early tender deadline (which was September 18, 2013), in connection with the cash tender offers commenced by the Corporation on September 5, 2013. In October 2013, Air Canada used a portion of the remaining net proceeds and borrowings to redeem the remaining Existing Notes of \$70 million not tendered prior to the early tender deadline. Air Canada is using the remaining net proceeds for working capital and general corporate purposes.

The New Senior Notes and Air Canada's obligations under the New Credit Facility are senior secured obligations of Air Canada, guaranteed on a senior secured basis by one or more of Air Canada's subsidiaries, and secured (on a first lien basis with respect to the New Senior First Lien Notes and Air Canada's obligations under the New Credit Facility, and on a second lien basis with respect to the New Senior Second Lien Notes), subject to certain permitted liens and exclusions, by certain accounts receivable, certain real estate interests, certain spare engines, ground service equipment, certain airport slots and gate leaseholds, and certain Pacific routes and the airport slots and gate leaseholds utilized in connection with those Pacific routes.

- In 2012, the repayment date of a short-term loan of \$78 million (US\$75 million) entered into in 2008 was extended to March 2015.
- In 2011, Air Canada entered into a revolving loan facility consisting of a Canadian dollar denominated revolving facility in the amount of \$50 million and a U.S. dollar denominated revolving facility in the amount of \$100 million. In 2013, Air Canada increased the Canadian dollar denominated revolving facility by \$75 million to a total of \$125 million. The agreement expires on January 31, 2015. As at December 31, 2013, an amount of approximately \$181 million (\$125 million and US\$53 million) was drawn under the facility.

## RATINGS

Ratings are intended to provide investors with an independent view of credit quality. However, they are not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the rating organization. Each rating should be evaluated independently of any other rating. Customary payments were made to credit rating organizations for the provision of rating services in respect of the Corporation's ratings and in respect of the ratings for the New Senior Notes and the Enhanced Equipment Trust Certificates ("EETCs").

Air Canada's corporate credit and/or Air Canada's New Senior Notes are rated (as of the dates indicated below) by the following rating agencies:

- Moody's Investors Service, Inc. ("Moody's");
- Standard & Poor's Rating Services ("Standard & Poor's");
- Fitch Ratings, Inc. ("Fitch"); and
- DBRS Limited ("DBRS").

### Moody's Ratings

On November 27, 2013, Moody's upgraded the following ratings relating to Air Canada:

- Air Canada's corporate family rating and probability of default ratings to B3 from Caa1 (rank 16 out of 21).
- New Senior First Lien Notes rating to B1 from B2 (rank 14 out of 21).
- New Senior Second Lien Notes rating to Caa1 from Caa2 (rank 17 out of 21).

The ratings on Air Canada's 2013-1 Class A, B, C EETCs were upgraded by one notch to: Baa2 (rank 9 out of 21), Ba3 (rank 13 out of 21), B2 (rank 15 out of 21), respectively.

### Standard & Poor's Ratings

On March 18, 2014, Standard & Poor's upgraded the following ratings relating to Air Canada:

- Air Canada's corporate credit rating to B from B-, with a stable outlook (rank 15 out of 22).
- New Senior First Lien Notes rating to BB- from B+ (rank 13 out of 22).
- New Senior Second Lien Notes rating to B- from CCC+ (rank 16 out of 22).
- Air Canada's recovery ratings: New Senior First Lien Notes ratings of 1 (rank 2 out of 7), indicating a very high (90 to 100%) recovery in a default scenario, and a New Senior Second Lien Notes rating of 5 (rank 6 out of 7), indicating a modest (10-30%) recovery in a default scenario.

The ratings on Air Canada's 2013-1 Class A, Class B and Class C EETCs were upgraded by one notch to: A (rank 6 out of 22), BB+ (rank 11 out of 22), and B+ (rank 14 out of 22), respectively.

### Fitch Ratings

On September 18, 2013, Fitch assigned the following ratings relating to Air Canada's New Senior Notes and New Credit Facility:

- Air Canada's long-term issuer default rating (IDR): B (rank 15 out of 21).

- New Senior First Lien Notes rating of BB (rank 12 out of 21) and a New Senior Second Lien Notes rating of BB- (rank 13 out of 21).
- Air Canada's recovery ratings: New Senior First Lien Notes ratings of RR1 (rank 1 out of 6), indicating an estimated recovery rate of 91-100%, and a New Senior Second Lien Notes rating of RR2 (rank 2 out of 6), indicating an estimated recovery rate of 71-90%.

The following respective ratings on Air Canada's 2013-1 Class A, Class B and Class C EETCs were issued by Fitch on May 7, 2013: A (rank 6 out of 21), BB+ (rank 11 out of 21) and BB- (rank 13 of 21), respectively.

#### **DBRS Ratings**

On November 14, 2013, DBRS reaffirmed Air Canada's Issuer Rating of "B" (rank 15 out of 26), with a stable trend.

### **PENSION PLAN ARRANGEMENTS**

Air Canada maintains several pension plans, including defined benefit and defined contribution pension plans and plans providing other retirement and post-employment benefits to its employees. The Canadian registered pension plans solvency deficit at January 1, 2013 was \$3.7 billion. The next required valuations to be made as at January 1, 2014, will be completed in the first half of 2014, but as described below, they will not increase the 2014 pension past service cost funding obligations. Based on preliminary estimates, in aggregate, the domestic registered pension plans are estimated to be in a small surplus position on a solvency basis as at January 1, 2014.

For information on Air Canada's pension plan arrangements, refer to Air Canada's consolidated financial statements for the year ended December 31, 2013, and section 9.7 "Pension Funding Obligations" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference.

### **FOREIGN EXCHANGE**

Air Canada's cash inflows are primarily in Canadian dollars, while a large portion of its outflows are in U.S. dollars. Fluctuations in foreign exchange rates may adversely impact operating results and cash flows. Air Canada has a risk management objective to reduce cash flow risk related to foreign denominated cash flows. Additional information can be found in Air Canada's consolidated financial statements for the year ended December 31, 2013, and section 12 "Financial Instruments and Risk Management" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference.

### **AIRCRAFT FUEL**

Aircraft fuel is a major expense in the airline industry and the single largest expense to Air Canada, representing approximately 30% of Air Canada's 2013 total operating expenses. Additional information can be found in Air Canada's consolidated financial statements for the year ended December 31, 2013, and section 12 "Financial Instruments and Risk Management" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference.

### **AIRCRAFT FLEET**

For information relating to Air Canada's fleet as at December 31, 2013 and fleet plans, refer to section 8 "Fleet" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference..

## EMPLOYEES AND ARRANGEMENTS WITH UNIONS

The following table provides a breakdown of Air Canada's average full-time equivalent ("FTE") employees for the years 2013 and 2012 together with the unions that represent them.

Employee Group	Union <sup>(1)</sup>	2013	2012
Management and Administrative Support	n/a <sup>(2)</sup>	3,617	3,403
Pilots	ACPA	2,802	2,760
Flight Attendants	CUPE	6,186	5,840
Customer Sales and Service Agents	UNIFOR/IBT	3,521	3,579
Technical Services, Ramp and Cargo	IAMAW	7,497	7,533
United Kingdom Unionized Employees	UNITE	575	579
Other Unionized	various	297	309
<b>Total</b>		<b>24,495</b>	<b>24,003</b>

*(1) ACPA: Air Canada Pilots Association; CUPE: Canadian Union of Public Employees; UNIFOR (formerly CAW: Canadian Auto Workers); IBT: International Brotherhood of Teamsters; IAMAW: International Association of Machinists and Aerospace Workers; and UNITE.*

*(2) Certain administrative support employees are represented by IAMAW.*

Most of Air Canada's employees are unionized, and labour costs constituted one of Air Canada's largest operating cost items in 2013. In 2011, tentative collective agreements with the CAW (now referred to as UNIFOR), the union representing Air Canada's customer service employees at airports and call centres, as well as with CUPE, the union representing Air Canada's flight attendants, were concluded and, respectively, ratified or conclusively settled through arbitration. The agreement with the CAW (now referred to as UNIFOR) is in effect until February 28, 2015 and the agreement with CUPE is in effect until March 31, 2015. In 2011, Air Canada also entered into a collective agreement with UNITE, the union representing the airline's London Heathrow-based employees. In the first quarter of 2012, Air Canada concluded agreements with the CAW, in relation to in-flight crew schedulers and flight operations crew schedulers, and with CALDA, in relation to flight dispatchers. In June 2012, the decision of the arbitrator was issued in respect of the IAMAW final offer selection arbitration conducted in accordance with the process legislated by the federal government in the Protecting Air Service Act. The arbitrator's final offer selection concluded a new five-year collective agreement between Air Canada and the IAMAW which is in effect until March 31, 2016. In July 2012, the decision of the arbitrator was issued in respect of the ACPA final offer selection arbitration conducted in accordance with the process legislated by the federal government in the Protecting Air Service Act. The arbitrator's final offer selection concluded a new five-year collective agreement between Air Canada and ACPA which is in effect until April 1, 2016.



## FACILITIES

Air Canada owns or leases facilities in major airports consisting of offices, hangar space, aircraft maintenance and ground handling facilities. The following describes the principal properties owned or leased by Air Canada as at December 31, 2013:

<u>Principal Properties</u>	<u>Description</u>	<u>Square Footage</u>	<u>Nature of Title</u>
Montreal – Air Canada Centre Air Canada Headquarters	Head office and training facilities	272,000	Owned facilities on leased land
Montreal Trudeau Airport – Maintenance Base	Offices, computer centre, aircraft maintenance, hangars, workshops and training facilities	1,326,664	Owned facilities on leased land
Toronto Pearson Airport – Terminal Building	Counters, offices, passenger and baggage handling facilities	180,000	Leased
Toronto Pearson Airport – Maintenance Base	Offices, hangars, shops and simulators	1,021,632	Owned facilities on leased land
Toronto Pearson Airport	Offices, shops, training and equipment storage	258,757	Leased
Toronto – Cargo Facility and Equipment Maintenance	Offices, cargo and equipment maintenance facilities	426,000	Leased
Brampton, Ontario SOC Building	Systems Operations Control	74,000	Owned facility on owned land
Vancouver – Technical Operations Centre	Offices, hangars, shops and simulators	1,087,985	Owned facilities on leased land
Vancouver – South Hangar	Offices, hangars, shops, stores	131,626	Owned facilities on leased land
Calgary International Airport	Hangar, commissary, ground support equipment and warehouse	267,891	Owned facilities on leased land
Winnipeg – Air Canada Building	Offices and computer centre	394,650	Owned land and facility
Winnipeg Airport – Maintenance Base	Offices, aircraft maintenance hangars and workshops	278,891	Owned facilities on leased land

Air Canada operates additional office, terminal, maintenance and/or cargo facilities under long-term leases at Toronto, Montreal, Vancouver, Calgary, London (England) and Los Angeles. A portion of the hangar space and aircraft maintenance facilities in Montreal and Toronto are leased or subleased by Air Canada to Jazz and other third parties. In February 2012, Air Canada repurchased the Air Canada Building in Winnipeg. A significant portion of the office space in the Air Canada Building in Winnipeg is subleased to third parties.

On March 18, 2012, Aveos announced that it had ceased operating its airframe maintenance facilities in Montreal, Winnipeg and Vancouver. On March 19, 2012, Aveos filed for court protection pursuant to the CCAA. As part of their restructuring, Aveos notified Air Canada that it was repudiating all leases from Air Canada of hangar space, effective September 30, 2012. Aveos has since vacated these premises.

