AIR CANADA

Second Quarter 2015

INTERIM UNAUDITED

Condensed Consolidated
Financial Statements and Notes

August 12, 2015

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Unaudited **(Canadian dollars in millions)**		**June 30, 2015**	**December 31, 2014**
ASSETS			
Current			
Cash and cash equivalents		$ 1,077	$ 661
Short-term investments		1,944	1,614
Total cash, cash equivalents and short-term investments		3,021	2,275
Restricted cash		51	89
Accounts receivable		822	656
Aircraft fuel inventory		50	72
Spare parts and supplies inventory		97	91
Prepaid expenses and other current assets		252	295
Total current assets		4,293	3,478
Property and equipment		6,277	5,998
Pension	Note 5	623	-
Intangible assets		308	305
Goodwill		311	311
Deposits and other assets		562	556
Total assets		**$ 12,374**	**$ 10,648**
LIABILITIES			
Current			
Accounts payable and accrued liabilities		$ 1,423	$ 1,259
Advance ticket sales		2,395	1,794
Current portion of long-term debt and finance leases	Note 4	528	484
Total current liabilities		4,346	3,537
Long-term debt and finance leases	Note 4	5,093	4,732
Pension and other benefit liabilities	Note 5	2,209	2,403
Maintenance provisions		831	796
Other long-term liabilities		283	313
Total liabilities		**$ 12,762**	**$ 11,781**
EQUITY			
Shareholders' equity			
Share capital		838	835
Contributed surplus		75	77
Deficit		(1,362)	(2,113)
Total shareholders' equity		(449)	(1,201)
Non-controlling interests		61	68
Total equity		(388)	(1,133)
Total liabilities and equity		**$ 12,374**	**$ 10,648**

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

CONSOLIDATED STATEMENT OF OPERATIONS

Unaudited		Three months ended June 30		Six months ended June 30	
(Canadian dollars in millions except per share figures)		**2015**	**2014**	**2015**	**2014**
Operating revenues					
Passenger		$ 3,082	$ 2,965	$ 5,868	$ 5,573
Cargo		123	122	252	241
Other		209	218	543	556
Total revenues		**3,414**	**3,305**	**6,663**	**6,370**
Operating expenses					
Aircraft fuel		648	835	1,240	1,628
Regional airlines expense	Notes 2 & 10	594	578	1,146	1,145
Wages, salaries and benefits	Note 5	568	535	1,136	1,092
Airport and navigation fees		201	186	386	369
Aircraft maintenance		190	171	378	333
Sales and distribution costs		152	143	306	291
Depreciation, amortization and impairment	Note 3	177	128	330	254
Ground package costs		84	77	265	247
Aircraft rent		84	76	166	152
Food, beverages and supplies		80	74	142	140
Communications and information technology		52	47	109	99
Other		261	210	536	437
Total operating expenses		**3,091**	**3,060**	**6,140**	**6,187**
Operating income		**323**	**245**	**523**	**183**
Non-operating income (expense)					
Foreign exchange gain (loss)	Note 9	56	40	(352)	(121)
Interest income		12	9	21	18
Interest expense		(94)	(81)	(184)	(158)
Interest capitalized		21	10	30	15
Net financing expense relating to employee benefits	Note 5	(25)	(34)	(50)	(68)
Fuel and other derivatives	Note 9	5	36	6	21
Other		(2)	(2)	(7)	(8)
Total non-operating expense		(27)	(22)	(536)	(301)
Income (loss) before income taxes		**296**	**223**	**(13)**	**(118)**
Income taxes		-	-	-	-
Net income (loss) for the period		**$ 296**	**$ 223**	**$ (13)**	**$ (118)**
Net income (loss) attributable to:					
Shareholders of Air Canada		295	222	(15)	(120)
Non-controlling interests		1	1	2	2
		$ 296	**$ 223**	**$ (13)**	**$ (118)**
Net income (loss) per share attributable to shareholders of Air Canada	Note 7				
Basic earnings (loss) per share		$ 1.03	$ 0.77	$ (0.06)	$ (0.42)
Diluted earnings (loss) per share		1.00	0.75	(0.06)	(0.42)

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

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

Unaudited		Three months ended June 30		Six months ended June 30	
(Canadian dollars in millions)		**2015**	**2014**	**2015**	**2014**
Comprehensive income (loss)					
Net income (loss) for the period		$ 296	$ 223	$ (13)	$ (118)
Other comprehensive income (loss), net of taxes of nil:					
Items that will not be reclassified to net income					
Remeasurements on employee benefit liabilities	Note 5	542	(90)	790	(293)
Items that will be reclassified to net income					
Loss on derivatives designated as cash flow hedges	Note 9	(1)	-	(1)	-
Total comprehensive income (loss)		**$ 837**	**$ 133**	**$ 776**	**$ (411)**
Comprehensive income (loss) attributable to:					
Shareholders of Air Canada		$ 836	$ 132	$ 774	**$** (413)
Non-controlling interests		1	1	2	2
		$ 837	**$ 133**	**$ 776**	**$ (411)**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Unaudited (Canadian dollars in millions)	Share capital	Contributed surplus	Deficit	Total shareholders' equity	Non-controlling interests	Total equity
January 1, 2014	$ 827	$ 80	$ (2,367)	$ (1,460)	$ 63	$ (1,397)
Net income (loss)	–	–	(120)	(120)	2	(118)
Remeasurements on employee benefit liabilities	–	–	(293)	(293)	–	(293)
Total comprehensive income (loss)	–	–	(413)	(413)	2	(411)
Share-based compensation	–	(4)	(13)	(17)	–	(17)
Shares issued	1	–	–	1	–	1
Shares vested for employee recognition award	6	(4)	–	2	–	2
June 30, 2014	$ 834	$ 72	$ (2,793)	$ (1,887)	$ 65	$ (1,822)
January 1, 2015	$ 835	$ 77	$ (2,113)	$ (1,201)	$ 68	$ (1,133)
Net income (loss)	–	–	(15)	(15)	2	(13)
Remeasurements on employee benefit liabilities	–	–	790	790	–	790
Loss on derivatives designated as cash flow hedges	–	–	(1)	(1)	–	(1)
Total comprehensive income	–	–	774	774	2	776
Share-based compensation	–	(1)	(22)	(23)	–	(23)
Shares issued	3	(1)	–	2	–	2
Distributions	–	–	–	–	(9)	(9)
Shares purchased and cancelled under issuer bid (Note 6)	–	–	(1)	(1)	–	(1)
June 30, 2015	$ 838	$ 75	$ (1,362)	$ (449)	$ 61	$ (388)

