Jazz Air Income Fund

Consolidated Financial Statements
December 31, 2009 and 2008

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February 9, 2010

Auditors' Report

To the Unitholders of Jazz Air Income Fund

We have audited the consolidated balance sheets of **Jazz Air Income Fund** as at December 31, 2009 and 2008 and the consolidated statements of unitholders' equity, income (loss), comprehensive income (loss) and cash flows for the years ended December 31, 2009 and 2008. These consolidated financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years ended December 31, 2009 and 2008 in accordance with Canadian generally accepted accounting principles.

(signed) "*PricewaterhouseCoopers LLP*"

Chartered Accountants
Halifax, Nova Scotia

February 9, 2010

Management's Report

The accompanying consolidated financial statements of Jazz Air Income Fund are the responsibility of management and have been approved by the Board of Trustees. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The consolidated financial statements include some amounts and assumptions based on management's best estimates which have been derived with careful judgement.

In fulfilling its responsibilities, management has developed and maintains a system of internal accounting controls. These controls are designed to provide reasonable assurance that the financial records are reliable for preparation of the financial statements. The Audit, Finance and Risk Committee of the Board of Trustees reviewed and approved Jazz's consolidated financial statements, and recommended their approval by the Board of Trustees.

(signed) "Joseph D. Randell"
President and Chief Executive Officer

(signed) "Allan D. Rowe"
Chief Financial Officer

Jazz Air Income Fund
Consolidated Balance Sheets
As at December 31, 2009 and 2008

(expressed in thousands of Canadian dollars)

	2009 $	2008 $
Assets		
Current assets		
Cash and cash equivalents	223,559	131,876
Accounts receivable – trade and other (note 15)	59,044	71,618
Spare parts, materials and supplies	40,755	46,150
Prepaid expenses	19,909	12,905
Total current assets	343,267	262,549
Property and equipment (note 3)	202,994	219,028
Intangible assets (note 4)	682,479	722,102
Other assets (note 6)	37,731	29,468
	1,266,471	1,233,147
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 15)	179,216	197,046
Distributions payable	6,143	10,296
Current portion of obligations under capital leases (note 7)	2,681	2,837
Current portion of long-term debt (note 8)	114,706	-
Total current liabilities	302,746	210,179
Obligations under capital leases (note 7)	15,097	20,581
Long-term debt (note 8)	-	114,729
Convertible debentures (note 9)	78,180	-
Future income tax (note 10)	13,294	23,561
Other long-term liabilities (note 11)	52,699	56,068
	462,016	425,118
Unitholders' Equity	804,455	808,029
	1,266,471	1,233,147

Economic dependence (note 15)
Commitments (note 16)
Contingencies (note 22)
Subsequent event (note 23)

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

Approved by the Trustees

By: (signed) *"Katherine M. Lee"*
Trustee

By: (signed) *"Richard H. McCoy"*
Trustee

Jazz Air Income Fund

Consolidated Statements of Unitholders' Equity

For years ended December 31, 2009 and 2008

(expressed in thousands of Canadian dollars)

	Unitholders' capital $	Retained earnings (deficit) Accumulated earnings $	Retained earnings (deficit) Distributions $	Contributed surplus $	Accumulated other comprehensive income (loss) $	Equity component of convertible debentures $	Total $
Balance - December 31, 2007	1,034,656	29,512	(127,186)	5,952	(158)	-	942,776
Change in fair value during the year	-	-	-	-	(3,028)	-	(3,028)
Distributions	-	-	(123,552)	-	-	-	(123,552)
Units held by unit based compensation plans (note 18)	(205)	-	-	(1,626)	-	-	(1,831)
Accretion related to the initial long-term incentive plan (note 18)	-	-	-	1,850	-	-	1,850
Accretion related to the ongoing long-term incentive plan (note 18)	-	-	-	1,224	-	-	1,224
Net loss for the year	-	(9,410)	-	-	-	-	(9,410)
Balance - December 31, 2008	1,034,451	20,102	(250,738)	7,400	(3,186)	-	808,029
Change in fair value during the year	-	-	-	-	2,384	-	2,384
Distributions	-	-	(102,787)	-	-		(102,787)
Issue of convertible debentures (note 9)	-	-	-	-	-	4,324	4,324
Units held by unit based compensation plans (note 18)	829	-	-	(2,879)	-	-	(2,050)
Accretion related to the ongoing long-term incentive plan (note 18)	-	-	-	1,917	-	-	1,917
Net income for the year	-	92,638	-	-	-	-	92,638
Balance - December 31, 2009	1,035,280	112,740	(353,525)	6,438	(802)	4,324	804,455

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

Jazz Air Income Fund

Consolidated Statements of Income (Loss)