## TRADEMARKS

Air Canada believes that its trademarks are important to its competitive position. Air Canada is Air Canada's trade name and trademark. Other trademarks include Air Canada Express™, Air Canada Jetz®, Air Canada Jazz®, Jazz®, Air Canada Vacations®, Vacances Air Canada®, Executive First®, Executive Class®, AC Priority™, AC Air Freight™, Rapidair®, Maple Leaf™, Feuille d'érable™, Maple Leaf Lounge™, Air Canada Elite®, Air Canada Super Elite®, Air Canada *rouge*™, Altitude™, Altitude Prestige™, Altitude Elite™, Altitude Super Elite™ and related design marks such as the Air Canada Roundel®. Air Canada has granted Aimia Canada Inc. (formerly Aeroplan Canada Inc.) a license to use Air Canada® and Air Canada Roundel® trademarks around the world solely in association with the Aeroplan® program. Air Canada has granted Jazz a license to use Air Canada Jazz®, Jazz®, Air Canada®, Air Canada Design®, Air Canada and Design® and other trademarks in Canada and the United States in association with the provision of scheduled airline services in regions of Canada and across the Canada–United States border on behalf of Air Canada. Air Canada protects its proprietary information, including its trademarks and database, through trademark laws, contractual provisions, confidentiality procedures and other means. Employees, service providers, and other parties with whom Air Canada carries on business are, as appropriate, contractually bound to protect Air Canada's proprietary information in order to control access to and the distribution of any such information.

## REGULATORY ENVIRONMENT

In Canada, commercial air transportation, including policy, maintenance standards, operations standards, safety and ground and navigation facilities, falls wholly within the jurisdiction of the Government of Canada and is the responsibility of the Minister of Transport. The Canadian Transportation Agency, an independent administrative body of the Government of Canada, acts as a quasi-judicial tribunal to resolve a range of commercial and consumer transportation-related disputes and acts as an economic regulator, to make determinations and to issue authorities, licenses and permits related to the air transportation industry. NAV Canada, a private sector, non-share capital corporation, is responsible for providing air navigation services in Canada. All major Canadian airports are operated by Canadian airport authorities that are not-for-profit corporations.

### Domestic Services

On December 16, 2011, the Government of Canada announced that the Canadian Transportation Agency would proceed with developing regulations requiring, among other things, air carriers to include all fees, taxes and surcharges in their advertised prices, by bringing into force section 86.1 of the *Canada Transportation Act* ("CTA"). The regulations were published on January 2, 2013 and are in force.

### Transborder Services

Transborder services between Canada and the United States were initially liberalized by the 1995 Canada–U.S. Air Services Agreement. This agreement provides Canadian air carriers unlimited route rights to provide "own aircraft" services between points in Canada and points in the United States. Under the 1995 Canada–U.S. Air Services Agreement, carriers of both countries are free to set their own prices for transborder services according to market forces. Prices may only be disallowed under special circumstances if the authorities of both countries agree, for example in response to predatory or monopolistic pricing behaviour on specific routes. In November 1997, Canada and the United States concluded an agreement that allows Canadian and U.S. carriers to code share to, from and via each other's territory, with carriers from other countries provided the other country allows code sharing and the carriers hold the underlying rights to serve that country. Air Canada code shares with certain Star Alliance™ partners via Canada and the United States and some of these Star Alliance™ partners' codes appear on some transborder flights operated by other airlines operating flights on behalf of Air Canada, including Jazz Aviation LP ("Jazz"), a subsidiary of Chorus Aviation Inc., and Sky Regional Airlines Inc. ("Sky Regional").

The Open Skies Agreement between Canada and the United States, which came into force in 2007, further liberalized air transportation services. The Open Skies Agreement allows air carriers of both countries (i) to pick up passenger and/or cargo traffic in the other country and carry that traffic to a third country as part of a service to or from the carrier's home country, (ii) to operate stand-alone all-cargo services between the other country's territory and third countries, and (iii) greater pricing flexibility for services between the other country and a third country. The carriage of local traffic between points within one country by carriers of the other country, commonly known as cabotage, continues to be prohibited.

### **International Services**

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

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

On November 27, 2006, the Minister of Transport released a new international air transportation policy called Blue Sky that includes a more liberalized approach to Canada's bilateral air transportation negotiations. The Government of Canada indicated that, under the new policy, when in Canada's overall interest, it would proactively pursue opportunities to negotiate more liberalized agreements for international scheduled air transportation that will provide maximum opportunity for passenger and all-cargo services to be added according to market conditions. On December 9, 2008, the Minister of Transport announced that Canada had successfully concluded negotiations with the European Union on a comprehensive air transport agreement. Such agreement includes, among other things, unrestricted direct air services between Canada and European Union member states, flexible pricing arrangements, increased flexibility on code sharing and improved flexibility on cargo services. Although not yet in force, these rights and others contained in this new air transport agreement have been available, on a provisional basis, since December 18, 2009.

### **Charter Services**

Charter operations are generally not covered by bilateral agreements, although charter services are covered under the Open Skies Agreement. Canadian government policy permits Canadian carriers to operate charter services between Canada and any point in the world subject to prior approval of the Canadian and other appropriate regulatory authorities.

The policy governing international passenger charter air services does not contain restrictions relating to advance booking, minimum stay requirements or prohibitions on one-way travel, however it requires that the entire seating capacity of an aircraft is chartered and that charter carriers are prohibited from selling seats directly to the public.

### **Foreign Ownership Rules**

The Government of Canada's Bill C-10, the *Budget Implementation Act 2009*, contains provisions whereby the provisions relating to voting securities in the *Air Canada Public Participation Act* ("ACPPA") would be repealed and the CTA would be amended to provide the Governor in Council with flexibility to increase the foreign ownership limit from the existing 25% level to a maximum of 49%. These provisions will come into force on a date to be fixed by order of the Governor in Council made on the recommendation of the Minister of Finance, in the case of the ACPPA, and on the recommendation of the Minister of Transport, in the case of the CTA. Management cannot predict if or when the provisions relating to foreign ownership limits will come into force.

## Carbon Emissions

There continues to be heightened focus on carbon emissions emanating from the aviation industry and legislation in various jurisdictions is being considered or adopted. Legislative initiatives include, for example, market-based mechanisms such as emissions trading systems, designed to reduce the total amount of carbon emissions by all targeted industries through the setting of permissible emissions allowances for these industries. Individual operators within those industries are generally allocated a certain number of free emission allowances and may purchase additional allowances from the pool of permissible emissions allowances. In certain circumstances, they may also purchase or sell permissible emissions allowances among operators across different industries and may obtain emissions credits by investing in certified carbon reduction projects or by taking certain early action in reducing their carbon footprint.

On November 19, 2008, the European Parliament adopted directive 2008/101/EC to add the aviation industry to the industries covered by the existing European Emission Trading Scheme ("EU ETS"). The EU ETS caps greenhouse gas ("GHG") emissions from covered industries while allowing trading of permissible GHG emissions allowances among the operators in the covered industry. Aviation emissions were incorporated in the EU ETS starting January 2012 to include flights operated between Canada and countries within the European Union. The EU ETS would require aircraft operators to monitor and report fuel consumption and carbon dioxide emissions data. While this legislation would be expected to result in increased costs to the aircraft operators, as it relates to the purchase of emissions allowances, the net financial impact depends, in part, upon the percentage of such cost that, if any, would be recoverable in the form of higher passenger and cargo fares.

In November 2012, the European Commission announced that it would defer the implementation of the EU ETS as it applies to flights to and from third countries ("extra-EU flights") pending work being done by the International Civil Aviation Organization ("ICAO") on market-based measures and that was then expected to be agreed on at the ICAO assembly in the fall of 2013. Flights between EU aerodromes ("intra-EU flights") operated in 2012 were still subject to carbon emission reporting and surrender of allowance to cover the emissions. The derogation, referred to as the "Stop the Clock Decision", suspends the application of the EU Emissions Trading Aviation Directive 2008/1001 in regards to the remittance of allowances and monitoring requirement for extra-EU flights on both EU and non-EU airlines for the year 2012. The Directive was therefore not enforced and payment was not required by EU regulatory authorities in respect of extra-EU flights operated in 2012, however, as indicated above, intra-EU flights remained covered. The suspension of compliance obligations was conditioned on a requirement that aircraft operators return any free allowances that had been allocated for 2012 in respect of their international flights. The final regulatory text for the derogation was adopted by the EU Parliament and the derogation went into effect in April 2013.

Following the outcome of the ICAO General Assembly, on October 16, 2013, the European Commission announced a legislative proposal to replace the "Stop the Clock Decision". This new proposal, which was further amended by EU council on March 5, 2014, if implemented, would mean that for the 2013 EU ETS reporting year, only intra-EU flights would be counted and the reporting and surrendering of allowances for 2013 would be deferred until March 31, 2015 and April 30, 2015, respectively. For the 2014 to 2020 reporting years, intra-EU flights and flights to and from third countries to the EU would be covered; however for the EU-third country flights only the portion of the flights over EU airspace would be counted.

A decision by the EU Parliament on this new proposal is expected by April 7, 2014. Until such a decision is reached, the current full application of EU ETS is in effect and emissions from flights to and from third countries to the EU are counted for the complete journey, with reporting deadlines for 2014 in effect as well; however recent communication from the European Commission indicates that these deadlines may not be enforced by Member States given the timing of the decision deadline. No allowances will be issued in 2014 before the proposal is approved, as the new rules would require a recalculation of the free allocation, as well as of the amount of allowances to be auctioned, both for 2013 and for 2014 to 2020.

Based on the uncertainty of acceptance of the legislative proposals, on a preliminary basis, Air Canada has estimated its compliance costs (which include the free allowances) for 2014 to be \$3 million. This preliminary estimate is subject to change based on the change in the market price of European Union CO<sub>2</sub> allowances ("EUAs") and other factors such as Air Canada's operations to the EU, its ability to offset costs through higher passenger fares, cargo rates and/or surcharges. At the present time, Air Canada has not implemented a specific Emission Trading Scheme ("ETS") surcharge and is currently taking these costs under consideration in the context of its global fuel surcharge strategy.

Air Canada *rouge* would also be required to comply with the EU ETS legislation. In 2013, the carrier was exempt from EU ETS reporting, however, given the increase in routes to Europe, it will be required to participate in the ETS in 2014. Air Canada *rouge* will report its emissions and surrender its allowances independently of Air Canada. Until such time that Air Canada *rouge* is activated in the ETS and free allowances are allocated, Air Canada will not be in a position to estimate the cost of Air Canada *rouge*'s compliance with the EU ETS.

On the domestic front, on October 19, 2006, the Government of Canada tabled the *Clean Air Act* with the intention to strengthen the legislative basis for taking action on reducing air pollution and GHG emissions. Since then, a number of supporting regulations on a sector-by-sector basis have been developed, and a national target set in alignment with the United States. At this time, there are no specific targets for aviation emissions.

However, in 2012, the Government of Canada and the Canadian aviation industry announced the development of Canada's Action Plan to Reduce Greenhouse Gas Emissions from Aviation, which is a voluntary action plan that sets an aspirational goal to improve fuel efficiency from a 2005 baseline by an average annual rate of at least 2 percent per year until 2020 (the "Voluntary Action Plan"). The three principle measures to achieve this target are fleet renewals and upgrades, more efficient air operations, and improved capabilities in air traffic management. The Voluntary Action Plan also supports the aspirational goal of carbon neutral growth from 2020 onwards and absolute GHG emission reductions by 2050. Further work is underway to establish monitoring and reporting standards under this plan.

In 2010, Air Canada endorsed the new industry targets (as set out by the International Air Transport Association "IATA") to collectively achieve: (i) an average improvement of fuel efficiency of 1.5% per year from 2009 to 2020, (ii) carbon neutral growth from 2020 onwards, and (iii) a reduction in CO<sub>2</sub> emissions of 50% by 2050, relative to 2005. Air Canada has achieved a cumulative fuel efficiency improvement of 5.85% between 2009 and 2013.

### **Official Languages Act**

Pursuant to the ACPPA, Air Canada is subject to the *Official Languages Act* (Canada) (the "OLA"). The OLA compels Air Canada to, among other things, ensure that any member of the traveling public can communicate with and obtain services in either official language, French and English, where there is significant demand for those services in that language (Part IV of the OLA) and to allow its direct employees to work in either official language (Part V of the OLA) where there is significant demand. The ACPPA also imposes on Air Canada the obligation to ensure any of its subsidiaries' customers can communicate with the subsidiary in respect of air services and incidental services, and obtain those services, in either official language, where the number of customers warrants such services.