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

CONSOLIDATED STATEMENT OF CASH FLOW

Unaudited		Three months ended June 30		Six months ended June 30	
(Canadian dollars in millions)		**2015**	**2014**	**2015**	**2014**
Cash flows from (used for)					
Operating					
Net income (loss) for the period		$ 296	$ 223	$ (13)	$ (118)
Adjustments to reconcile to net cash from operations					
Depreciation, amortization and impairment		181	133	338	263
Foreign exchange loss (gain)		(51)	(46)	365	128
Employee benefit funding greater than expense	Note 5	(13)	(23)	(23)	(36)
Fuel and other derivatives	Note 9	(15)	(30)	(17)	(16)
Change in maintenance provisions		9	21	2	32
Changes in non-cash working capital balances		132	141	706	508
Other		(30)	(33)	(41)	(31)
Net cash flows from operating activities		**509**	**386**	**1,317**	**730**
Financing					
Proceeds from borrowings		7	626	289	784
Reduction of long-term debt and finance lease obligations		(147)	(348)	(262)	(390)
Distributions related to aircraft special purpose leasing entities		-	-	(9)	-
Issue of common shares		2	-	3	-
Shares purchased for cancellation	Note 6	(1)	-	(1)	-
Financing fees	Note 4	(7)	-	(22)	-
Net cash flows (used in) from financing activities		**(146)**	**278**	**(2)**	**394**
Investing					
Short-term investments		(139)	(264)	(290)	(294)
Additions to property, equipment and intangible assets		(210)	(422)	(635)	(732)
Proceeds from sale of assets		9	1	10	3
Other		19	7	16	10
Net cash flows used in investing activities		**(321)**	**(678)**	**(899)**	**(1,013)**
Increase in cash and cash equivalents		**42**	**(14)**	**416**	**111**
Cash and cash equivalents, beginning of period		1,035	875	661	750
Cash and cash equivalents, end of period		**$ 1,077**	**$ 861**	**$ 1,077**	**$ 861**

Cash payments of interest	**$ 114**	**$ 97**	**$ 149**	**$ 139**
Cash payments of income taxes	**$ -**	**$ -**	**$ -**	**$ -**

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
(CANADIAN DOLLARS IN MILLIONS – EXCEPT PER SHARE AMOUNTS)

1. GENERAL INFORMATION

The accompanying unaudited interim condensed consolidated financial statements (the "financial statements") are of Air Canada (the "Corporation"). The term "Corporation" also refers to, as the context may require, Air Canada and/or one or more of its subsidiaries, including its principal wholly-owned operating subsidiaries, Touram Limited Partnership doing business under the brand name Air Canada Vacations® ("Air Canada Vacations") and Air Canada *rouge* LP doing business under the brand name Air Canada *rouge*® ("Air Canada *rouge*"). These financial statements also include certain aircraft leasing entities, which are consolidated under IFRS 10 Consolidated Financial Statements, with nominal equity owned by other parties.

Air Canada is incorporated and domiciled in Canada. The address of its registered office is 7373 Côte-Vertu Boulevard West, Saint-Laurent, Quebec.

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

2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Corporation prepares its financial statements in accordance with generally accepted accounting principles in Canada ("GAAP") as set out in the CPA Canada Handbook – Accounting ("CPA Handbook") which incorporates International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). These financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including IAS 34 "Interim Financial Reporting". In accordance with GAAP, these financial statements do not include all of the financial statement disclosures required for annual financial statements and should be read in conjunction with the Corporation's annual consolidated financial statements for the year ended December 31, 2014. In management's opinion, the financial statements reflect all adjustments that are necessary for a fair presentation of the results for the interim period presented.

These financial statements were approved for issue by the Board of Directors of the Corporation on August 11, 2015.

Except as described below, these financial statements are based on the accounting policies consistent with those disclosed in Note 2 to the 2014 annual consolidated financial statements. Refer to Note 2 to the 2014 annual consolidated financial statements for information on new accounting standards and amendments not yet effective and, with the exception of the early adoption of IFRS 9 described below, which are not yet adopted or described herein.