For the years ended December 31, 2009 and 2008

(expressed in thousands of Canadian dollars, except Units and earnings per Unit)

	2009 $	2008 $
Operating revenue (note 15)		
Passenger	1,463,623	1,622,850
Other	10,277	13,439
	1,473,900	1,636,289
Operating expenses (note 15)		
Salaries and wages	293,958	292,647
Benefits	50,547	52,563
Aircraft fuel	255,842	430,216
Depreciation and amortization of property and equipment and other	30,689	30,409
Amortization of Capacity Purchase Agreement ("CPA") intangible asset	39,623	42,100
Food, beverage and supplies	13,097	14,795
Aircraft maintenance materials, supplies and services	163,677	129,533
Airport and navigation fees	192,039	199,419
Aircraft rent	135,680	127,758
Terminal handling services	101,984	107,345
Other	107,990	103,333
	1,385,126	1,530,118
Operating income	88,774	106,171
Non-operating income (expenses)		
Interest revenue	760	4,236
Interest expense	(8,607)	(8,505)
Gain on disposal of property and equipment	1,936	182
Foreign exchange loss	(1,142)	(6,263)
Goodwill impairment loss (note 5)	-	(153,230)
Unrealized gain (loss) on asset backed commercial paper ("ABCP") (note 21)	650	(2,985)
	(6,403)	(166,565)
Income (loss) before future income taxes	82,371	(60,394)
Recovery of future income taxes (note 10)	10,267	50,984
Net income (loss) for the years	92,638	(9,410)
Earnings (loss) per Unit, basic (note 13)	$0.76	$(0.08)
Earnings (loss) per Unit, diluted (note 13)	$0.75	$(0.08)

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

Jazz Air Income Fund

Unaudited Consolidated Statements of Comprehensive Income (Loss)

For the years ended December 31, 2009 and 2008

(expressed in thousands of Canadian dollars)

	2009 $	2008 $
Net income (loss) for the years	92,638	(9,410)
Other comprehensive income (loss)		
Change in fair value of derivatives designated as cash flow hedges	(293)	(2,408)
Reclassification of net realized gains on derivatives designated as cash flow hedges to income	2,677	(620)
Comprehensive income (loss)	95,022	(12,438)

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

Jazz Air Income Fund

Consolidated Statements of Cash Flows

For the years ended December 31, 2009 and 2008

(expressed in thousands of Canadian dollars)

	2009 $	2008 $
Cash provided by (used in)		
Operating activities		
Net income (loss) for the years	92,638	(9,410)
Charges (credits) to operations not involving cash		
Depreciation and amortization of property and equipment and other	30,689	30,409
Amortization of CPA intangible asset (note 2)	39,623	42,100
Amortization of prepaid aircraft rent and related fees	1,929	1,928
Gain on disposal of property and equipment	(1,936)	(182)
Unit based compensation	1,917	3,074
Foreign exchange (gain) loss	(2,843)	4,090
Future income taxes	(10,267)	(50,984)
Accretion of debt component of convertible debentures	239	-
Goodwill impairment loss	-	153,230
Unrealized (gain) loss on asset backed commercial paper	(650)	2,985
Other	(302)	(1,383)
Funding of unit based compensation plan, net of forfeitures	(2,050)	(1,831)
	148,987	174,026
Net changes in non-cash working capital balances related to operations (note 14)	(18,898)	(18,938)
	130,089	155,088
Financing activities		
Repayment of obligations under capital leases (note 7)	(2,669)	(2,265)
Convertible debentures, net of issue costs	82,265	-
Distributions	(106,940)	(123,552)
	(27,344)	(125,817)
Investing activities		
Additions to property and equipment	(13,417)	(20,661)
Decrease in long-term receivables	419	210
Proceeds on disposal of property and equipment	1,936	182
	(11,062)	(20,269)
Net change in cash and cash equivalents during the years	91,683	9,002
Cash and cash equivalents – Beginning of years	131,876	122,874
Cash and cash equivalents – End of years	223,559	131,876
Cash payments of interest	9,026	10,747
Cash receipts of interest	837	4,579
Cash and cash equivalents comprise:		
Cash	36,273	29,042
Term deposits and fixed income securities	187,286	102,834

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

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

1 Nature of operations and economic dependence

Jazz Air Income Fund (the "Fund") is an unincorporated, open-ended trust established under the laws of the Province of Ontario by a declaration of trust dated November 25, 2005 and amended by an amended and restated declaration of trust dated January 24, 2006, and an amending agreement dated as of March 23, 2009 (the "Jazz Declaration of Trust"). The Fund qualifies as a "mutual fund trust" for the purposes of the Income Tax Act (Canada). The principal and head office of the Fund is located at 1000 de la Gauchetière Street West, Suite 2100, Montréal, Québec H3B 4W5. The Fund has been established to acquire and hold, directly or indirectly, investments in Jazz Air LP (the "Partnership") and its general partner Jazz Air Holding GP Inc. ("Jazz GP"), a regional airline, and such other investments as the Board of Trustees of the Fund (the "Trustees") may determine. Reference to Jazz in the following notes to the consolidated financial statements refers to, as the context may require, the Fund and its subsidiaries (Jazz Air Trust (the "Trust"), the Partnership and Jazz GP) collectively, the Fund and one or more of its subsidiaries, one or more of the Fund's subsidiaries or the Fund itself.