Pursuant to the OLA, where services are performed on behalf of Air Canada by another party, Air Canada has the duty to ensure that any member of the public can communicate with and obtain those services in either official language in any case where those services, if provided by Air Canada, would be required under the OLA to be provided in either official language.

On October 17, 2011, Bill C-17, *An Act to amend the Air Canada Public Participation Act* was tabled for first reading in the House of Commons. Such proposed legislation, if enacted without amendment, would (i) extend the application of Parts IV, IX and X of the Official Languages Act to designated air carriers under contract with Air Canada; and (ii) exempt Air Canada from the application of section 25 of the Official Languages Act with respect to air services provided or made available by air carriers with which it has only code-sharing arrangements. This bill has not been reintroduced in the current parliamentary session. Management cannot predict if or when Parliament will proceed with such proposed legislation.

### **Security**

Air Canada's first priority is to ensure the safety and security of its customers, employees and aircraft by maintaining the highest safety and security standards.

Since the September 11, 2001, terrorist attacks in the United States, new air security measures have been and are being regularly introduced in Canada and elsewhere (such as increased passenger and baggage screening, enhanced security procedures at check-in gates and on board the aircraft, reinforced cockpit doors on aircraft, an expanded program of armed police on aircraft and a requirement for passengers to produce valid identification prior to boarding all flights). On April 1, 2002, the Government of Canada established the Canadian Air Transport Security Authority ("CATSA"). CATSA's responsibilities fall into four major air security areas, namely, pre-board screening of passengers and their belongings, hold

baggage screening, non-passenger screening of those entering airport restricted areas and restricted area identity card implementation and management. An air traveler's security charge was introduced on April 1, 2002, to cover the costs of CATSA. The charges have been revised in subsequent federal budgets. As of January 1, 2013, the maximum charge is \$15 for domestic travel, \$25 for transborder travel and \$26 for international travel.

In October 2002, the Government of Canada implemented its Advance Passenger Information initiative to help identify potentially high risk individuals and address other border security issues. In March 2003, it also established a Passenger Name Record program. Canadian and foreign carriers are required by regulation to provide the Canada Border Services Agency ("CBSA") with specific personal information on all passengers and crew members on board international flights destined to Canada at the time of departure, as well as to provide access to passenger name records in the carriers' internal reservation systems.

Foreign countries such as the United States, the United Kingdom, Australia, Mexico, South Korea, Costa Rica, the Dominican Republic, Japan, China and countries that are members of the Caribbean Community and Common Market ("CARICOM") have enacted similar information requirements with respect to flights operating into and/or from their territory. Air Canada also complies with the Secure Flight requirements imposed by the U.S. Transportation Security Administration ("TSA") which require the provision of basic passenger information prior to flight and more complete information at check-in to enable the TSA and U.S. Customs and Border Protection ("CBP") to perform their watch list and Electronic System for Travel Authorization ("ESTA") verifications prior to the issuance of the passenger's boarding pass. Effective December 1, 2013, Russia requested detailed advance passenger and crew data for any flight operating to, from or overflying Russian airspace.

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

The Passenger Protect Program and Identity Screening Regulations came into effect in June 2007. Passengers aged 18 or over are required to have in their possession government-issued identification which includes their name, date of birth and gender. The identification may be required at check-in and must be presented at the boarding gate. The verification requirements were amended in 2010 to require a comparison of the passenger's full face with the identification document. If a passenger refuses to remove facial coverings, Air Canada must deny carriage. All immigration documentation requirements still apply on international flights.

The failed terrorist attack in December 2009 on board a U.S. commercial carrier prompted the implementation of additional security measures for flights to the United States, including restrictions relating to carry-on baggage. The October 2010 attempted attacks on cargo aircraft bound for the United States have resulted in regulations imposing stricter controls on cargo security.

Air Canada continues to work with the appropriate authorities to ensure full compliance with security requirements, including new programs that will affect the airline industry:

- Air Canada was the first carrier in Canada to provide Transport Canada with a security management system. The security management system uses threat/risk assessments in conjunction with government regulations to define appropriate security measures and then monitors compliance through audits and incident reporting;
- Air Canada has implemented the measures imposed by Transport Canada under the Passenger Protect Program as Air Canada already complies with similar requirements imposed by the TSA, a U.S. government agency for its Secure Flight program;
- Air Canada works with CATSA and other agencies to continuously improve security measures and to ensure that any innovation adopted by Air Canada maintains the highest degree of security; and

- More stringent cargo screening regulations requiring 100% screening took effect in various jurisdictions, including in Canada effective December 31, 2012. This has led to increased security related costs for screening equipment and security services providers. Complexities of screening various cargo commodities necessitate additional staff for validation, segregation procedures and record keeping. Participants may perform their own screening and be registered by the various jurisdictions to become secure supply chain participants. In 2013, the charges applied to supply chain participants who are not registered are expected to largely offset the expected increased costs to Air Canada.

## Safety

In order to improve the safety performance of Canadian air operators and increase accountability in the aviation sector, Canadian Aviation Regulations require air operators to implement a Safety Management System ("SMS") in their organizations and appoint executives who are accountable for safety.

Air Canada has an approved safety management system in place in accordance with the Canadian Aviation Regulations. Air Canada's President and Chief Executive Officer has been appointed as the Accountable Executive ("AE") for Air Canada's Safety Management System and Air Canada's Senior Director, Corporate Safety, Environment and Quality, is responsible for the day-to-day administration and oversight of the Safety Management System on behalf of the AE.

The development of Safety Management Systems in Canada continues to evolve. In October 2013, Air Canada completed a full SMS assessment with Transport Canada. This process ensures that Air Canada is fully committed to the principles of the SMS program and that its operations are compliant with all aspects of it. Further, Air Canada, as a founding member of Star Alliance™, is actively engaged in helping ensure that Star Alliance™ members, including Air Canada, are guided by best industry practices and enhanced safety performance. Additional non-regulated measures, such as the completion of Line Operations Safety Audits, the establishment of Flight Data Monitoring programs, the implementation of Fatigue Risk Management Programs and compliance with IATA, Operational Safety Audit standards are key examples where Air Canada is leading international safety efforts.

Air Canada is an active member of the international safety team and actively involved in IATA, ICAO and regional safety meetings and working groups. Air Canada is closely aligned with IATA and Star Alliance™ concerning international benchmarking of standards and safety performance and is sharing its experience and knowledge to help develop advanced safety tools to better understand risk, and hazards.

## Privacy

Air Canada is subject to applicable Canadian and foreign privacy laws regarding the collection, use, disclosure and protection of passenger and employee data. In Canada, Canada's federal private sector privacy legislation, the *Personal Information Protection and Electronic Documents Act* (Canada) (the "PIPEDA"), governs the collection, use and disclosure of personal information in the course of commercial activities by a federally-regulated business. In addition, the PIPEDA regulates the handling of employee personal information by federally-regulated employers. With certain exceptions, the PIPEDA also applies to the collection or disclosure of personal information across provincial or Canadian international borders and within provinces without substantially similar private sector privacy legislation. The PIPEDA requires informed implicit or explicit consent, as the case may be, by the individuals whose personal information is collected and used. The personal information may then only be used for the purposes for which it was originally collected or for other purposes specified in, or allowed by, the PIPEDA. Air Canada has a privacy policy which is designed to meet or exceed the requirements of such privacy legislation.

## INDUSTRY OVERVIEW AND COMPETITIVE ENVIRONMENT

### General

The airline industry has traditionally been dominated by large established network carriers. Network carriers generally benefit from brand name recognition and a long operating history. They offer scheduled flights to major domestic and international cities while also serving smaller cities. They generally concentrate most of their operations in a limited number of hub cities, serving most other destinations in their network by providing one-stop or connecting service through their hubs.

Over the past three decades, governments gradually reduced economic regulation of commercial aviation. This has resulted in a more open and competitive environment for domestic, transborder and international airline services, for both scheduled and leisure charter operations. This deregulation transformed the airline industry and allowed the emergence of low-cost carriers, which resulted in a rapid shift in the competitive environment. With their relatively low unit costs largely resulting from lower labour costs and a simplified operational model and product offering, low-cost carriers are able to operate profitably while generally achieving lower yields than network carriers. By offering lower fares, these carriers have expanded and succeeded in gaining market share from network carriers. While the majority of low-cost carriers offer predominantly point-to-point services between designated cities, some utilize a similar "hub and spoke" strategy to the network carriers. WestJet Airlines Ltd. ("WestJet") is the largest low-cost carrier in Canada and operates flights to destinations in North America, Central America and the Caribbean. WestJet reported operating a fleet of 113 aircraft as at December 31, 2013. In June 2013, WestJet launched a new short-haul regional airline, named WestJet Encore, which at maturity, according to plans announced by WestJet, could operate up to 45 Q400 turboprop aircraft (comprised of 20 committed and 25 option aircraft), eight of which were delivered in 2013.

### Domestic Market

The Canadian domestic market is characterized by a large geographic territory with a limited number of high density markets accounting for the majority of passenger traffic and revenue. This leads to a concentration of routes in Canada around four major hubs: Toronto, Montreal, Vancouver and Calgary.

Air Canada is the largest provider of scheduled passenger services in the Canadian market. Based on Official Airline Guide ("OAG") data, during the period from January 1, 2013 to December 31, 2013, Air Canada, together with its Contracted Carriers, led the Canadian airline industry's domestic scheduled capacity with an estimated market share of approximately 55% based on Available Seat Miles ("ASMs"). Air Canada is Canada's largest domestic airline. Jazz is the largest regional airline in Canada and operates regional services for Air Canada under a capacity purchase agreement (the "Jazz CPA"). Air Canada, together with its Contracted Carriers, carries more passengers, serves more non-stop destinations and provides more flights in the domestic market than any other airline.

Competition in the domestic market is primarily from WestJet. As at December 31, 2013, Air Canada, together with its Contracted Carriers, provided service to 60 domestic destinations within Canada, while WestJet provided service to 35 domestic destinations.

Porter Airlines Inc. ("Porter") is a regional passenger carrier based at and operating primarily from Billy Bishop Toronto City Airport in the eastern triangle market to compete with Air Canada's Rapidair services at Toronto Pearson Airport. The airline serves primarily short-haul business markets such as Ottawa, Montreal, New York (Newark), Chicago (Midway), Washington (Dulles) and Boston (Logan) from Toronto, operating with a fleet of 26 70-seat Bombardier Q400 aircraft.

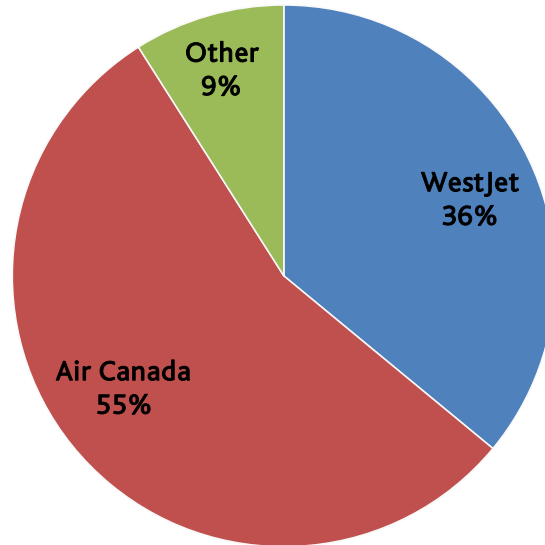
On May 1, 2011, Sky Regional commenced service between Toronto Island's Billy Bishop Toronto City Airport and Montreal Trudeau Airport on behalf of Air Canada pursuant to a capacity purchase agreement. Air Canada's schedule provides up to 15 daily non-stop return flights between downtown Toronto and Montreal Trudeau Airport.