Change in presentation – Regional airlines expense

As described in Note 2D to the 2014 annual consolidated financial statements, the Corporation has capacity purchase agreements with Jazz Aviation LP ("Jazz"), Sky Regional Airlines Inc. and certain other regional carriers. Under these arrangements, Air Canada markets, tickets and enters into other commercial arrangements relating to these flights and records the revenue it earns under Passenger revenues. Operating expenses under capacity purchase agreements include the capacity purchase fees, pass-through costs and other costs incurred by the Corporation which are directly related to regional carrier operations. Pass-through costs are costs charged to the Corporation without a mark-up and include fuel, airport and user fees and other costs. Prior to 2015, these expenses were recorded in the applicable category within Operating expenses with capacity purchase fees presented as a separate line item. As of 2015, expenses incurred related to capacity purchase agreements are now presented in a separate line item in the consolidated statement of operations titled Regional airlines expense which reflects the inclusion of all expenses related to the third-party contract carrier arrangements, including capacity purchase fees, pass-through costs and other costs. This change in presentation has been adopted to provide improved presentation of the economic costs associated with regional carrier operations. Prior period amounts have been reclassified to conform to the current period presentation.

Effective January 1, 2015, Air Canada and Jazz amended the terms of their capacity purchase agreement and extended its term to December 31, 2025. As a result of the amendments, certain costs that were previously capacity purchase agreement fees are now pass-through costs. Other costs that were pass-through costs are now costs directly incurred by Air Canada.

A reconciliation of operating expenses as previously reported to the current year presentation for the three and six month periods ended June 30, 2014 is provided below.

(Canadian dollars in millions)	Three Months Ended June 30, 2014		Adjustment		Three Months Ended June 30, 2014 Reclassified	
Operating expenses						
Aircraft fuel	$	962	$	(127)	$	835
Regional airlines expense		-		578		578
Wages, salaries and benefits		548		(13)		535
Capacity purchase agreements		294		(294)		-
Airport and navigation fees		256		(70)		186
Aircraft maintenance		180		(9)		171
Sales and distribution costs		171		(28)		143
Depreciation, amortization and impairment		133		(5)		128
Ground package costs		77		-		77
Aircraft rent		78		(2)		76
Food, beverages and supplies		77		(3)		74
Communications and information technology		49		(2)		47
Other		235		(25)		210
Total operating expenses	$	3,060	$	-	$	3,060

(Canadian dollars in millions)	Six Months Ended June 30, 2014		Adjustment		Six Months Ended June 30, 2014 Reclassified	
Operating expenses						
Aircraft fuel	$	1,880	$	(252)	$	1,628
Regional airlines expense		-		1,145		1,145
Wages, salaries and benefits		1,117		(25)		1,092
Capacity purchase agreements		575		(575)		-
Airport and navigation fees		503		(134)		369
Aircraft maintenance		361		(28)		333
Sales and distribution costs		346		(55)		291
Depreciation, amortization and impairment		263		(9)		254
Ground package costs		247		-		247
Aircraft rent		157		(5)		152
Food, beverages and supplies		147		(7)		140
Communications and information technology		102		(3)		99
Other		489		(52)		437
Total operating expenses	$	6,187	$	-	$	6,187

Adoption of new accounting standard – IFRS 9 – Financial Instruments

The Corporation has early adopted IFRS 9 – Financial Instruments with a date of initial application of January 1, 2015. IFRS 9 introduces new requirements for the classification and measurement of financial assets. IFRS 9 requires all recognized financial assets to be measured at amortized cost or fair value in subsequent accounting periods following initial recognition. Specifically, financial assets that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. All other financial assets including equity investments are measured at their fair values at the end of subsequent accounting periods, with any changes taken through profit and loss or other comprehensive income depending on certain criteria. The requirements for classification and measurement of financial liabilities largely carried forward existing requirements in IAS 39, Financial Instruments – Recognition and Measurement, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss would generally be recorded in other comprehensive income. IFRS 9 also amends the requirements around hedge accounting, and introduces a single, forward-looking expected loss impairment model.

The adoption of this standard has no impact on the Corporation's consolidated financial statements on the date of adoption or for comparative periods. There was no change in the carrying amounts on the basis of allocation from original measurement categories under IAS 39 to the new measurement categories under IFRS 9. Refer to Note 17 to the 2014 annual consolidated financial statements for a summary of classifications under IAS 39. All financial assets, other than Accounts receivable and Aircraft related and other deposits, are now included in the measurement category of fair value through profit and loss. Financial assets previously allocated to Loans and receivables are now allocated to the amortized cost category. There was no change to the measurement category for financial liabilities at amortized cost.

The Corporation has begun to apply hedge accounting for certain designated fuel derivatives prospectively from April 1, 2015. Crude oil prices, while not contractually specified in the Corporation's jet fuel purchase contracts, are economically related to jet fuel prices. The Corporation enters into option contracts on crude oil and designates the contracts in cash flow hedges of the crude oil component of its future jet fuel purchases. The Corporation has established a hedge ratio of 1:1 for its hedging relationships. Under hedge accounting, the effective gain or loss on fuel hedging derivatives is recorded in other comprehensive income and reclassified to Aircraft fuel expense when the underlying jet fuel being hedged is used. Premiums paid for option contracts and the time value of the option contracts are deferred as a cost of the hedge in other comprehensive income and reclassified to Aircraft fuel expense when the underlying hedged jet fuel is used. Any ineffective gain or loss on fuel hedging derivatives is recorded in non-operating expense in fuel and other derivatives. Refer to Note 9 for the results from fuel hedge accounting in the second quarter of 2015.