Jazz operates a regional airline in Canada and the United States. Jazz forms an integral part of Air Canada's domestic and transborder market presence and strategy. Jazz and Air Canada are parties to an amended and restated capacity purchase agreement, effective January 1, 2006, as amended by a letter agreement (the "Rate Amending Agreement") dated July 28, 2009 and an amending agreement (the "CPA Amending Agreement") dated September 22, 2009 (as amended, the "CPA"), pursuant to which Air Canada purchases substantially all of Jazz's fleet capacity on aircraft operated by Jazz (the "Covered Aircraft"), based on predetermined rates (the "Rates") charged by Jazz to Air Canada for operating the Covered Aircraft. Jazz is economically and commercially dependent upon Air Canada and certain of its subsidiaries, as, in addition to being the primary source of revenue, these entities currently provide significant services to Jazz. In addition, Air Canada and its subsidiaries provide a substantial portion of the aircraft financing for Jazz.

Jazz has historically experienced 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, thereby increasing the flying hour requirements of Air Canada. Jazz has substantial fixed costs that do not meaningfully fluctuate with passenger demand in the short-term. Jazz revenues under the CPA do not fluctuate significantly with passenger load factors.

2 Significant accounting policies

a) Basis of presentation

These consolidated financial statements are expressed in Canadian dollars and are prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Actual results could differ from those estimates.

b) Principles of consolidation

These consolidated financial statements include the accounts of Jazz, and the consolidated accounts of the Partnership, the variable interest entity for which Jazz is the primary beneficiary. All inter-company and inter-entity balances and transactions are eliminated.

c) Variable Interest Entities

At its inception, Jazz adopted Accounting Guideline 15 ("AcG 15") - *Consolidation of Variable Interest Entities ("VIE")*. AcG 15 defines a VIE as an entity that either does not have sufficient equity at risk to finance its activities without subordinated financial support from other parties, or where the equity investors lack the characteristic of a controlling financial interest, or that do not absorb the expected losses or receive the expected returns of the entity. VIEs are subject to consolidation by an entity if that entity is deemed the primary beneficiary of the VIE. The primary beneficiary is the party that is either exposed to a majority of the losses from the VIE's activities or is entitled to receive a majority of the VIE's residual returns or both.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

2 Significant accounting policies (continued)

Management has reviewed its ownership, contractual and financial interests in other entities and determined that, other than the consolidation of the consolidated accounts of the Partnership and unit based compensation plans referred to in note 2(g), this guideline does not impact the financial statements of Jazz.

d) Cash and cash equivalents

Cash and cash equivalents consist of current operating bank accounts, term deposits and fixed income securities with an original term to maturity of 90 days or less. The weighted average interest rate on investments as at December 31, 2009 is 0.32% (2008 – 1.62%).

e) Operating revenue

Under the CPA, Jazz is paid to provide services to Air Canada as explained in notes 1 and 15. The related fees payable by Air Canada are recognized in revenue as the capacity is provided. Incentive payments and margin adjustments as described in note 15 are recognized, respectively, as increases in and reductions of, passenger revenue based on management estimates during the year.

Other revenues include charter flights, maintenance, repair and overhaul ("MRO") operations and other sources of revenue such as third party ground handling services and flight simulator revenue, all of which are recognized when the service is provided.

The CPA with Air Canada provides for a monthly payment for an amount per aircraft designed to reimburse Jazz for certain aircraft ownership costs. In accordance with Emerging Issues Committee No. 150, *Determining Whether an Arrangement Contains a Lease*, Jazz has concluded that a component of its revenue under the CPA is rental income since the CPA identifies the "right of use" of a specific type and number of aircraft over a stated period of time otherwise known as the Covered Aircraft. The amount deemed to be rental income is $175,966 for the year ended December 31, 2009 (2008 - $168,974). This amount was recorded in passenger revenue of Jazz's consolidated statements of income.

f) Employee future benefits

The significant policies related to employee future benefits, consistent with Section 3461, "*Employee Future Benefits"* of the Canadian Institute of Chartered Accountants ("CICA") Handbook relating to Jazz's defined benefit pension plan for its pilots, the supplemental executive retirement plan for Jazz executives, and the Other Employee Future Benefits are as follows:

- The cost of pensions earned by employees is actuarially determined using the projected benefit method prorated on service, market interest rates, and management's best estimate of expected plan investment performance, salary escalation and retirement ages of employees. Obligations are attributed to the period beginning on the employee's date of joining the plan and ending on the earlier of the date of termination, death or retirement.