Other airlines operating in the domestic market include Canadian North and First Air, based in Yellowknife and Iqaluit, respectively, and they operate services primarily within northern Canada and connecting northern Canada to the rest of the country.



The following chart illustrates the estimated share of the overall domestic scheduled capacity provided by Air Canada, together with its Contracted Carriers, as measured by ASMs.

### Estimated Domestic Scheduled Capacity Market Share



(1) Source: OAG data, based on ASMs during the period from January 1, 2013 to December 31, 2013; represents the estimated share of the overall domestic scheduled capacity of Air Canada and its Contracted Carriers. The estimated share of the overall domestic scheduled capacity of the other carriers presented also includes the domestic scheduled capacity of their respective affiliated or contracted regional carrier(s), when applicable.

#### U.S. Transborder Market

In 2013, there were, on average, 1,138 daily scheduled transborder flights operated between Canada and the United States across the industry. Toronto Pearson Airport, Air Canada's largest hub, is the world's largest originator of flights into the United States.

Air Canada is the largest provider of scheduled passenger services in the U.S. transborder market. Based on OAG data, during the period from January 1, 2013 to December 31, 2013, Air Canada, together with its Contracted Carriers, provided more U.S. transborder scheduled capacity than any other airline with an estimated market share of approximately 36% based on ASMs.

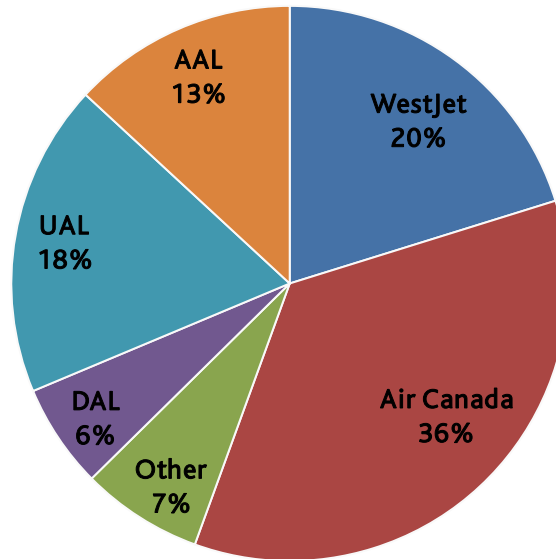
Air Canada, together with its Contracted Carriers, carries more passengers, serves more non-stop destinations and provides more flights in the U.S. transborder market than any other airline. Competition in the U.S. transborder market is primarily from U.S. network carriers and their regional affiliates and from WestJet. The U.S. network carriers tend to operate flights between the United States and Canada into their hubs, connecting to flights to other U.S. destinations. U.S. network carriers with U.S. transborder operations include Alaska Airlines, American Airlines, United Airlines and Delta Airlines. In 2013, Air Canada, together with its Contracted Carriers, provided service to 54 U.S. destinations from Canada, while U.S. network carriers provided service to 24 U.S. destinations from Canada and WestJet provided service to 21 U.S. destinations.

In 2013, Air Canada transferred its 15 Embraer 175 aircraft from the mainline fleet to Sky Regional who operates these aircraft on Air Canada's behalf under a capacity purchase agreement. These aircraft continue flying on U.S. short-haul routes, primarily from Toronto and Montreal to destinations in the Northeast U.S, as well from Toronto to Texas. As part of the airline's diversification strategy, in December 2013, Air Canada concluded a memorandum of understanding to expand its relationship and amend its capacity purchase agreement with Air Georgian. Air Georgian has been selected to operate a number of regional routes starting in mid-2014, including transborder routes, using Canadair regional jet aircraft.

Canadian low-cost carriers also operate U.S. transborder services and have expressed an intention to further expand these operations in the future.

The following chart illustrates the estimated share of the overall U.S. transborder scheduled capacity of Air Canada, together with its Contracted Carriers, as measured by ASMs.

### Estimated Transborder Scheduled Capacity Market Share



(1) Source: OAG data, based on ASMs during the period from January 1, 2013 to December 31, 2013; represents the estimated share of the overall transborder scheduled capacity of Air Canada and its Contracted Carriers. The estimated share of the overall transborder scheduled capacity of the other carriers presented also includes the transborder scheduled capacity of their respective affiliated or contracted regional carrier(s), when applicable.

(2) AAL = American Airlines; DAL = Delta Air Lines; UAL = United Airlines.

### International Market

Air Canada principally services the international market from three strategically-positioned airports, which are further described below:

- Toronto Pearson Airport, Canada's largest airport, is located in Canada's largest city and offers regular non-stop flights to numerous destinations in Europe, Central America/Caribbean/South America and Asia. Toronto Pearson Airport offers, on average, approximately 544 daily departures, of which 15% are to international destinations.
- Montreal Trudeau Airport is located in Canada's second largest city, and offers regular non-stop service to several European destinations and certain Central American/Caribbean/Mexico destinations. Montreal Trudeau Airport offers, on average, approximately 254 daily departures, of which 12% are to international destinations.
- Vancouver International Airport, located in Canada's third largest city, is strategically positioned on Canada's west coast and acts as a gateway to many Asian destinations. Vancouver International Airport offers, on average, approximately 296 daily departures, of which 9% are to international destinations.

Air Canada is Canada's largest provider of scheduled passenger services in the international market to and from Canada and has a broad portfolio of international route rights. Based on OAG data, during the period from January 1, 2013 to December 31, 2013, Air Canada provided more international scheduled capacity in the international market to and from Canada than any other airline with an estimated market share of approximately 37% based on ASMs. Air Canada is currently the only Canadian scheduled carrier with routes from Canada to Asia, although a number of Asian carriers service Canadian destinations. Air Canada is also the sole Canadian scheduled carrier offering flights to South America, and no South American scheduled network carrier currently provides non-stop service from South America to Canada.

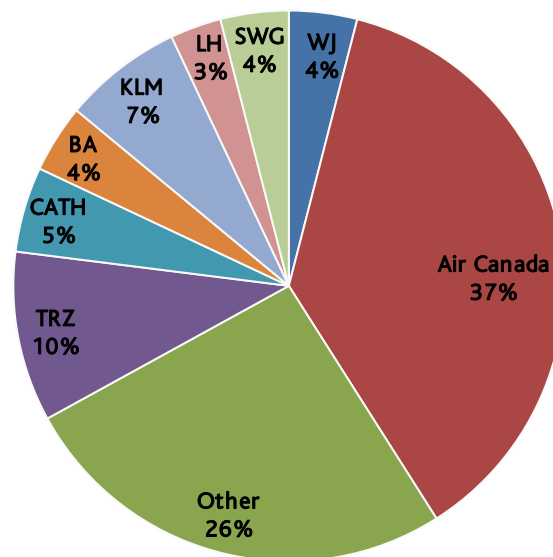
Canadian low-cost carriers as well as Canadian charter airlines and tour operators, such as Transat A.T. Inc. ("Transat") and Sunwing Airlines ("Sunwing"), also operate services to Mexico and the Caribbean and certain of them have expressed an intention to further expand these operations in the future. In 2013, WestJet, Sunwing and Transat provided service to 39, 19 and 16 destinations, respectively, to Mexico and the Caribbean. Air Canada *rouge* will enable Air Canada to compete more effectively against these low-cost carriers serving international leisure destinations.

Air Canada *rouge*, Air Canada's lower cost leisure airline, launched its operations on July 1, 2013 with a start-up fleet of four aircraft transferred from Air Canada's mainline fleet – two Boeing 767-300ER and two Airbus A319 aircraft were operated to Athens, Edinburgh, Venice, the Dominican Republic, Cuba, Costa Rica and Jamaica.

In the transatlantic and transpacific markets, Air Canada competes primarily with foreign network carriers and, to a lesser extent, with charter carriers on higher density routes during peak travel seasons. In addition, U.S. network carriers compete by flying Canadian passengers through their hubs to destinations in international markets.

The following chart illustrates the estimated share of the overall international scheduled capacity provided by Air Canada and other airlines as measured by ASMs.

### Estimated International Scheduled Capacity Market Share



(1) Source: OAG data, based on ASMs during the period from January 1, 2013 to December 31, 2013; represents the estimated share of the overall international scheduled capacity of Air Canada. The estimated share of the overall international scheduled capacity of the other carriers presented also includes the international scheduled capacity of their respective affiliated or contracted regional carrier(s), when applicable.

(2) KLM = Air France KLM; LH = Lufthansa; BA = British Airways; CATH = Cathay Pacific Airways; TRZ = Transat A.T. Inc.; WJ = Westjet Airlines; SWG = Sunwing Airlines.

### RISK FACTORS

For a description of risk factors associated with Air Canada and its business, refer to section 18 "Risk Factors" of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference.

## MARKET FOR SECURITIES

The Variable Voting Shares and the Voting Shares are traded on the TSX under the trading symbols "AC.A" and "AC.B", respectively. The following table sets forth the price range and trading volume of the Variable Voting Shares and the Voting Shares as reported by the TSX for the months of January to, and including, December 2013, as applicable.

2013	Variable Voting Shares (AC.A)				Voting Shares (AC.B)			
	High	Low	Average Daily Trading Volume	Total Monthly Volume	High	Low	Average Daily Trading Volume	Total Monthly Volume
January	\$ 2.50	\$ 1.70	56,423	1,241,305	\$ 2.51	\$ 1.75	1,737,581	38,226,777
February	\$ 2.49	\$ 2.22	84,499	1,605,488	\$ 2.51	\$ 2.22	1,077,175	20,466,320
March	\$ 3.16	\$ 2.38	45,809	915,177	\$ 3.13	\$ 2.40	1,172,642	23,448,338
April	\$ 3.39	\$ 2.45	102,325	2,124,553	\$ 3.40	\$ 2.46	2,170,502	47,717,940
May	\$ 3.00	\$ 1.96	68,961	1,517,140	\$ 3.00	\$ 1.96	2,401,647	53,266,228
June	\$ 2.69	\$ 2.01	92,665	1,853,304	\$ 2.68	\$ 2.00	2,802,793	56,055,850
July	\$ 2.49	\$ 2.08	22,344	491,562	\$ 2.47	\$ 2.07	1,152,536	25,355,799
August	\$ 2.97	\$ 2.12	127,319	2,673,701	\$ 2.96	\$ 2.12	1,594,667	33,588,015
September	\$ 3.73	\$ 2.76	241,531	4,358,700	\$ 3.72	\$ 2.76	3,562,070	71,241,997
October	\$ 5.81	\$ 3.43	307,070	6,755,539	\$ 5.80	\$ 3.45	3,669,758	80,734,680
November	\$ 7.60	\$ 5.16	184,262	3,869,496	\$ 7.59	\$ 5.125	4,024,302	84,510,344
December	\$ 8.00	\$ 6.84	142,376	2,847,510	\$ 8.00	\$ 7.19	2,278,551	45,571,017

## TRANSFER AGENT AND REGISTRAR

The transfer agent and registrar for the Variable Voting Shares and Voting Shares of Air Canada is CST Trust Company with its principal offices in Montreal, Toronto, Vancouver, Calgary and Halifax.

## DIVIDEND RECORD

The Corporation has not declared or paid dividends on its Voting Shares and Variable Voting Shares for any of the financial years ended December 31, 2013, 2012 and 2011.

Air Canada's current policy is to reinvest earnings in order to finance the growth and development of its business and to improve liquidity levels and pay down debt. Agreements entered into in relation to the private offerings of senior secured notes described in the section entitled "Significant Financing Transactions" in this AIF and the agreement with the Government of Canada to extend Air Canada's pension funding arrangements to December 31, 2020 (which is described in section 9.7 of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference), and certain other agreements of Air Canada may restrict Air Canada's ability to declare and pay dividends. As a result, Air Canada does not expect to pay dividends in the foreseeable future. Any future determination to pay cash dividends is subject to legal restrictions applicable at the time to Air Canada, at the discretion of Air Canada's Board of Directors and will depend on Air Canada's financial condition, results of operations, capital requirements, restrictive covenants in contracts and such other factors as Air Canada's Board of Directors deems relevant.

