

October 23, 2003

Mr. Calin Rovinescu
CEO Restructuring
Air Canada
Air Canada Centre
P.O. Box 14000, Station Airport
Dorval, Quebec
H4Y 1H4

Dear Mr. Rovinescu

I am in receipt of your letter dated October 21, 2003. Your specific comments on the issues raised by the Office of the Superintendent of Financial Institutions ("OSFI") will require further review by OSFI.

Notwithstanding this, I would like to make it clear that your letter contains a number of comments and assertions with which we strongly disagree. I will not attempt to address all of these in this response, but rather speak to certain points in your letter that we believe must be corrected at this time. I would also like to take this opportunity to address similar issues that were raised by your litigators, Stikeman Elliot, in a letter to Cole & Partners Ltd. which seem as well to misrepresent the events over the last few months.

First I would like to point out that OSFI did not present a framework to any parties. Rather, we have, over the last number of months, shared and discussed with Air Canada and union representatives alike a list of issues that OSFI believes should be considered by all stakeholders in the pension plans to address the future funding of the pension plans. These issues were first presented in a meeting between representatives of OSFI and Air Canada on August 28, 2003, and have been discussed with Air Canada on several other occasions. Your letter of October 21 is the first official response received by OSFI. It is surprising that throughout these discussions, this is the first time that Air Canada has raised concerns over OSFI's role. If concerns had been raised earlier, OSFI could have rectified Air Canada's misunderstanding.

Your comment that OSFI's proposal had been made after extensive consultation with the trade unions and retiree representatives is not correct. Any OSFI discussions on these issues have occurred equally amongst trade unions and retiree representatives, Air Canada and the Monitor. OSFI's role is not to negotiate a solution between the various parties. We recognize

that this is the role of Air Canada and the beneficiaries of the plans. The purpose of providing the discussion points and our communication in related meetings was to help parties move forward to prepare a proposal. Indeed, our actions were in large measure in response to various requests to clarify factors that OSFI would take into account in assessing whether or not a proposal was acceptable.

As you know, from the outset of this process, OSFI was insistent that all parties be appropriately represented so that discussions, such as that referred to in this letter, could proceed efficiently. It is disappointing that all parties are now being admonished by Air Canada for entering into these discussions.

I also want to emphasize that OSFI has been prepared to consider and support a fundamental change in the funding regulations precisely because we recognized that a successful restructuring could not be accomplished under the current rules. As OSFI has previously pointed out, any proposed change to the regulation will likely involve more than simply increasing the 5-year funding of solvency deficits to 10 years. This change in regulation will of necessity have some conditions attached to it. Although Air Canada has reached agreements with unions on a number of issues, it is important that Air Canada and the unions recognize that any agreement on plan funding that does not meet current regulatory requirements could only be implemented with the Government's approval in the form of changes to those requirements. It is appropriate, therefore, that the Government enter into adequate discussions. To do otherwise would cause further delay to this process. In developing any proposed amendments to legislation, the Government must be open to receive input and comments from all stakeholders in the pension plans and not just those of the employer.

You refer to OSFI's unwillingness to meet with creditor or investor representatives. As you are aware, OSFI's mandate is to regulate pension plans and in doing so to strive to protect the interests of plan beneficiaries. OSFI's mandate is not to negotiate policy or the application of the law with any party. In fact, OSFI is not in a position to do so. That said, OSFI has always been willing to clarify any issues or its position with the various stakeholders, including creditor and investor representatives. In fact, OSFI has never refused to meet with any person who has requested to meet with us. Recently, the unsecured creditors committee wrote to us requesting that OSFI broaden any communications concerning the "Proposed Regulations" so that they be given an opportunity to comment on them. We would be pleased to accommodate that request at the appropriate time.

As we have indicated to you in our letter of October 21, numerous requests were made for information necessary for us to understand the context of your concerns but to no avail. Therefore you can appreciate we take issue with the comments that OSFI has proceeded without the "reality check" of the marketplace.

A number of comments in your letter refer to OSFI's efforts as jeopardizing the restructuring of Air Canada and the continuation of the pension plans. However, OSFI has repeatedly informed Air Canada and various representatives of the plan beneficiaries that it was open to discuss any issues presented to them. It is therefore inappropriate that Air Canada is attributing its lack of effort to resolve these issues to OSFI and in doing so has characterized OSFI as being impractical and non-responsive to Air Canada's situation and as OSFI being the catalyst that "triggers the end of" the plan benefits.

Finally, all parties have been advised on numerous occasions that any decision on proposed amendments to the regulations lies with Cabinet on the recommendation of the Minister of Finance. It is expected that the Department of Finance in making a recommendation to the Minister will look to OSFI for its view on these proposed changes. Accordingly, OSFI must be free to receive comments and engage in discussions with all thereon.

We were pleased to see your opening statement in the letter which reads that "The preservation of these benefits was one of the cornerstones of Air Canada's labour cost realignment during the difficult labour negotiations of last May and we remain committed to maintaining existing benefits and avoiding termination of the Plans." It seems somewhat in contrast, however, to what has been reported in the financial press today with respect to the potential creditors motion to terminate the pension plans.

OSFI continues to be willing to discuss with you and the pension plan stakeholders any of these issues and to clarify any matters with interested persons.

Yours truly,

Nicholas Le Pan
Superintendent of Financial Institutions