- The cost of the Other Employee Future Benefits is actuarially determined using the projected benefit method prorated on service (where applicable), market interest rates, and management's best estimate of retirement ages of employees, health care cost inflation, salary escalation and general inflation.

- The expected return on plan assets is based on the long-term expected rate of return on plan assets and the fair value of the plan assets. It is reasonably possible that management's estimate of the long-term rate of return may change as management continues to assess future investments and strategies and as a result of changes in financial markets.

- Past service costs arising from plan amendments of the defined benefit pension plan and the supplemental executive retirement plan are amortized on a straight-line basis over the average remaining service period of employees active at the date of the amendment. This period is currently 19 years for the pension plan and 14 years for the supplemental executive retirement plan.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

2 Significant accounting policies (continued)

- Cumulative unrecognized net actuarial gains and losses of the defined benefit pension plan and the supplemental executive retirement plan in excess of 10% of the greater of the accrued benefit obligation and the market value of plan assets at the beginning of the year are amortized over the average remaining service periods of active members expected to receive benefits under the plan (currently 19 years for the pension plan and 14 years for the supplemental executive retirement plan).
- The fiscal year-end date is December 31 and the measurement date of the plan's assets and obligations is December 31. Pension obligations are attributed to the period beginning on the employee's date of joining the plan and ending on the earlier of the date of termination, death or retirement. The obligations for the Other Employee Future Benefits plans are attributed to the period beginning on the employee's date of joining the plan or disablement (whichever applicable) and ending on the earlier of retirement or end of disablement or age 65 (whichever applicable).

g) Unit based compensation

Initial long-term incentive plan

Jazz has made certain commitments in connection with the granting of Units to key executives as a one-time special award to recognize their efforts in connection with the completion of the initial public offering of the Jazz Air Income Fund ("Offering") and to provide them with incentive compensation under an Initial Long-Term Incentive Plan ("Initial LTIP"). On February 9, 2007, ACE Aviation Holdings Inc. ("ACE") transferred 638,223 Units to a trust for the purpose of funding the Initial LTIP. Under the terms of the Initial LTIP, 50% of the Units granted are subject to vesting conditions based on performance and the remaining 50% are time based and vested on December 31, 2008. Vesting is conditional on the approval of the board of directors. Performance based Units vest (1/3 per year) if the distributable cash target established by the board of directors, on behalf of Jazz GP, for the year is met. The distributable cash targets were met in each of the years, including the year ended December 31, 2008 and the related units vested.

Compensation costs related to the Units contributed by ACE are charged to compensation expense over the vesting period, as vesting conditions are met and based on the estimated annual performance, with the corresponding equity contribution being accreted to contributed surplus. Distributions declared by Jazz on the Units granted ultimately accrue to the employees. Forfeited Units, to the extent they were contributed by ACE, and accumulated distributions thereon, accrue to ACE. The trust is a VIE with respect to Jazz, and as such it is consolidated with Jazz's financial statements. Units contributed by ACE are credited to contributed surplus at their aggregate value on February 9, 2007, the contribution date, with an equivalent reduction of Unit holders' (the "Unitholders") capital. Compensation expense under this plan is charged to earnings over the vesting period, with a corresponding increase to equity. At December 31, 2009, the Initial LTIP is no longer in effect.

Ongoing long-term incentive plan

Under the terms of the Ongoing Long-term Incentive Plan ("Ongoing LTIP"), eligible employees are entitled to yearly Unit grants determined on the basis of a percentage of their annual base salary. The Units, which are held in a trust for the benefit of the eligible employees, vest at the end of a three year period (the "Performance Cycle"), commencing January 1 of the year in respect of which they are granted, subject to achieving distributable cash targets, established by the board of directors, on behalf of Jazz GP, for the Performance Cycle. Jazz has the option to issue the Units from treasury or purchase them on the secondary market. If Jazz chooses to issue Units from treasury, the Units will be granted on a deferred basis. On the grant date, plan members will be credited with the deferred Units granted to them. Grantees are also entitled to receive additional deferred Units based on cash distributions that would have been received had the deferred Units been converted to Jazz Units at the time of issuance. Distributions declared by Jazz on any Units granted under this plan, may be invested in additional Units, which will vest concurrently and proportionately with the Units granted. Forfeited Units and accumulated distributions thereon accrue to Jazz. The trust is a VIE with respect to Jazz, and as such, it is consolidated with Jazz's financial statements. The fair value of the Units, which approximates their cost under this plan, is charged to earnings as compensation expense over the vesting period, with a corresponding increase to equity. Jazz's cost of the Units held is presented as a reduction of Unitholders' capital. Estimated compensation costs relative to this plan are accrued on the basis of actual performance relative to targets.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