ACCOUNTING STANDARDS AND AMENDMENTS ISSUED BUT NOT YET ADOPTED

IFRS 15 – Revenue from Contracts with Customers

IFRS 15 replaces IAS 18 Revenue and related interpretations. The core principle of the new standard is to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the Corporation expects to be entitled in exchange for those goods or services. In July 2015, the International Accounting Standards Board confirmed a deferral of the effective date by one year to January 1, 2018, with earlier application permitted. The Corporation continues to evaluate the impact that the adoption of this standard may have on the consolidated financial statements.

3. ASSET IMPAIRMENT

During the second quarter of 2015, an impairment charge of $14 was recorded in Depreciation, amortization and impairment expense related to two A340-300 aircraft (neither of which was operated by Air Canada). The lease agreements relating to these aircraft expired and the aircraft are being prepared for return or purchase and sale. The impairment charge is based upon the net proceeds expected upon their disposal. The total carrying amount of these two aircraft is $20 as at June 30, 2015.

4. LONG-TERM DEBT AND FINANCE LEASES

	Final Maturity	Weighted Average Interest Rate (%)	June 30 2015	December 31 2014
Aircraft financing (a)				
Fixed rate U.S. dollar financing	2015 – 2027	5.74	$ 2,153	$ 2,029
Floating rate U.S. dollar financing	2017 – 2026	1.84	579	582
Floating rate CDN dollar financing	2026 - 2027	1.65	414	310
Floating rate Japanese yen financing	2020	0.23	89	94
Senior secured notes – U.S. dollar	2019 – 2020	7.61	875	812
Senior secured notes – CDN dollar	2019	7.63	300	300
Senior unsecured notes – U.S. dollar	2021	7.75	500	464
Other secured financing – U.S. dollar (b)	2018 – 2019	4.44	465	433
Other secured financing – CDN dollar	2018	8.15	50	-
Long-term debt		**5.42**	**5,425**	**5,024**
Finance lease obligations	2015 – 2033	10.08	291	283
Total debt and finance leases		**5.66**	**5,716**	**5,307**
Unamortized debt issuance costs			(95)	(91)
Current portion			(528)	(484)
Long-term debt and finance leases			**$ 5,093**	**$ 4,732**

The above table provides terms of instruments disclosed in Note 8 to the 2014 annual consolidated financial statements of the Corporation as well as terms of instruments concluded during the six months ended June 30, 2015 described below.

(a) In March 2015, in connection with the financing of one Boeing 787-8 delivered in January 2015 and eight new Boeing 787-9 aircraft, which are currently scheduled for delivery from July 2015 to March 2016, Air Canada announced the closing of a private offering of three tranches of enhanced equipment trust certificates with a combined aggregate face amount of US$1,031.

The private offering is comprised of Class A certificates, Class B certificates and Class C certificates.

- The Class A certificates, with a US$667 face amount, have an interest rate of 3.600% per annum and a final expected distribution date of March 15, 2027.
- The Class B certificates, with a US$182 face amount, have an interest rate of 3.875% per annum and a final expected distribution date of March 15, 2023.
- The Class C certificates, with US$182 face amount, have an interest rate of 5.000% per annum and a final expected distribution date of March 15, 2020.

The certificates have a combined weighted average interest rate of 3.81% per annum.

Each class of certificates represents an interest in a related pass through trust. The trusts consist of a separate trust for the Class A certificates, Class B certificates and Class C certificates, respectively. Equipment notes related to the Boeing 787-8 delivered in January 2015 were issued in the first quarter of 2015. Air Canada used the proceeds from the sale of equipment notes to the trusts related to the Boeing 787-8 aircraft delivered in January 2015 for general corporate purposes and to pay fees and expenses related to the offering (as that aircraft was paid for prior to the completion of the private offering of enhanced equipment trust certificates). The proceeds from the sale of the other equipment notes will be used to finance the acquisition of the eight new Boeing 787-9 aircraft. Proceeds from the offering are held in escrow until the delivery of the respective Boeing 787-9 aircraft. These funds held in escrow are not assets of Air Canada and are not reported as assets and the certificates relating thereto are not reported as debt on Air Canada's condensed consolidated statement of financial position. In connection with the financing of the first aircraft, an amount of US$99 was drawn from the proceeds held in escrow and is included in fixed rate U.S. dollar financing in the table above.

The equipment notes issuable at each draw-down are structured to be secured by the Boeing 787-8 aircraft delivered in January 2015 and each of the eight Boeing 787-9 aircraft being acquired, and the security interest in each of the aircraft is structured to benefit from the protections of the Cape Town Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment, as enacted in Canada.

In respect of the Class A, Class B and Class C certificates, the trustee will distribute all payments of principal, premium (if any) and interest received on the related equipment notes held in each trust to the holders of the respective certificates, subject to the subordination provisions applicable to the certificates. Commencing on September 15, 2015, scheduled payments made on the equipment notes will be distributed to the holders of the certificates as follows:

- To Class A and Class B certificate holders, scheduled payments of principal and interest will be distributed on the regular distribution dates of March 15 and September 15.

- To Class C certificate holders, scheduled payments of interest will be distributed on the regular distribution dates of March 15 and September 15, commencing on September 15, 2015 and the entire principal amount is scheduled to be paid on March 15, 2020.