## DESCRIPTION OF CAPITAL STRUCTURE

The authorized share capital of Air Canada is comprised of an unlimited number of Variable Voting Shares and Voting Shares. As at March 27, 2014, 38,808,819 Class A Variable Voting Shares and 247,071,520 Class B Voting Shares were issued and outstanding. The following summary describes the rights, privileges, restrictions and conditions that are attached to the Variable Voting Shares and the Voting Shares. This summary does not purport to be complete and is subject to, and is qualified in its entirety by, reference to the terms of Air Canada's articles of amalgamation, as amended.

### **Variable Voting Shares**

#### ***Voting***

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

The Variable Voting Shares may only be held, beneficially owned or controlled, directly or indirectly, by persons who are not Canadians, as such term is defined in the CTA ("Qualified Canadians") and are entitled to one vote per Variable Voting Share unless (i) the number of Variable Voting Shares outstanding, as a percentage of the total number of votes attaching to all issued and outstanding voting shares, exceeds 25% (or any higher percentage that the Governor in Council may by regulation specify) or (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares at any meeting exceeds 25% (or any higher percentage that the Governor in Council may by regulation specify) of the total number of votes that may be cast at such meeting. If either of the above noted thresholds would otherwise be surpassed at any time, the vote attached to each Variable Voting Share will decrease proportionately such that (i) the Variable Voting Shares as a class do not carry more than 25% (or any higher percentage that the Governor in Council may by regulation specify) of the aggregate votes attached to all issued and outstanding voting shares of Air Canada and (ii) the total number of votes cast by or on behalf of holders of Variable Voting Shares at any meeting do not exceed 25% (or any higher percentage that the Governor in Council may by regulation specify) of the votes that may be cast at such meeting.

The Government of Canada's Bill C-10, the *Budget Implementation Act 2009*, contains provisions whereby the provisions relating to voting securities in the ACPPA would be repealed and the CTA would be amended to provide the Governor in Council with flexibility to increase the foreign ownership limit from the existing 25% level to a maximum of 49%. These provisions will come into force on a date to be fixed by order of the Governor in Council made on the recommendation of the Minister of Finance, in the case of the ACPPA, and on the recommendation of the Minister of Transport, in the case of the CTA.

#### ***Dividends***

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

#### ***Subdivision or Consolidation***

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

### ***Rights upon Liquidation, Dissolution or Winding Up***

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

### ***Conversion***

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

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

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

There shall be no right to convert the Variable Voting Shares into Voting Shares or to convert Voting Shares into Variable Voting Shares, except in accordance with the conversion procedure set forth in the Air Canada articles of amalgamation.

### ***Constraints on Ownership of Shares***

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

### ***Voting Shares***

#### ***Voting***

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

#### ***Dividends***

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

### ***Subdivision or Consolidation***

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

### ***Rights upon Liquidation, Dissolution or Winding Up***

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

### ***Conversion***

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

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

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

There shall be no right to convert the Variable Voting Shares into Voting Shares or to convert Voting Shares into Variable Voting Shares, except in accordance with the conversion procedure set forth in the Air Canada articles of amalgamation.

### ***Constraints on Ownership of Shares***

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

### ***Declaration as to Canadian Status***

Air Canada's articles of amalgamation, as amended, provide that: (i) the Voting Shares may only be held, beneficially owned and controlled, directly or indirectly, by persons who are Qualified Canadians; and (ii) the Variable Voting Shares may only be held, beneficially owned or controlled, directly or indirectly, by persons who are not Qualified Canadians.

### ***Repurchase of Shares***

Air Canada may be allowed, from time to time, to purchase shares for cancellation in accordance with applicable securities legislation and the rules prescribed under applicable stock exchange or regulatory policies. Any such repurchase would constitute an "issuer bid" under Canadian provincial securities legislation and would be conducted in accordance with the applicable requirements thereof. Any future decision to purchase shares for cancellation will depend on Air Canada's financial condition, results of operations, capital requirements, restrictive covenants in contracts and such other factors as Air Canada's Board of Directors deems relevant.

Under the agreement reached with the Government of Canada in March 2013 relating to Air Canada pension funding arrangements in Canada (which is further described in section 9.7 of Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference), Air Canada is prohibited from purchasing its Shares. Agreements entered into in relation to the private offerings of senior secured notes described in the section entitled "Significant Financing Transactions" in this AIF and other agreements of Air Canada may also restrict Air Canada's ability to purchase Shares.

### **Information and Reports**

Air Canada or its transfer agent will furnish to shareholders, in accordance with applicable securities laws, all financial statements of Air Canada (including quarterly and annual financial statements) and other reports as are from time to time required by applicable law, including prescribed forms needed for the completion of shareholders' tax returns under the *Tax Act* and equivalent provincial legislation.

Prior to each meeting of shareholders, the Board of Directors of Air Canada will provide to the shareholders (along with notice of the meeting) a form of proxy and all information as is required by applicable law and the rules of the TSX to be provided to shareholders.

The directors and officers of Air Canada are required to file insider reports and comply with insider trading provisions under applicable Canadian securities legislation in respect of trades made by such persons in securities of Air Canada.

### **Air Canada Shareholder Rights Plan**

The Board of Directors of Air Canada approved a shareholder rights plan on March 30, 2011 (the "Rights Plan"). The Rights Plan was designed to foster fair treatment of all shareholders of Air Canada in connection with any take-over bid for Air Canada. The plan was approved by the shareholders of Air Canada at the annual and special shareholder meeting held on May 5, 2011.

The Rights Plan creates one right in respect of each Variable Voting Share and Voting Share of Air Canada outstanding as at March 30, 2011 or subsequently issued. Until the separation time, which typically occurs at the time of an unsolicited take-over bid, whereby an Acquiring Person (as defined in the Rights Plan) acquires or attempts to acquire 20% or more of Air Canada's Variable Voting Shares or 20% or more of Air Canada's Voting Shares, the rights are not separable from the shares, are not exercisable and no separate rights certificates are issued.

Under the Rights Plan approved on March 30, 2011, each right, other than those held by an Acquiring Person and certain of its related parties, entitles the holder in certain circumstances following the acquisition by an Acquiring Person of 20% or more of the Variable Voting Shares or 20% or more of the Voting Shares of Air Canada (otherwise than through the "Permitted Bid" requirements of the Rights Plan) to purchase from Air Canada \$200 worth of Variable Voting Shares or Voting Shares for \$100 (i.e. at a 50% discount). Upon such exercise, holders of rights beneficially owned and controlled by Qualified Canadians would receive Voting Shares and holders of rights beneficially owned or controlled by persons who are not Qualified Canadians would receive Variable Voting Shares.

In 2012, the shareholders of Air Canada approved amendments to the Rights Plan. Subject to certain exceptions identified in the Rights Plan, the Rights Plan, as currently amended, would be triggered in the event of an offer to acquire 20% or more of the outstanding Class A variable voting shares and Class B voting shares of Air Canada calculated on a combined basis, instead of 20% or more of the outstanding Class A variable voting shares or Class B voting shares calculated on a per class basis as was the case under the Rights Plan prior to the amendments that came into effect in 2012.

The amendments to the Rights Plan were proposed in order to render effective a decision issued by Canadian securities regulatory authorities (pursuant to an application of Air Canada) that effectively treats Air Canada's Class A variable voting shares and Class B voting shares as a single class for the purposes of applicable take-over bid requirements and early warning reporting requirements contained under Canadian securities laws. A copy of the decision is available under Air Canada's profile at [www.sedar.com](http://www.sedar.com).



The Rights Plan, originally approved at Air Canada's 2011 annual and special shareholder meeting, is designed to provide Air Canada's shareholders and the Board of Directors additional time to assess an unsolicited take-over bid for the company and, where appropriate, to give the Board of Directors additional time to pursue alternatives for maximizing shareholder value. It also encourages fair treatment of all shareholders by providing them with an equal opportunity to participate in a take-over bid.

The Rights Plan is scheduled to expire at the close of business on the date immediately following the date of Air Canada's annual and special meeting of shareholders to be held on May 15, 2014, unless renewed at that meeting or terminated earlier in accordance with the terms of the Rights Plan.

## DIRECTORS AND OFFICERS

### Directors

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

Name and Municipality of Residence	Principal Occupation	Director Since
Thomas Birks <sup>(1)(2)(3)</sup> Montreal, Québec	President, Birinco Inc.	February 7, 2013
Christie J.B. Clark <sup>(2)(4)</sup> Toronto, Ontario	Corporate Director	June 27, 2013
Michael M. Green <sup>(3)(5)</sup> Radnor, Pennsylvania	Chief Executive Officer and Managing Director Tenex Capital Management, a private investment firm	March 30, 2009
Jean Marc Huot <sup>(3)</sup> Montreal, Québec	Partner, Stikeman Elliott LLP	May 8, 2009
Joseph B. Leonard <sup>(3)(4)(5)</sup> Minneapolis, Minnesota	Corporate Director	May 21, 2008
David I. Richardson <sup>(1)(4)(6)</sup> Grafton, Ontario	Corporate Director	November 15, 2006
Roy J. Romanow <sup>(1)(3)</sup> Saskatoon, Saskatchewan	Senior Fellow, Public Policy University of Saskatchewan	February 9, 2010
Calin Rovinescu Montreal, Québec	President and Chief Executive Officer Air Canada	April 1, 2009
Vagn Sørensen <sup>(2)(4)(5)</sup> London, United Kingdom	Corporate Director	November 15, 2006
Annette Verschuren <sup>(2)(4)(5)</sup> Toronto, Ontario	Chair and Chief Executive Officer NRStor Inc.	November 12, 2012

(1) Member of the Governance and Corporate Matters Committee.

(2) Member of the Audit, Finance and Risk Committee.

(3) Member of the Pension Committee.

(4) Member of the Nominating Committee.

(5) Member of the Human Resources and Compensation Committee.

(6) Prior to completion of the initial public offering of Air Canada on November 17, 2006, Mr. Richardson was reconfirmed as a director of Air Canada on November 15, 2006. He was initially appointed a director of Air Canada on September 30, 2004 and continued to hold such position up to and since the completion of Air Canada's initial public offering. Mr. Richardson became Chairman of the Board of Air Canada on January 1, 2008.

Unless otherwise indicated below, each of the directors has held the occupation listed above for more than five years. Mr. Clark was Chief Executive Officer of PricewaterhouseCoopers LLP from 2005 to 2011. Mr. Green was Managing Director at Cerberus Capital Management, L.P. from 2004 to 2009. Mr. Leonard was Interim Chief Executive Officer of Walter Energy, Inc. from 2010 to 2011. Ms. Verschuren was the President of The Home Depot Canada from 1996 to 2011.

## Officers

The Board of Directors of Air Canada may from time to time appoint one or more officers of Air Canada. A majority of the officers of Air Canada shall be residents of Canada within the meaning of the *Tax Act* and Canadians within the meaning of the CTA.