2 Significant accounting policies (continued)

h) Financial instruments

Financial instruments are classified as follows:

- Cash and cash equivalents are classified as "Financial Assets Held for Trading". These financial assets are marked-to-market through net income at each period end.
- Accounts receivable are classified as "Loans and Receivables". After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method. Allowances for doubtful accounts are established by management, on an account-by-account basis, based on, among other factors, prior experience and knowledge of the specific debtor and its assessment of the current economic environment.
- Accounts payable, distributions payable, credit facilities, and convertible debentures are classified as "Other Financial Liabilities". After their initial fair value measurement they are measured at amortized cost, net of transaction costs, using the effective interest rate method.

i) Hedges

Jazz applies hedge accounting to its interest rate swaps and treats them as cash flow hedges. These derivatives are marked-to-market at each period end and resulting gains/losses are recognized in comprehensive income to the extent the hedging relationship is effective.

j) Property and equipment

Property and equipment are depreciated to estimated residual values based on the straight-line method over their estimated service lives. Aircraft and flight equipment are depreciated over 20 to 30 years, with 5 - 20% estimated average residual values.

Buildings are depreciated over their useful lives not exceeding 40 years on a straight-line basis. An exception to this is where the useful life of the building is greater than the term of the land lease. In these circumstances, the building is depreciated over the life of the lease.

Depreciation on other property and equipment is provided on a straight-line basis from the date assets are placed in service, to their estimated residual values, over the following estimated useful lives:

Leaseholds	Over the term of the related lease
Ground and other equipment	5 years

Property under capital leases and the related obligation for future lease payments are initially recorded at an amount equal to the lesser of fair value of the property or equipment and the present value of those lease payments. Property and equipment under capital leases are depreciated to estimated residual value over the life of the lease.

Property and equipment is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be used is measured by comparing the net book value of the asset to the undiscounted future cash flows expected to be generated by the asset. An impairment is recognized to the extent that the carrying amount exceeds the fair value of the asset.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

2 Significant accounting policies (continued)

k) Transaction costs

Transaction costs that are incremental and directly attributable to the acquisition or issue of a financial asset or financial liability are recorded as follows:

- Held for trading – expensed as incurred; and
- Loans and receivables, and other liabilities – included in the carrying value of the financial asset or financial liability and amortized over the expected life of the financial instrument using the effective interest method.

Transaction costs for operating leases are capitalized and amortized over the life of the lease on a straight-line basis.

l) Intangible assets and goodwill

Intangible assets with finite lives are carried at their cost, net of amortization; while assets with indefinite lives are not amortized and are reviewed annually for impairment.

The CPA intangible asset has a finite life, is carried at cost and amortized over the initial term of the CPA plus renewal periods.

Goodwill represents the excess of the acquisition cost of companies over the fair value of the identifiable net assets acquired and is not amortized. At December 31, 2008, Jazz determined its goodwill was fully impaired and recorded a write-down of $153,230.

m) Impairment of long-lived assets

Long-lived assets are tested for impairment whenever circumstances indicate that the carrying value may not be recoverable. When events or circumstances indicate that the carrying amount of long-lived assets, other than indefinite life intangibles, are not recoverable, the long-lived assets are tested for impairment by comparing the estimate of future expected cash flows to the carrying amount of the assets or groups of assets. If the carrying value is not recoverable from future expected cash flows, any loss is measured as the amount by which the asset's carrying value exceeds fair value and recorded in the period. Recoverability is assessed relative to undiscounted cash flows from the direct use and disposition of the asset or group of assets.

Indefinite life assets are subject to annual impairment tests under GAAP, or when events or circumstances indicate a potential impairment. Any impairment would be recognized as an expense in the period of impairment.

n) Foreign currency translation

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates of exchange in effect at the date of the balance sheet. Non-monetary assets, liabilities and other items recorded in income are translated at rates of exchange in effect at the date of the transaction. Foreign exchange losses of $1,142 for the year ended December 31, 2009 (2008 - $6,263) were included in other non-operating income/expense.

o) Aircraft lease payments

Total aircraft rentals under operating leases and the related lease inducements received and fees paid over the lease term are amortized to operating expense on a straight-line basis. Prepaid aircraft rentals and related fees are the difference between the straight-line aircraft rent and the payments stipulated under the lease agreements and legal and related transaction fees associated with the leases. Current and non-current unamortized lease inducements are included in accounts payable and accrued liabilities and other long-term liabilities, respectively.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

2 Significant accounting policies (continued)

p) Spare parts, materials and supplies

Spare parts, materials and supplies are valued at the lower of cost, determined on a first in, first out basis, and net realizable value. For the year ended December 31, 2009, the cost of inventories recognized as expense was $38,206 (2008 - $37,277). For the year ended December 31, 2009, inventory writedowns to net realizable value of $3,359 were recognized as an expense (2008 - $431).

q) Maintenance and repairs

Maintenance and repair costs are charged to operating expenses as incurred. Significant modification costs considered to be betterments are capitalized and amortized over the remaining service lives of the applicable assets.