Financing fees paid in conjunction with the offering were $15 and are reported in Financing on the consolidated statement of cash flow.

In connection with the acquisition of a Boeing 787-8 aircraft in February 2015, an amount of $118 was financed and included in floating rate CDN dollar financing. Interest and principal is payable quarterly until maturity and the financing is supported by a loan guarantee by the Export-Import Bank of the United States ("EXIM").

(b) During the second quarter of 2015, the Corporation re-negotiated the interest rate terms of the US$510 senior secured credit facility, comprised of a US$300 term loan maturing in 2019 and a US$210 revolving credit facility (collectively, the "New Credit Facility" as also referred to in Note 8b to the 2014 annual consolidated financial statements). The applicable margin with respect to loans under the revolving credit facility in the New Credit Facility is 3.25% with respect to LIBOR loans and banker's acceptances and 2.25% with respect to the Index Rate loans or Canadian Prime Rate loans. The applicable margin with respect to term loans under the New Credit Facility is 3.25% with respect to LIBOR loans and 2.25% with respect to the Index Rate loans. As at June 30, 2015, the Corporation had not drawn on the revolving credit facility and the outstanding term loan principal is US$297.

Refer to Note 8 for the Corporation's principal and interest repayment requirements as at June 30, 2015.

5. PENSIONS AND OTHER BENEFIT LIABILITIES

Pension Plan Cash Funding Obligations

In the second quarter of 2015, the Corporation elected to opt out of the *Air Canada Pension Plan Funding Regulations, 2014*, (the "2014 Regulations"), effective at that time. As described in Note 9 to the 2014 annual consolidated financial statement, the 2014 Regulations became effective on January 1, 2014 and under their terms, the Corporation was required to make solvency deficit payments of $200 per year, on average, over a seven-year period. The agreement with the Government of Canada entered into in connection with these regulations contained several restrictions, including a prohibition on dividends and share repurchases. However, the agreement allowed the Corporation to opt out at any time.

Total employer contributions to defined benefit pension plans for 2015 are expected to be $322, which includes solvency deficit payments of approximately $96 versus the $200 that would have been required under the 2014 Regulations.

Pension Plan Assets

As described in Note 9 to the 2014 annual consolidated financial statements, included in pension plan assets for determining the net pension benefit obligation for accounting purposes are 17,647,059 Class B Voting Shares of Air Canada, held in trust, which were issued in 2009 in connection with pension funding agreements reached with all of the Corporation's Canadian-based unions. The trust arrangement provides that proceeds of any sale of the trust shares will be retained and applied to reduce future pension solvency deficits, if any should materialize. With the impact of the opt out as described above, and with the Corporation's domestic registered pension plans in a surplus position on a solvency basis, the accounting rules now prevent the recognition of the value of the shares held in trust as part of the pension assets. The shares held in trust have a fair value of $233 at June 30, 2015, however after giving effect to the asset ceiling, the recognized accounting value of the trust asset is nil.

Certain pension plans are now in net asset positions and, as a result, those plans are required to be reported as Pension assets on the consolidated statement of financial position.

Pension and Other Employee Future Benefit Expense

The Corporation has recorded net defined benefit pension and other employee future benefits expense as follows:

	Three Months Ended June 30		Six Months Ended June 30	
	2015	**2014**	**2015**	**2014**
Consolidated Statement of Operations				
Operating expenses				
Wages, salaries and benefits				
Pension benefits	$ 65	$ 45	$ 129	$ 105
Other employee benefits (a)	(13)	9	(9)	20
	$ 52	**$ 54**	**$ 120**	**$ 125**
Non-operating income (expense)				
Net financing expense relating to employee benefit liabilities				
Pension benefits	$ (12)	$ (20)	$ (25)	$ (40)
Other employee benefits	(13)	(14)	(25)	(28)
	$ (25)	**$ (34)**	**$ (50)**	**$ (68)**
Consolidated Other Comprehensive Income (Loss)				
Remeasurements on employee benefit liabilities				
Pension benefits	$ 478	$ (41)	$ 778	$ (179)
Other employee benefits	64	(49)	12	(114)
	$ 542	**$ (90)**	**$ 790**	**$ (293)**

(a) During the second quarter of 2015, as a result of a plan amendment which included a reduction in post-retirement benefits for both current and future retirees and increased member contributions towards the cost of the benefits, a benefit plan amendment credit of $19 was recorded.

The funding of employee benefits as compared to the expense recorded in the consolidated statement of operations is summarized in the table below.

	Three Months Ended June 30		Six Months Ended June 30	
	2015	**2014**	**2015**	**2014**
Net defined pension and other future employee benefits expense recorded in the consolidated statement of operations				
Wages, salaries and benefits	$ 52	$ 54	$ 120	$ 125
Net financing expense relating to employee benefit liabilities	25	34	50	68
	$ 77	**$ 88**	**$ 170**	**$ 193**
Employee benefit funding by Air Canada				
Pension benefits	$ 81	$ 99	$ 174	$ 206
Other employee benefits	9	12	19	23
	$ 90	**$ 111**	**$ 193**	**$ 229**
Employee benefit funding greater than expense	**$ (13)**	**$ (23)**	**$ (23)**	**$ (36)**

Starting in 2015, the Corporation is refining the method to estimate the current service cost for pension and other post-retirement benefits. Previously, the current service cost was estimated utilizing a single weighted-average discount rate derived from the yield curve used to measure the defined benefit obligation at the beginning of the year. Under the refined method, different discount rates are derived from the same yield curve, reflecting the different timing of benefit payments for past service (the defined benefit obligation) and future service (the current service cost). Differentiating in this way represents a refinement in the basis of estimation applied in prior periods. This change does not affect the measurement of the total defined benefit obligation recorded on the consolidated statement of financial position as at December 31, 2014 or any other period. The refinement compared to the previous method resulted in a decrease in the current service cost and interest components with an equal offset to actuarial gains (losses) with no net impact on the total benefit obligation. The refinement did not have a material impact on the 2015 consolidated statement of operations. This change is accounted for prospectively as a change in accounting estimate.