The name, municipality of residence and position held with Air Canada of each of the officers are, as of the date hereof, as set forth below:

<b>Name and municipality of Residence</b>	<b>Position with Air Canada</b>	<b>Officer since</b>
David I. Richardson <sup>(1)</sup> Grafton, Ontario	Chairman of the Board	January 1, 2008
Calin Rovinescu <sup>(2)</sup> Montreal, Québec	President and Chief Executive Officer	April 1, 2009
Klaus Goersch Oakville, Ontario	Executive Vice President and Chief Operating Officer	October 1, 2012
Michael Rousseau St. Lambert, Quebec	Executive Vice President and Chief Financial Officer	October 22, 2007
Benjamin M. Smith Toronto, Ontario	Executive Vice President and Chief Commercial Officer	April 26, 2004
Lise Fournel Beaconsfield, Québec	Senior Vice President and Chief Information Officer	April 10, 1995
Kevin C. Howlett Delta, British Columbia	Senior Vice President, Regional Markets	March 18, 2002
David J. Shapiro Hampstead, Québec	Senior Vice President and Chief Legal Officer	November 12, 2004
Alan D. Butterfield Beaconsfield, Québec	Vice President, Air Canada Maintenance and Engineering	February 19, 2007
Nick Careen Candiac, Québec	Vice President, Airports, Call Centers and Customer Relations	June 1, 2009
Yves Dufresne Montreal, Québec	Vice President, Alliances and Regulatory Affairs	April 26, 2004
Marcel Forget Montreal, Québec	Vice President, Network Planning	April 8, 2009
Zeina Gedeon Dollard des Ormeaux, Québec	Vice President, Sales Canada and Product Distribution	March 1, 2012
Lucie Guillemette Beaconsfield, Québec	Vice President, Revenue Management and International Sales	February 6, 2008
Carolyn M. Hadrovic Beaconsfield, Québec	Corporate Secretary	February 16, 2006

<b>Name and municipality of Residence</b>	<b>Position with Air Canada</b>	<b>Officer since</b>
Chris Isford Winnipeg, Manitoba	Vice President and Controller	November 1, 2006
Amos Kazzaz, Saint-Laurent, Québec	Vice President, Financial Planning and Analysis	May 3, 2010
Craig Landry Montreal, Québec	Vice President, Marketing	August 1, 2010
Priscille LeBlanc Toronto, Ontario	Vice President, Corporate Communications	November 8, 2007
Arielle Meloul-Wechsler Montreal, Quebec	Vice President, Human Resources	September 18, 2013
Scott Morey Georgetown, Ontario	Vice President, Labour Relations	January 15, 2007
Jim Tabor Oakville, Ontario	Vice President, System Operations Control	May 8, 2013
Lise-Marie Turpin Pointe-Claire, Québec	Vice President, Cargo	March 1, 2012
Derek Vanstone Toronto, Ontario	Vice President, Corporate Strategy, Industry and Government Affairs	September 10, 2012
Michael Friisdahl Toronto, Ontario	President and Chief Executive Officer, Leisure Group	October 1, 2012

- (1) *Mr. Richardson is a non-executive officer of Air Canada. Mr. Richardson's principal occupation is a corporate director.*  
(2) *Mr. Rovinescu was also an executive officer of Air Canada from 2000 to 2004.*

Unless otherwise indicated below, each of the officers has held a position with Air Canada similar to that listed above for more than five years. Mr. Goersch was Executive Vice President, Operations and Customer Service of AirTran Airways from 2010 to 2012 and Senior Vice President, Operations of AirTran Airways from 2008 to 2010. Ms. Gedeon was President and Chief Executive Officer of Air Canada Vacations from 2007 to 2012. Mr. Howlett was Senior Vice President, Employee Relations of Air Canada from 2006 to 2013. Mr. Kazzaz was Chief Operating Officer of ZAP! from 2007 to 2010. Mr. Landry was Senior Vice President, Commercial of Aeroplan Canada from 2009 to 2010 and Senior Vice President, Corporate Development of Groupe Aeroplan from 2008 to 2009. Ms. Meloul-Wechsler was Senior Director, Human Resources of Air Canada from 2011 to 2013 and Assistant General Counsel and Director of Legal Services of Air Canada from 2005 to 2011. Mr. Tabor was Senior Operations Advisor for AirTran Airways from 2012 to 2013 (during the transition to Southwest Airlines) and Vice President, Operations for AirTran Airways from 2005 to 2012. Ms. Turpin was Managing Director of Air Canada Cargo from 2008 to 2012. Mr. Vanstone was Deputy Chief of Staff to the Prime Minister of Canada from 2010 to 2012 and Chief of Staff to the Minister of Finance from 2007 to 2010. Mr. Friisdahl was Chief Executive Officer of Thomas Cook North America from 2003 to 2012.

As at March 27, 2014, the directors and officers mentioned above, as a group, owned, or had control or direction over, directly or indirectly, 1,320,975 Class B Voting Shares representing approximately 0.53% of the outstanding Class B Voting Shares and 184,451 Class A Variable Voting Shares representing approximately 0.48% of the outstanding Class A Variable Voting Shares.

#### **Cease Trade Orders, Bankruptcies, Penalties or Sanctions**

To the knowledge of Air Canada, no director or executive officer of Air Canada is, as at the date of this AIF, or was, within 10 years before the date of this AIF, a director, chief executive officer or chief financial officer of any company that, (a) was subject to a cease trade order, an order similar to a cease trade order or an order that denied the relevant company access to any exemption under securities legislation, that was in effect for a period of more than 30 consecutive days (an "Order") that was issued while the director or executive officer of Air Canada was acting in the capacity as director, chief executive officer or chief financial officer, or (b) was subject to an Order that was issued after the director or executive officer of Air Canada ceased to be a director, chief executive officer or chief financial officer and which resulted from an event that occurred while that person was acting in the capacity as director, chief executive officer or chief financial officer.

To the knowledge of Air Canada, no director or executive officer of Air Canada, or a shareholder holding a sufficient number of securities of Air Canada to affect materially the control of Air Canada, (a) is, as at the date of this AIF, or has been within the 10 years before the date of this AIF, a director or executive officer of any company that, while that person was acting in that capacity, or within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets; or (b) has, within the 10 years before the date of the AIF, become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or become subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director, executive officer or shareholder of Air Canada, except for:

- (i) Michael M. Green was a director of Anchor Glass Container Corporation when it filed a voluntary petition for reorganization under Chapter 11 of the U.S. Bankruptcy Code in August 2005;
- (ii) Calin Rovinescu was an executive officer of Air Canada when it filed for protection under the CCAA on April 1, 2003;
- (iii) Lise Fournel was an executive officer of Air Canada when it filed for protection under the CCAA on April 1, 2003;
- (iv) Kevin C. Howlett was an executive officer of Air Canada when it filed for protection under the CCAA on April 1, 2003;
- (v) Alan D. Butterfield was appointed Vice President, Line and Airframe Maintenance at United Airlines in March 2004 while United Airlines and its parent company, UAL Corp. were operating under bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code;

- (vi) Amos Kazzaz was Vice President, Corporate Real Estate at United Airlines when its parent company, UAL Corp. filed for protection under Chapter 11 of the U.S. Bankruptcy Code in December 2002; and

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

## AUDIT, FINANCE AND RISK COMMITTEE

### Audit Committee Charter

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

### Composition of Audit Committee

As of the date hereof, the Audit Committee of Air Canada consists of Christie J.B. Clark (chair), Thomas Birks, Vagn Sørensen and Annette Verschuren. Each member of the Audit Committee is independent and financially literate as defined under National Instrument 52-110 – *Audit Committees*.

### Relevant Education and Experience of Audit Committee Members

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

- (i) Christie J.B. Clark is a corporate director. Mr. Clark is a director of Brookfield Office Properties Inc., IGM Financial Inc. and Loblaw Companies Limited, and a trustee of Choice Properties Real Estate Investment Trust. From 2005 to 2011, Mr. Clark was the Chief Executive Officer and senior partner of PricewaterhouseCoopers LLP. Prior to being elected as Chief Executive Officer, Mr. Clark was a National Managing Partner and a member of the firm's Executive Committee from 2001 to 2005. Mr. Clark is also Chair of the board of the Canadian Partnership Against Cancer Corporation, Chair of the Finance Committee of Alpine Canada and a member of the Advisory Council of Queen's University School of Business. Mr. Clark graduated from Queen's University with a Bachelor of Commerce degree and the University of Toronto with a Master of Business Administration degree. He is a Fellow Chartered Professional Accountant.
- (ii) Thomas Birks is the President of Birinco Inc., a merchant bank with investment portfolios ranging from private equity to passive investments. From 1985 to 1989, Mr. Birks served as President of Henry Birks and Sons Ltd. Mr. Birks has extensive global experience having worked in various countries including Australia, Japan and South Africa for Coles-Myer, Mitsubishi Bank, and Van Zwam, Vladykin and Douglas, respectively. He previously served as Chair of Viterra Inc., as well as Chair and board member of numerous corporations, educational institutions, hospitals and foundations. Mr. Birks graduated from McGill University with a Bachelor of Arts degree and holds a Master of Business Administration degree from the Harvard Business School. He has also studied at the University of Lausanne, the University of Fribourg and the University of Paris.
- (iii) Vagn Sørensen is a corporate director. Mr. Sørensen is the Chairman of FLSmidth & Co. A/S, Scandic Hotels AB, Select Service Partner Plc U.K., TDC A/S and Automic Software GmbH, and Vice Chairman of DFDS A/S. Mr. Sørensen is a director of Braganza AS, Lufthansa Cargo AG, Nordic Aviation Capital A/S and Royal Caribbean Cruises Ltd. Mr. Sørensen is also a Senior Industrial Advisor with EQT Partners, a private equity fund. Mr. Sørensen was previously President and Chief Executive Officer of Austrian Airlines Group from 2001 to 2006, and held various senior commercial positions and served as Deputy Chief Executive Officer with SAS Scandinavian Airlines System. Mr. Sørensen has served as Chairman of the Association of European Airlines, member of the IATA Board of Governors and member of the Board of Vienna Stock Exchange. Mr. Sørensen holds a Master in Economics and Business degree from Aarhus Business School of Business, University of Aarhus, Denmark.

- (iv) Annette Verschuren is the Chair and Chief Executive Officer of NRStor Inc., a new venture focused on commercializing energy storage technologies. From 1996 to 2011, Ms. Verschuren was the President of The Home Depot Canada and prior to joining The Home Depot Canada, Ms. Verschuren was the President and co-owner of Michaels of Canada. Previously, Ms. Verschuren was the Vice President, Corporate Development of Imasco Ltd. and the Executive Vice President of Canada Development Investment Corporation. Ms. Verschuren is a board member of Liberty Mutual Insurance Group, Saputo Inc. and the North West Company. She also serves as Chancellor of Cape Breton University and is a board member of numerous non-profit organizations including the CAMH Foundation, the Conference Board of Canada and Habitat for Humanity's national leadership council. Ms. Verschuren holds honorary doctorate degrees from Dalhousie University, Mount Saint Vincent University, Carleton University and St. Francis Xavier University where she also earned a Bachelor of Business Administration degree.

#### Pre-approval Policies and Procedures

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

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

#### Auditors' Fees

PricewaterhouseCoopers LLP has served as Air Canada's auditing firm since April 26, 1990. Fees payable for the years ended December 31, 2013 and December 31, 2012 to PricewaterhouseCoopers LLP and its affiliates are \$2,981,707 and \$2,725,564, respectively, as detailed below.

	<u>Year ended</u> <u>December 31, 2013</u>	<u>Year ended</u> <u>December 31, 2012</u>
Audit fees	\$1,777,208	\$1,769,465
Audit-related fees	606,332	612,639
Tax fees	61,530	131,558
All other fees	<u>536,637</u>	<u>211,902</u>
	<u><b>\$2,981,707</b></u>	<u><b>\$2,725,564</b></u>

The nature of each category of fees is described below:

#### Audit fees

Audit fees were paid for professional services rendered for the audit of Air Canada's annual consolidated financial statements and for services that are normally provided in connection with statutory and regulatory filings or engagements related to the annual consolidated financial statements, including review engagements performed on the interim consolidated financial statements of Air Canada.

#### Audit-related fees

Audit-related fees were paid for professional services related to the audit of the non-consolidated financial statements of Air Canada, pension plan audits, audits of subsidiary companies, where required, specified procedures reports and other audit engagements not related to the consolidated financial statements of Air Canada.

### Tax fees

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

### All other fees

Other fees were paid for translation services, advisory services and fees related to the auditors' involvement with offering documents, if any. In 2013, two offering documents were concluded, which related to the EETC aircraft financing and the private offerings of new senior notes and a new credit facility, both of which are described under the heading "Significant Financing Transactions" in this AIF. No such offerings were completed in 2012.