Jazz uses the direct expense method of accounting for its airframe overhauls where the expense is recorded when the overhaul event occurs. Jazz has most of its aircraft engines under long-term engine service agreements that cover the scheduled and unscheduled repairs for the covered engines. Under the terms of the agreements, Jazz pays a set dollar amount per engine hour flown on a monthly basis and the third party vendor assumes the responsibility to repair the engines at no additional cost to Jazz, subject to certain specified exclusions. Maintenance costs under these contracts are recognized when a contractual obligation exists. For those engines not covered under a long-term engine service agreement, the overhaul events are expensed in the period when the event occurs. The costs of maintenance for airframe and avionics components, landing gear and normal recurring maintenance are expensed as incurred.

r) Future income tax

Jazz uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the year that includes the date of enactment or substantive enactment.

s) Earnings per Unit

Earnings per Unit are calculated on a weighted average number of units outstanding basis. Units held under the Unit based compensation plans reduce the weighted average number of outstanding Units from the date they are contributed to the plan.

Diluted earnings per Unit are calculated using the "if converted" method. Under this method, the interest charges on convertible debentures are added back to the numerator, net of tax. The convertible debentures are considered to have been issued at the beginning of the period on time of issuance and the resulting weighted average dilutive Units are included in the denominator.

t) Distribution to Unitholders

Distributions payable by Jazz to its Unitholders, which are determined at the discretion of the Trustees, are recorded when declared.

Changes in accounting policies

Goodwill and Intangible Assets

In February 2008, the Canadian Accounting Standards Board ("AcSB") issued Section 3064, "*Goodwill and Intangible Assets*", to replace Section 3062, "*Goodwill and Other Intangible Assets*". This new section establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets by profit-oriented enterprises. The adoption of this new section had no impact on Jazz's consolidated financial statements.

2 Significant accounting policies (continued)

Financial Instruments

In June 2009, the AcSB issued amendments to Section 3862, *"Financial Instruments - Disclosures"*, to require enhanced disclosures about the relative reliability of the data, or "inputs", that an entity uses in measuring the fair values of its financial instruments. The new requirements are effective for annual financial statements for fiscal years ending after September 30, 2009. The additional disclosures are included in note 21.

Credit Risk and Fair Value of Financial Assets and Financial Liabilities

On January 20, 2009, the Emerging Issues Committee ("EIC") of the Canadian Accounting Standards Board issued EIC Abstract 173, *"Credit Risk and Fair Value of Financial Assets and Financial Liabilities"*, which establishes guidance requiring an entity to consider its own credit risk as well as the credit risk of the counterparty in determining the fair value of financial assets and financial liabilities, including derivative instruments. This interpretation must be applied retrospectively without restatement of prior years. The adoption of this interpretation did not have a significant impact on Jazz's consolidated financial statements.

Change in accounting estimate

In the fourth quarter of 2009, Jazz changed its estimate of the useful life of the CPA intangible asset to coincide with the extended term of the CPA provided under the CPA Amending Agreement. This change has been applied prospectively. The change had the effect of decreasing amortization by $2,477 for the year ended December 31, 2009.

Future accounting changes

Convergence with International Financial Reporting Standards ("IFRS")

In January 2006, the AcSB announced its decision to replace Canadian GAAP with IFRS. On February 13, 2008 the AcSB confirmed January 1, 2011 as the mandatory changeover date to IFRS for all Canadian publicly accountable enterprises. This means that Jazz will be required to prepare IFRS financial statements for the interim periods and fiscal year ends beginning in 2011. Jazz has created an implementation team, which consists of internal resources and an external consultant. A changeover plan is being established to convert to the new standards within the allotted timeline and consists of the following phases: raise awareness and initial assessment; detailed assessment; and implementation and review. Phase 1 was completed in the third quarter of 2008. Jazz continues to work on Phase 2 and has commenced work on Phase 3. At this time, Jazz does not believe any significant changes to the financial reporting system will be necessary to facilitate the change-over.