6. SHARE CAPITAL

Issuer Bid

In May 2015, Air Canada announced that it received approval from the Toronto Stock Exchange ("TSX") to implement a normal course issuer bid to purchase, for cancellation, up to 10,000,000 Class A variable voting and/or Class B voting shares (the "Shares"), representing, at that time, 3.49% of the total issued and outstanding shares. The repurchase program, which is authorized for the period from May 29, 2015 to May 28, 2016, will be conducted through the facilities of the TSX.

Prior to the end of the second quarter of 2015, the Corporation purchased and cancelled 100,000 Shares for cash at an average cost of $13.80 per Share.

7. EARNINGS PER SHARE

The following table outlines the calculation of basic and diluted earnings per share.

	Three months ended June 30		Six months ended June 30	
in millions, except per share amounts	**2015**	**2014**	**2015**	**2014**
Numerator:				
Numerator for basic and diluted earnings per share:				
Net income (loss) attributable to shareholders of Air Canada	$ 295	$ 222	$ (15)	$ (120)
Denominator:				
Weighted-average shares - basic	287	286	287	286
Effect of potential dilutive securities:				
Stock options	8	7	8	7
Total potential dilutive securities	8	7	8	7
Remove anti-dilutive impact	-	-	(8)	(7)
Adjusted denominator for diluted earnings per share	295	293	287	286
Basic earnings (loss) per share	**$ 1.03**	**$ 0.77**	**$ (0.06)**	**$ (0.42)**
Diluted earnings (loss) per share	**1.00**	**0.75**	**(0.06)**	**(0.42)**

The calculation of earnings per share is based on whole dollars and not on rounded millions. As a result, the above amounts may not be recalculated to the per share amount disclosed above.

Excluded from the calculation of diluted earnings per share were outstanding options where the exercise prices were greater than the average market price of the ordinary shares for the period.

8. COMMITMENTS

Aircraft and Related Financing

As described in Note 16 to the 2014 annual consolidated financial statements, the Corporation as at December 31, 2014, had outstanding purchase commitments with The Boeing Company ("Boeing") for the acquisition of 31 Boeing 787 aircraft scheduled from 2015 to 2019. Two of such aircraft were delivered, in the first quarter of 2015, such that as at June 30, 2015, the Corporation had outstanding purchase commitments with Boeing for 29 Boeing 787 aircraft. One aircraft was, following its acquisition and delivery in the first quarter of 2015, included in the enhanced equipment trust certificates financing transaction as described in Note 4 Long-term Debt and Finance Leases and the other delivery was financed with EXIM financing support.

The Corporation also has purchase options for 13 Boeing 787 aircraft (entitling Air Canada to purchase aircraft based on previously determined pricing and delivery positions), and purchase rights for 10 Boeing 787 aircraft (entitling Air Canada to purchase aircraft based on Boeing's then current pricing).

Subject to certain conditions, the Corporation has various financing or sale and leaseback commitments available covering up to 24 of the remaining 29 Boeing 787 firm aircraft orders, which such commitments are summarized as follows:

- As described in Note 4 Long-term Debt and Finance Leases, for eight Boeing 787-9 aircraft, which are currently scheduled for delivery from July 2015 to March 2016, Air Canada announced the closing of a private offering of enhanced equipment trust certificates.
- For 14 of the Boeing 787 aircraft, the financing terms are for 80% of the aircraft delivery price and the term to maturity is 12 years with straight-line principal repayments.
- A sale and leaseback transaction with a third party for two Boeing 787 firm aircraft.

In the first quarter of 2015, Air Canada and Boeing concluded an amendment to the Boeing 787 purchase agreement which substitutes the remaining seven Boeing 787-8 with seven Boeing 787-9 aircraft. Air Canada's Boeing 787 fleet is planned to be comprised of eight Boeing 787-8 aircraft, all of which were in Air Canada's operating fleet as at June 30, 2015, and 29 Boeing 787-9 aircraft which are scheduled for delivery between 2015 and 2019.

As described in Note 16 to the 2014 annual consolidated financial statements, the Corporation has outstanding purchase commitments with Boeing for the purchase of Boeing 737 MAX aircraft. This agreement includes firm orders for 33 737 MAX 8 and 28 737 MAX 9 aircraft with substitution rights between them as well as for the 737 MAX 7 aircraft. It also provides for purchase options for 18 Boeing 737 aircraft and certain rights to purchase an additional 30 Boeing 737 aircraft. Deliveries are scheduled to begin in 2017 with two aircraft, with the remaining deliveries between 2018 to 2021, subject to deferral and acceleration rights.

The Corporation has financing commitments, subject to certain conditions, covering all 61 of the Boeing 737 MAX firm aircraft orders. The financing terms are for 80% of the aircraft delivery price and the term to maturity is 10 years with mortgage-style repayments.