## **INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS**

Other than as described elsewhere in this AIF, none of the (i) directors or executive officers of Air Canada, (ii) shareholders of Air Canada, that, to the knowledge of Air Canada, beneficially own, or control, directly or indirectly, more than 10% of any class of shares of Air Canada, or (iii) any associate or affiliate of the persons referred to in (i) and (ii), has or has had any material interest, direct or indirect, in any transaction during the three most recently completed financial years or the current financial year that has materially affected or is reasonably expected to materially affect Air Canada or any of its subsidiaries.

## **LEGAL PROCEEDINGS**

A description of certain legal proceedings to which Air Canada is a party appears under the heading "Current Legal Proceedings" in section 18 entitled "Risk Factors" in Air Canada's 2013 MD&A, which section is hereby incorporated into the AIF by this reference.

## **MATERIAL CONTRACTS**

The contracts that are material to the Corporation and that were entered into within the year ended December 31, 2013, or before such year but which are still in effect, and which are required to be filed with Canadian securities regulatory authorities in accordance with section 12.2 of National Instrument 51-102 - Continuous Disclosure Obligations, are as follows:

- (i) the Indentures dated September 2013 governing the First Lien Notes and the Second Lien Notes, and the Collateral Trust Agreement dated September 2013 governing the holding of collateral securing the First Lien Notes and the Second Lien Notes;
- (ii) the Loan Agreement dated September 2013 governing the New Credit Facility;
- (iii) the Jazz CPA; and
- (iv) the Aircraft General Terms Agreement AGTA-ACN and related agreements between Boeing and Air Canada dated November 4, 2005.

## **EXPERTS**

The Corporation's independent auditors are PricewaterhouseCoopers LLP, Chartered Accountants. PricewaterhouseCoopers LLP has advised that they are independent with respect to the Corporation within the meaning of the Code of Ethics of the Ordre des comptables agréés du Québec.

## ADDITIONAL INFORMATION

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of Air Canada's securities and securities authorized for issuance under equity compensation plans is contained in Air Canada's management proxy circular for its 2013 annual meeting of shareholders held on June 27, 2013 and will be contained in Air Canada's management proxy circular for its 2014 annual and special meeting of shareholders to be held on May 15, 2014. .

Additional financial information is provided in Air Canada's consolidated financial statements for the year ended December 31, 2013 and Air Canada's 2013 MD&A. These documents and additional information related to Air Canada are available on Air Canada's website at [aircanada.com](http://aircanada.com) or on SEDAR at [www.sedar.com](http://www.sedar.com).

The following documents can be obtained by sending your request to the Corporate Secretary of Air Canada, at Air Canada Centre, P.O. Box 14000, Station Airport, Dorval, Québec, H4Y 1H4:

- (i) this AIF, together with any document incorporated herein by reference;
- (ii) the Consolidated Financial Statements of Air Canada as at and for the year ended December 31, 2013, including the auditor's report and notes related thereto, Air Canada's 2013 MD&A, and any interim financial statements filed after the audited financial statements for Air Canada's most recently completed financial year; and
- (iii) any other documents that are incorporated by reference into a short form prospectus pursuant to which securities of Air Canada are in the course of a distribution.

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



## GLOSSARY OF TERMS

"**ACE**" means ACE Aviation Holdings Inc., a corporation incorporated under the CBCA;

"**ACPA**" means the Air Canada Pilots Association;

"**ACPPA**" means the *Air Canada Public Participation Act*, as amended;

"**Adjusted net income**" means the consolidated net income (loss) of the Corporation attributable to shareholders of Air Canada adjusted to remove the effects of (to the extent included in consolidated net income (loss)) foreign exchange, net financing income (expense) relating to employee benefits, mark-to-market adjustments on derivatives and other financial instruments recorded at fair value, and unusual items;

"**AE**" means Accountable Executive;

"**Aeroplan**" means Aimia Canada Inc.;

"**Air Canada's 2013 MD&A**" means Air Canada's 2013 Management's Discussion and Analysis of Results of Operations and Financial Condition dated February 12, 2014;

"**Air Canada Cargo**" means the cargo services division of Air Canada;

"**Air Canada Vacations**" means Touram Limited Partnership (doing business as Air Canada Vacations), a limited partnership established under the laws of the Province of Québec;

"**Air Canada rouge**" means Air Canada *rouge* LP (doing business as Air Canada *rouge*), a limited partnership established under the laws of the Province of Quebec;

"**Air Georgian**" means Air Georgian Limited;

"**Available Seat Miles or ASMs**" means the total number of seats available for passengers multiplied by the miles flown;

"**Audit Committee**" means the Audit, Finance and Risk Committee of Air Canada;

"**Aveos**" means Aveos Fleet Performance Inc.;

"**Boeing**" means The Boeing Company;

"**Canadian Airlines**" means Canadian Airlines International Ltd.;

"**CARICOM**" means the Caribbean Community and Common Market;

"**CASM**" means cost per available seat mile;

"**CATSA**" means the Canadian Air Transport Security Agency;

"**CBCA**" means the *Canada Business Corporations Act*, as amended;

"**CBP**" means the U.S. Customs and Border Protection;

"**CBSA**" means the Canada Border Services Agency;

"**CCAA**" means the *Companies' Creditors Arrangement Act*, as amended;

"**CDP**" means the Carbon Disclosure Project;

**"Contracted Carriers"** means Jazz, Sky Regional, Air Georgian and other airlines operating flights on behalf of Air Canada under commercial agreements with Air Canada and which operate under the brand name "Air Canada Express";

**"Corporation"** shall have the meaning ascribed thereto under "Explanatory Notes";

**"CTA"** means the *Canada Transportation Act*, as amended;

**"CTP"** means Air Canada's cost transformation program which was launched in mid-2009;

**"CUPE"** means the Canadian Union of Public Employees;

**"DBRS"** means DBRS Limited;

**"EBITDAR"** means earnings before interest, taxes, depreciation, amortization and impairment, and aircraft rent;

**"Embraer"** means EMBRAER – Empresa Brasileira de Aeronautica S.A.;

**"ESTA"** means Electronic System for Travel Authorization;

**"EU ETS"** means European Emission Trading Scheme;

**"Fitch"** means Fitch Ratings, Inc.;

**"FTE"** shall have the meaning ascribed thereto under employees;

**"GAAP"** means generally accepted accounting principles in Canada;

**"GHG"** means greenhouse gas;

**"GTAA"** means the Greater Toronto Airport Authority;

**"IAMAW"** means the International Association of Machinists and Aerospace Workers;

**"IATA"** means the International Air Transport Association;

**"IBT"** means the International Brotherhood of Teamsters;

**"ICAO"** means the International Civil Aviation Organization;

**"Independent"** means independent as defined in National Policy 58-201 — Corporate Governance Guidelines;

**"Initial Public Offering"** shall have the meaning ascribed thereto under "Corporate Structure – Name, Address and Incorporation";

**"Jazz"** means Jazz Aviation LP;

**"Jazz CPA"** means the Amended and Restated Capacity Purchase Agreement between Air Canada and Jazz dated January 1, 2006, as amended;

**"Management"** means management of Air Canada;

**"Montreal Trudeau Airport"** means Montreal's Pierre Elliott Trudeau International Airport;

**"Moody's"** means Moody's Investors service, Inc.

"OAG" means Official Airline Guide;

"OLA" means the *Official Languages Act* (Canada), as amended;

"Open Skies Agreement" means the agreement negotiated between the governments of Canada and the United States which came into force on March 12, 2007;

"OSFI" means the Office of the Superintendent of Financial Institutions;

"PIPEDA" means the *Personal Information Protection and Electronic Documents Act* (Canada);

"Porter" means Porter Airlines Inc.;

"Shares" means both Variable Voting Shares and Voting Shares;

"SOC" means System Operations Centre;

"Sky Regional" means Sky Regional Airlines Inc.;

"Standard & Poor's" means Standard & Poor's Rating Services;

"Subsidiary" has the meaning attributed to such term in the CBCA, provided that, notwithstanding the reference to a body corporate in the CBCA, a subsidiary may refer to a limited partnership or trust;

"Sunwing" means Sunwing Airlines;

"Tax Act" means the *Income Tax Act* (Canada) and the regulations thereunder, as amended;

"Toronto Pearson Airport" means Toronto Pearson International Airport;

"Transat" means Transat A.T. Inc.;

"TSA" means the Transportation Security Administration;

"TSX" means the Toronto Stock Exchange;

"Unifor" refers to a trade union in Canada, launched in 2013, as a merger of the Canadian Auto Workers and Communications, Energy and Paperworkers unions.

"United Airlines" means United Air Lines, Inc.;

"Variable Voting Shares" means Class A variable voting shares in the capital of Air Canada;

"Voting Shares" means Class B voting shares in the capital of Air Canada;

"WestJet" means WestJet Airlines Ltd.;

"WTI" means West Texas Intermediate; and

"Yield" means average passenger revenue per Revenue Passenger Mile.

## SCHEDULE A

### CHARTER OF THE AUDIT, FINANCE AND RISK COMMITTEE

(the "Audit Committee")

### OF THE BOARD OF DIRECTORS OF AIR CANADA

(the "Corporation")

#### 1. PURPOSE

The purpose of the Audit Committee is as follows:

- (i) To assist the Board in the discharge of its responsibility to monitor the component parts of the Corporation's financial reporting and audit process.
- (ii) To maintain and enhance the quality, credibility and objectivity of the Corporation's financial reporting and to satisfy itself and oversee management's responsibility as to the adequacy of the supporting systems of internal financial and accounting controls.
- (iii) To assist the Board of Directors in its oversight of the independence, qualifications and appointment of the external auditor.
- (iv) To monitor the performance of the internal financial and accounting controls and of the internal and external auditors.
- (v) To provide independent communication among the Board, the internal auditor and the external auditor.
- (vi) To facilitate in-depth and candid discussions among the Audit Committee, management and the external auditor regarding significant issues involving judgment and impacting quality of controls and reporting.

#### 2. COMPOSITION AND QUALIFICATION

- (a) The Audit Committee of the Corporation shall be composed of not less than three directors, all of whom shall meet the independence, experience and other membership requirements under applicable laws, rules and regulations as determined by the Board of Directors. The members of the Audit Committee shall have no relationships with management, the Corporation and its related entities that in the opinion of the Board may interfere with their independence from management and from the Corporation. In addition, an Audit Committee member shall not receive, other than for service on the Board or the Audit Committee or other committees of the Board, any consulting, advisory, or other compensatory fee from the Corporation or any of its related entities, parties or subsidiaries. The members of the Audit Committee shall possess the mix of characteristics, experiences and skills to provide an appropriate balance for the performance of the duties of the Audit Committee and in particular each member of the Audit Committee shall be "financially literate" and at least one member shall be a "financial expert" as defined by relevant securities legislation or regulations.
- (b) The members of the Audit Committee shall be appointed by the Board to hold office from the time of their appointment until the next annual general meeting of the shareholders or until their successors are appointed. Unless a Chair and a Secretary are appointed by the Board, the members of the Audit Committee may designate a Chair and a Secretary by a majority vote of all the Audit Committee members.
- (c) The Audit Committee may invite, from time to time, such person as it may see fit to attend its meeting and to take part in discussion and consideration of the affairs of the Audit Committee. However, any such persons invited may not vote at any meeting of the Audit Committee.

- (d) The Board, may, at any time, remove any member of the Audit Committee at its discretion and may accept the resignation of any member of the Audit Committee. Vacancies at any time occurring on the Audit Committee shall be filled by the Board.