Business Combinations, Consolidated Financial Statements and Non-controlling Interests

In January 2009, the CICA issued Section 1582, *"Business Combinations"*, Section 1601, *"Consolidated Financial Statements"*, and Section 1602, *"Non-controlling Interests"* which replace Section 1581, *"Business Combinations"* and Section 1600, *"Consolidated Financial Statements"*. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Early adoption of this section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the entity's interim and annual consolidated financial statements for fiscal years beginning on or after January 1, 2011. Early adoption of this section is permitted. If the entity chooses to early adopt any one of these sections, the other two sections must also be adopted at the same time.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

3 Property and equipment

	As at December 31, 2009		
	Cost $	Accumulated amortization $	Net $
Flight equipment	167,114	26,347	140,767
Facilities	14,294	1,625	12,669
Equipment	27,855	13,101	14,754
Leaseholds	32,473	14,172	18,301
Assets under capital leases	23,201	6,698	16,503
	264,937	61,943	202,994

	As at December 31, 2008		
	Cost $	Accumulated amortization $	Net $
Flight equipment	160,204	13,504	146,700
Facilities	14,137	984	13,153
Equipment	23,893	7,206	16,687
Leaseholds	31,586	8,448	23,138
Assets under capital leases	23,201	3,851	19,350
	253,021	33,993	219,028

The net book value of the property and equipment pledged as collateral under the credit facility at December 31, 2009 was $186,491 (2008 - $199,678). Amortization expense related to property and equipment of $30,526 was recorded for the year ended December 31, 2009 (2008 - $28,926).

4 Intangible assets

	As at December 31, 2009		
	Cost $	Accumulated amortization $	Net $
Indefinite life assets			
Jazz tradename	1,836	-	1,836
Operating license	4,600	-	4,600
Finite life assets			
CPA	783,184	107,141	676,043
	789,620	107,141	682,479

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

4 Intangible assets (continued)

	As at December 31, 2008		
	Cost $	Accumulated amortization $	Net $
Indefinite life assets			
Jazz tradename	1,836	-	1,836
Operating license	4,600	-	4,600
Finite life assets			
CPA	783,184	67,518	715,666
	789,620	67,518	722,102

During the year ended December 31, 2009, Jazz recorded amortization expense of $39,623 (2008 - $42,883).

5 Goodwill

	As at December 31, 2009 $	2008 $
Opening balance - December 31	-	147,284
Goodwill adjustment (1)	-	5,946
Goodwill impairment loss	-	(153,230)
Closing balance - December 31	-	-

(1) During the second quarter of 2008, Jazz adjusted the purchase price allocation to reflect certain previously unrecorded long-term liabilities related to post-employment future benefits, which were assumed by the Partnership upon inception. This resulted in an increase in goodwill of $5,946.

At December 31, 2008 Jazz performed an impairment test of goodwill to compare its carrying value to fair value. The impairment test is based on a two step process. In step one a fair value was determined using two different valuation methods, a market based approach and a Discounted Cash Flow ("DCF") approach. The market based approach derives a fair value based on the market capitalization of Jazz. The DCF approach analyzes future cash flows based on internally developed forecasts and then discounts them based on an industry average weighted average cost of capital. Step one showed a carrying value that exceeded fair value and as a result Jazz proceeded to perform step two.

Step two required the fair value determined in step one to be allocated to each individual asset and liability (including any previously unrecognized intangible assets), as it would be in a business combination. After performing this allocation there was no remaining fair value to be allocated to goodwill and as a result, the entire $153,230 of goodwill was deemed to be impaired. The impairment loss was recorded in non-operating expenses.

The circumstances that led to the impairment of goodwill were as a result of the challenges and uncertainties in the airline industry.

In determining fair value, management relied on a number of factors including operating results, business plans, anticipated future cash flows and marketplace data. There are inherent uncertainties related to these factors and management's judgment in applying them to the analysis of goodwill impairment.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

6 Other assets

	As at December 31, 2009 $	2008 $
Promissory note receivable, non-interest bearing, repayable in equal annual installments over 10 years	-	419
Prepaid aircraft rent and related fees, net of accumulated amortization	25,362	26,644
Accrued pension benefit asset (note 19)	11,316	396
Asset backed commercial paper (note 21)	1,053	2,009
	37,731	29,468

7 Obligations under capital leases

Jazz has entered into capital leases related to aircraft and ground equipment. The obligations are as follows:

	2009 $	2008 $
Year ended December 31, 2009	-	4,796
2010	4,147	4,796
2011	4,119	4,764
2012	3,772	4,367
2013	3,746	4,341
2014	3,746	-
Thereafter	3,164	8,008
Total minimum lease payments	22,694	31,072
Less: Amount representing interest (at rates ranging from 8.755% to 9.450%)	4,916	7,654
Present value of net minimum capital lease payments	17,778	23,418
Less: Current portion	2,681	2,837
Obligations under capital leases	15,097	20,581