In 2014, the Corporation exercised purchase rights for two Boeing 777 aircraft, with scheduled deliveries in the second quarter of 2016. Financing alternatives will be considered prior to the planned delivery dates of these aircraft. As at June 30, 2015, the Corporation had purchase rights for 11 Boeing 777 (entitling the Corporation to purchase aircraft based on previously determined pricing).

As described in Note 16 to the 2014 annual consolidated financial statements, certain of the financing commitments for the Boeing 787 aircraft and/or the Boeing 737 MAX aircraft would be reduced based on allocation of the commitments between aircraft types to be determined by the Corporation. Following the closing of the private offering of enhanced equipment trust certificates, the Corporation completed the allocation of the commitments between aircraft types. The total committed financing on these Boeing 787 aircraft and/or the Boeing 737 MAX aircraft, including commitments from the private offering of enhanced equipment trust certificates and the sale and leaseback transaction with a third party will be at least $6,155.

Capital Commitments

The estimated aggregate cost of the future firm Boeing 787, Boeing 777 and Boeing 737 MAX aircraft deliveries and other capital purchase commitments as at June 30, 2015 approximates $8,551. U.S. dollar amounts are converted using the June 30, 2015 closing rate of CDN$1.249. The estimated aggregate cost of aircraft is based on delivery prices that include estimated escalation and, where applicable, deferred price delivery payment interest calculated based on the 90-day U.S. LIBOR rate at June 30, 2015.

	Remainder of 2015	2016	2017	2018	2019	Thereafter	Total
Capital commitments	$ 752	2,316	1,755	1,523	1,147	1,058	**$ 8,551**

Maturity Analysis

Principal and interest repayment requirements as at June 30, 2015 on Long-term debt and finance lease obligations are as follows.

Principal	Remainder of 2015	2016	2017	2018	2019	Thereafter	Total
Long-term debt obligations	$ 223	426	561	583	1,587	2,045	$ **5,425**
Finance lease obligations	38	34	35	42	39	103	**291**
	$ 261	**460**	**596**	**625**	**1,626**	**2,148**	**$ 5,716**

Interest	Remainder of 2015	2016	2017	2018	2019	Thereafter	Total
Long-term debt obligations	$ 138	260	260	207	178	184	$ **1,227**
Finance lease obligations	13	23	19	16	12	29	**112**
	$ 151	**283**	**279**	**223**	**190**	**213**	**$ 1,339**

9. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Refer also to Note 17 to the 2014 annual consolidated financial statements for information on the Corporation's risk management strategy.

Summary of Gain (Loss) on Fuel and Other Derivatives

	Three months ended June 30		Six months ended June 30	
	2015	2014	2015	2014
Fuel derivatives	$ -	$ 8	$ (4)	$ 6
Share forward contracts	5	28	9	14
Interest rate swaps	-	-	1	1
Gain (Loss) on Fuel and Other Derivatives	**$ 5**	**$ 36**	**$ 6**	**$ 21**

Fuel Price Risk Management

During the second quarter of 2015:

- The Corporation recorded a loss of less than $1 in Fuel and other derivatives related to fuel derivatives ($4 loss for the six months ended June 30, 2015; gain of $8 and $6 for the three and six months period ended June 30, 2014, respectively). These derivatives were not designated as hedges for accounting purposes.
- The Corporation purchased crude-oil call options covering a portion of 2015 fuel exposures. The cash premium related to these contracts was $9 ($17 for the six months ended June 30, 2015; $10 and $20 for the three and six months period ended June 30, 2014, respectively, for 2014 exposures).
- Fuel derivative contracts cash settled with a net fair value of $1 in favour of the Corporation ($1 in favour of the Corporation for the six months ended June 30, 2015; $11 and $18 in favour of the Corporation for the three and six months period ended June 30, 2014, respectively).
- The Corporation applies fuel hedge accounting for certain designated fuel derivatives prospectively from April 1, 2015. In the second quarter of 2015, premiums paid for option contracts and the time value of the option contracts of $1 was deferred as a cost of the hedge in other comprehensive income and will be reclassified to Aircraft fuel expense when the underlying hedged jet fuel is used.

  A summary of amounts related to fuel derivatives designated as hedging instruments at June 30, 2015 is presented below.

	Carrying amount of the hedging instrument				
	Nominal amount of the hedging instrument (in barrels)	Assets	Liabilities	Consolidated statement of financial position classification	Changes in fair value used for calculating hedge ineffectiveness
Cash flow hedge					
Fuel price risk – option contracts	2,580,000	$ 8	$ -	Prepaid expenses and other current assets	$ -

As of June 30, 2015, and based on the derivative structures in place as of that date, approximately 40% of the Corporation's anticipated purchases of jet fuel for the remainder of 2015 are hedged at an average West Texas Intermediate ("WTI") equivalent capped price of US$66 per barrel for WTI prices up to US$71 per barrel and an average equivalent capped price of US$72 per barrel for WTI prices above US$77 per barrel. The Corporation's contracts to hedge anticipated jet fuel purchases over the remainder of 2015 are comprised of call options with notional volumes of 5,790,000 barrels. The fair value of the fuel derivatives portfolio at June 30, 2015 is $16 in favour of the Corporation (As at December 31, 2014 – $4 in favour of the Corporation) and is recorded within Prepaid expenses and other current assets.