### **3. MEETINGS AND PROCEDURE**

- (i) The Audit Committee shall meet at least four times annually, or more frequently as circumstances dictate. Such meetings shall be held by telephone or by any other mean which enables all participants to communicate with each other simultaneously.
- (ii) The Audit Committee may fix its own procedure at meetings and for the calling of meetings except as may be otherwise provided by the Board.
- (iii) A quorum for the transaction of business at an Audit Committee meeting shall be a majority of the Audit Committee members. All decisions and recommendations made by the Audit Committee shall be made by a majority vote of the members present at the meeting.
- (iv) An "in-camera" session of the members of the Audit Committee shall be held as part of each meeting of the Audit Committee.
- (v) Notice of meetings shall be given by letter, facsimile, email or telephone not less than 24 hours before the time fixed for the meeting. Notice of meetings shall state the date, the place and the hour at which such meetings shall be held. Members may waive notice of any meeting.
- (vi) The minutes of the Audit Committee meetings shall accurately record the significant discussions of, and decisions made by, the Audit Committee, including all recommendations to be made by the Audit Committee to the Board and shall be distributed to Audit Committee members as well as to all the directors of the Corporation, with copies to the Chief Executive Officer of the Corporation.
- (vii) The Audit Committee shall report to the Board on all proceedings and deliberations of the Audit Committee at the first subsequent meeting of the Board, and at such other times and in such manner as the Board may require or as the Audit Committee in its discretion may consider advisable.

### **4. RESPONSIBILITIES AND DUTIES**

To achieve its objectives, the Audit Committee shall:

- (a) Monitor and review the quality and integrity of the Corporation's accounting and financial reporting process through discussions with management, the external auditor and the internal auditor. This will include a review of the annual and quarterly financial statements and Management's Discussion and Analyses ("MD&As") to be filed with regulatory authorities and provided to shareholders, and financial statements and other financial disclosure included in prospectuses, earnings press releases and other similar documents. The Audit Committee shall also review the Corporation's annual information form and other similar documents. These reviews will include:
  - (i) discussions with management and the external auditor and a consideration of the report by the external auditor to the Audit Committee of matters related to the conduct of an audit;
  - (ii) discussions with the external auditor respecting the auditor's judgment regarding both the acceptability and quality of the financial statements including the critical accounting policies and practices used by management in their preparation, alternative treatments and disclosures of financial information within generally accepted accounting principles that have been considered by management and their ramifications, the selection of changes in significant accounting policies, the method used to account for significant unusual transactions, the effect of significant accounting policies in controversial or emerging areas, the degree of aggressiveness or conservatism, as the case may be, of the accounting policies adopted by the Corporation, the process used by management in formulating particularly significant

- accounting estimates and the basis for the external auditor's conclusions regarding the reasonableness of those estimates;
- (iii) a review of significant adjustments arising from an audit;
  - (iv) a review of disagreements with management over the application of accounting policies as well as any disclosure in the financial statements. The Audit Committee is responsible for the resolution of disagreements between management and the external auditor regarding financial reporting;
  - (v) a review of all material off-balance sheet transactions and other relationships with non-consolidated entities that may have a material current or future effect on the financial condition of the Corporation including their disclosure or lack thereof in the applicable quarterly or annual financial statements;
  - (vi) a review of the external auditor's suggestions for improvements to the Corporation's operations and internal controls;
  - (vii) a review of the nature and size of unadjusted errors of a non-trivial amount;
  - (viii) a review to ascertain that various covenants are complied with; and
  - (ix) the selection of, and changes in, accounting policies and consideration of the appropriateness of such selections and changes.
- (b) Determine, based on its review and discussion, whether to recommend the approval by the Board of the annual and quarterly financial statements and related MD&A, and the financial disclosure in any such annual information forms, earnings press releases, prospectuses and other similar documents.
  - (c) Review with management, the external auditor and legal counsel, the Corporation's procedures to be satisfied that it complies with applicable laws and regulations, and any significant litigation, claim or other contingency, including tax assessments, that would have a material effect upon the financial position or operating results of the Corporation and the disclosure or impact on the results of these matters in the quarterly and annual financial statements. The Audit Committee should be satisfied that adequate procedures are in place for the review of the Corporation's public disclosure of financial information extracted or derived from the Corporation's financial statements, and must periodically assess the adequacy of those procedures.
  - (d) Meet with the Corporation's external auditor to review and approve their audit plan with particular emphasis on risk factors which could lead to a material misstatement of the financial statements, the scope and timing of the audit, the assumptions and decisions that have been made in developing the plan and co-ordination of work between the external auditor and the internal audit department. The Audit Committee is responsible for overseeing the work of the external auditor engaged for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Corporation.
  - (e) Review and approve estimated audit and audit-related fees and expenses for the current year. Pre-approve any significant additional audit and audit-related fees over the estimated amount. Review and approve audit and audit-related fees and expenses for the prior year. The authority for the determination and payment of fees to the external auditor rests solely and exclusively with the Audit Committee. The Corporation shall ensure that funding is available to the Audit Committee for payment of compensation to the external auditor.
  - (f) Review
    - (i) and approve, or delegate to a member of the Audit Committee the responsibility to review and approve, the nature of all non-audit services, as permitted by securities legislation and regulations, to be provided by the Corporations' external auditor prior to the commencement of such work. In this regard the Audit Committee will prepare a report for presentation to the shareholders of the Corporation quarterly or annually, as required, regarding the Audit Committee's approval of such non-audit services in the period. The pre-approval of non-audit services by a member of the Audit Committee to whom such authority is

delegated must be presented to the Audit Committee at its first scheduled meeting following such pre-approval;

- (ii) and implement from time to time a process in connection with non-audit services performed by the external auditor.
- (g) Review a report from the external auditor that in the external auditor's professional judgment it is independent of the Corporation and discuss this report with the external auditor in order to evaluate the objectivity and independence of the external auditor. The Audit Committee should specifically require the external auditor to confirm that it is a registered public accounting firm as prescribed by various applicable securities regulations and to confirm that it is not the subject of any other inquiry or investigation by governmental or professional authority relating to any audit conducted by the firm.
- (h) Receive reports on any consultations between management and other public accountants respecting accounting principles to be applied in preparing the quarterly or annual financial statements, and on any incidents involving fraud or illegal acts of which management, the internal audit department or the external auditor become aware. In this regard, review the relevant control procedures with management to satisfy itself that such matters are adequately guarded against.
- (i) At least once each year, meet privately with management to assess the performance of the external auditor and, at each quarterly meeting of the Audit Committee, meet privately with the external auditor, amongst other things, to understand any restrictions placed on them or other difficulties encountered in the course of the audit or review, including instructions on the scope of their work and access to requested information and the level of co-operation received from management during the performance of their work and their evaluation of the Corporation's financial, accounting and audit personnel and systems.
- (j) Evaluate the performance of the external auditor, and if so determined, recommend that the Board either take steps to replace the external auditor or provide for the reappointment of the external auditor by the shareholders.
- (k) Regarding the services provided by the internal audit department, the Audit Committee will:
  - (i) meet privately with internal audit, amongst other things, to understand any restrictions placed on them or other difficulties encountered in the course of their audits, including instructions on the scope of their work and access to requested information and the level of co-operation received from management during the performance of their work;
  - (ii) periodically review and approve the mandate, reporting relationships and resources of the internal audit group;
  - (iii) review the objectivity, qualifications, adequacy and experience of the internal audit staff and approve the appointment, dismissal or replacement of the head of the internal audit department;
  - (iv) review and approve annually the planned scope for the internal audit program, its objectives, and the resources required to attain these objectives;
  - (v) periodically throughout each year review the reports of the internal audit department which describe the activities of the internal audit department for the preceding period; and
  - (vi) review the working relationship between the internal audit department and the external auditor, and between the internal audit department and management.
- (l) Obtain from both the internal audit department and the Corporation's external auditor the major audit findings and internal control recommendations reported during the period under review, the response of management to those recommendations, and review the follow-up performed by management and the internal audit department in order to monitor whether management has implemented an effective system of internal accounting control.

- (m) Review significant emerging accounting and reporting issues, including recent professional and regulatory pronouncements, and assess their impact on the Corporation's financial statements.
- (n) Establish policies and procedures for the receipt, retention and treatment of complaints received by the Corporation from employees, shareholders and other stakeholders regarding accounting issues and financial reporting, internal accounting controls and internal or external auditing matters. The Audit Committee should be satisfied that sufficient controls are in place with the objective that all such complaints can be received anonymously and with an appropriate degree of confidentiality and that potential employee informants are aware of the process that is in place. The Audit Committee should also be satisfied that processes are in place with the objective that all such complaints, regardless of significance, are presented to the Audit Committee.
- (o) Review policies for approval of senior management expenses.
- (p) Review the process relative to the periodic certifications by the Chief Executive Officer and the Chief Financial Officer of the Corporation in respect of financial disclosures, the existence of any significant deficiencies in the design or operation of internal controls which could adversely affect the Corporation's ability to record, process, summarize and report financial data and any significant changes in internal controls or changes to the environment in which the internal controls operate, including corrections of material deficiencies and weaknesses.
- (q) Review with management the Corporation's computer systems, including procedures to keep the systems secure and contingency plans developed to deal with possible computer failures.
- (r) Review and approve all related party transactions as such term is defined from time to time in Regulation 61-101 respecting Protection of Minority Security Holders in Special Transactions of the Autorité des marchés financiers and Multilateral Instrument 61-101 issued by the Ontario Securities Commission, as may be amended from time to time.
- (s) Review risk management systems and controls, especially in relation to derivatives, foreign currency exposure, hedging and insurance.
- (t) Whenever it may be appropriate to do so, retain and receive advice from experts, including independent legal counsel and independent public accountants, and conduct or authorize the conduct of investigations into any matters within the scope of the responsibility of the Audit Committee as the Audit Committee may consider appropriate. The Corporation shall ensure that funding is available to the Audit Committee in respect of the aforementioned activities.
- (u) Report regularly to the Board on the activities, findings and conclusions of the Audit Committee.
- (v) Review this Charter on an annual basis and recommend to the Board any changes to it that the Audit Committee considers advisable.
- (w) Complete a self-assessment annually to determine how effectively the Audit Committee is meeting its responsibilities.
- (x) Perform such other functions as may be delegated from time to time by the Board.
- (y) Review the process for the rotation of the lead audit partner, the concurring partner and any other audit engagement team partner of the external auditor of the Corporation.
- (z) Review and approve the Corporation's hiring policies regarding partners, employees and former partners and employees of the present and former external auditors of the Corporation.



## **OTHER**

### **(a) Public Disclosure**

The Audit Committee shall:

- (i) Review and approve the Corporation's Public Disclosure Policy and any changes related thereto and satisfy itself that such policy is consistent with current developments and best practices;
- (ii) Where practicable, management will review with the Audit Committee or the Chairman of the Audit Committee draft news releases to be disseminated to the public related to earnings warnings or financial results forecasting by the Corporation which are expected by management to be material in relation to the market price of any of the Corporation's securities.

### **(b) Risk Identification and Management**

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

### **(c) Contingent Liabilities**

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

### **(d) Corporate Authorizations Policies**

The Audit Committee shall:

- (i) Periodically review and approve policies relative to the financial control, conduct, regulation and administration of subsidiary companies;
- (ii) Periodically review any administrative resolutions adopted from time to time pursuant to the Corporation's By-laws pertaining to the establishment of procedures relative to commitment and transaction authorizations, the determination of the officers or other persons by whom any instrument in writing or document is to be executed and the manner of execution thereof;
- (iii) Review, monitor and approve the Corporate Donations Policy and any changes thereto and the annual Corporate Donations Budget; and
- (iv) Review, monitor and approve any other financial expenditure policies that would affect the Corporation's and its subsidiaries' financial condition or reputation.

### **(e) Performance to Budget**

The Audit Committee shall review actual financial performance compared to budget.

### **(f) Responsibilities**

Nothing contained in the above mandate is intended to assign to the Audit Committee the Board of Directors' responsibility regarding the Corporation's compliance with applicable laws or regulations or to expand applicable standards

of liability under statutory or regulatory requirements for the directors or the members of the Audit Committee. Even though the Audit Committee has a specific mandate and its members have financial experience and expertise, it is not the duty of the Audit Committee to plan or conduct audits, or to determine that the Corporation's financial statements are complete and accurate and are in accordance with generally accepted accounting principles. Such matters are the responsibility of management, the internal auditor and the external auditor.

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

November 7, 2013