Foreign Exchange Risk Management

The level of foreign exchange derivatives entered into and their related maturity dates are dependent upon a number of factors, which include the amount of foreign revenue conversion available, U.S. dollar net cash flows, as well as the amount attributed to aircraft and debt payments. For the net U.S. dollar shortfall, the Corporation has increased its target coverage from 60% to 70% on a rolling 18 month basis. Based on the notional amount of currency derivatives outstanding at June 30, 2015, as further described below, approximately 72% of net U.S. cash outflows are hedged for the remainder of 2015 and 46% for 2016, resulting in derivative coverage of 55% over the next 18 months. U.S. dollar cash and investment reserves combined with derivative coverage results in 67% target coverage.

As at June 30, 2015, the Corporation had outstanding foreign currency options and swap agreements, settling in 2015 and 2016, to purchase at maturity $2,642 (US$2,116) of U.S. dollars at a weighted average rate of $1.1980 per US$1.00 (as at December 31, 2014 – $2,658 (US$2,292) with settlements in 2015 and 2016 at a weighted average rate of $1.0884 per $1.00 U.S. dollar). The Corporation also has protection in place to sell a portion of its excess Euros, Sterling and Yen (EUR $19, GBP $15, JPY $1,069) which settle in 2015 at weighted average rates of $1.1850, $1.5667, and $0.0084 per $1.00 U.S. dollar respectively (as at December 31, 2014 - EUR $35, GBP $27 with settlement in 2015 at weighted average rates of $1.2806 and $1.6217 respectively per $1.00 U.S. dollar).

The hedging structures put in place have various option pricing features, such as knock-out terms and profit cap limitations, and based on the assumed volatility used in the fair value calculation, the net fair value of these foreign currency contracts as at June 30, 2015 was $11 in favour of the Corporation (as at December 31, 2014 – $30 in favour of the Corporation). These derivative instruments have not been designated as hedges for accounting purposes and are recorded at fair value. During the second quarter of 2015, a loss of $13 was recorded in Foreign exchange gain (loss) related to these derivatives (gain of $41 for the first six months of 2015; loss of $89 and $93, respectively, for the three and six months period ended June 30, 2014). In the second quarter of 2015, foreign exchange derivative contracts cash settled with a net fair value of $9 in favour of the Corporation ($60 in favour of the Corporation for the first six months of 2015; $9 and $32 in favour of the Corporation, respectively for the three and six months period ended June 30, 2014).

The Corporation also holds U.S. dollar cash and investment reserves as an economic hedge against changes in the value of the U.S. dollar. U.S. dollar cash and short-term investment balances as at June 30, 2015 amounted to $920 (US$737) ($717(US$620) as at December 31, 2014). In the second quarter of 2015, an unrealized loss of $12 was recorded in Foreign exchange gain (loss) reflecting the change in Canadian equivalent market value of the U.S. dollar cash and short-term investment balances held ($59 in favour of the Corporation for the first six months of 2015; unrealized loss of $37 and $8, respectively for the three and six months period ended June 30, 2014).

Financial Instrument Fair Values in the Consolidated Statement of Financial Position

The carrying amounts reported in the consolidated statement of financial position for short term financial assets and liabilities, which includes Accounts receivable and Accounts payable and accrued liabilities, approximate fair values due to the immediate or short-term maturities of these financial instruments. Based on significant observable inputs (Level 2 in the fair value hierarchy), the estimated fair value of long term debt is $5,758 compared to its carrying value of $5,621.

The following is a classification of fair value measurements recognized in the consolidated statement of financial position using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. There are no changes in classifications or methods of measuring fair value from those disclosed in Note 17 to the 2014 annual consolidated financial statements. There were no transfers within the fair value hierarchy or change in the fair value of Level 3 assets during the six months ended June 30, 2015.

		Fair value measurements at reporting date using:		
	June 30, 2015	**Quoted prices in active markets for identical assets (Level 1)**	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Financial Assets				
Held–for–trading securities				
Cash equivalents	$ 282	$ –	$ 282	$ –
Short–term investments	1,944	–	1,944	–
Deposits and other assets				
Prepayment option on senior secured notes	4	–	–	4
Derivative instruments				
Fuel derivatives	16	–	16	–
Share forward contracts	77	–	77	–
Foreign exchange derivatives	21	–	21	–
Interest rate swaps	4	–	4	–
Total	**2,348**	**–**	**2,344**	**4**
Financial Liabilities				
Derivative instruments				
Foreign exchange derivatives	10	–	10	–
Total	**$ 10**	**$ –**	**$ 10**	**$ –**

Financial assets held by financial institutions in the form of cash and restricted cash have been excluded from the fair value measurement classification table above as they are not valued using a valuation technique.

10. REGIONAL AIRLINES EXPENSE

The Corporation has capacity purchase agreements with Jazz, Sky Regional and certain other regional carriers. Expenses associated with these arrangements are classified as Regional airlines expense on the consolidated statement of operations. Regional airlines expense consists of the following:

	Three months ended June 30		Six months ended June 30	
	2015	2014	2015	2014
Capacity purchase fees	$ 302	$ 294	$ 576	$ 575
Aircraft fuel	97	127	183	252
Airport and navigation	70	70	135	134
Sales and distribution costs	33	28	66	55
Other operating expenses	92	59	186	129
Regional airlines expense	**$ 594**	**$ 578**	**$ 1,146**	**$ 1,145**