A significant portion of the lease payments is payable in US dollars. Interest of $1,815 (2008 - $1,895) relating to capital lease obligations has been included in aircraft rent.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

8 Long-term debt

The following provides a breakdown of Jazz's authorized and outstanding credit facilities:

	Authorized $	Drawn at December 31, 2009 $	Drawn at December 31, 2008 $
Revolving term facility [a]	35,000	-	-
Term facility [b]	115,000	115,000	115,000
Prepaid interest [c]	-	(294)	(213)
Unamortized commitment fee [c]	-	-	(58)
	150,000	114,706	114,729
Less: Current portion	-	114,706	-
Total	150,000	-	114,729

(a) The revolving term facility matures on February 1, 2010 (refer to note 23) and bears interest at rates ranging from Canadian prime rate and US base rate plus 1.75% to 2.75% and the bankers' acceptance rate and LIBOR plus 2.75% to 3.75%. As at December 31, 2009, there were no borrowings under the revolving term facility. Available credit under the revolving term facility, after deducting letters of credit, bears interest at 0.50%. Interest expense on the credit facility for the year ended December 31, 2009 was $7,415 (2008 - $8,482).

Letters of credit

Jazz has issued irrevocable letters of credit in the aggregate amount of $3,241. This amount reduces the available credit under the revolving term facility and bears interest at 2.875%.

(b) The term facility matures on February 1, 2010 (refer to note 23) and bears interest at rates ranging from Canadian prime rate and US base rate plus 1.75% to 2.75% and the bankers' acceptance rate and LIBOR plus 2.75% to 3.75%. As at December 31, 2009, of borrowings under the term facility, $114,400 were in the form of bankers' acceptances with a 90 day term and an effective interest rate of 3.20%. A further $600 was in the form of prime rate advances bearing interest at 4.00%. As at December 31, 2009, Jazz had entered into interest rate swap agreements with a third party in respect of $115,000 of debt which has effectively resulted in a fixed interest rate of 5.98% until February 2, 2010.

(c) Long-term debt is presented net of prepaid interest and unamortized financing charges.

Borrowings under the credit facilities are secured by substantially all the present and future assets of Jazz. The continued availability of the credit facilities is subject to Jazz's ability to maintain certain leverage, debt service and interest coverage covenants, as well as other affirmative and negative covenants. As at December 31, 2009, Jazz is in compliance with all debt covenants.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

9 Convertible debentures

On October 22, 2009, Jazz announced that it had entered into an agreement to sell to a group of underwriters $75,000 principal amount of 9.50% convertible unsecured subordinated debentures (the “Debentures”). This transaction closed on November 12, 2009. Jazz granted the underwriters an option, exercisable in whole or in part at any time up until 30 days after the closing date, to purchase an additional $11,250 principal amount of Debentures, at the same price. This option was exercised on November 25, 2009. The total gross proceeds of the financing were $86,250. The net proceeds received by Jazz from the sale of Debentures were $82,265 after deduction of the underwriters’ fee and the expenses of the offering. Proceeds from the offering will be used for working capital requirements and for general purposes of Jazz.

The Debentures bear interest at a rate of 9.50% per annum, payable semi-annually in arrears on June 30 and December 31 in each year commencing on June 30, 2010, and will mature on December 31, 2014 (the “Maturity Date”). The Debentures are convertible at the holder's option into Units of Jazz at any time prior to 5:00 pm (EST), the earlier of the Maturity Date and the date fixed for redemption at a conversion price of $5.25 per Unit (the “Conversion Price”). The Debentures are not redeemable on or before December 31, 2012, except on change of control or default. After December 31, 2012 and prior to December 31, 2013, the Debentures may be redeemed in whole or in part from time to time at Jazz's option at a price equal to their principal amount plus accrued interest, provided that the volume weighted average trading price for the Units is not less than 125% of the Conversion Price. On and after December 31, 2013 and prior to the Maturity Date, the Debentures may be redeemed in whole or in part from time to time at Jazz's option at a price equal to their principal amount plus accrued interest. Subject to regulatory approval, Jazz may satisfy its obligation to repay the principal amount of the Debentures on redemption or at maturity, in whole or in part, by delivering that number of Units equal to the amount due divided by 95% of the market price for the Units at that time, plus accrued interest in cash. The offering was made in all provinces and territories of Canada.

Upon issuance, the Debentures were separated into liability and equity components based on the respective estimated fair values at the date of issuance. The fair value of the liability component is estimated based on the present value of future interest and principal payments due under the terms of the Debentures using a discount rate for similar debt instruments without a conversion feature. The value assigned to the equity component is the estimated fair value ascribed to the holder's option to convert. Interest expense on the Debenture is determined by applying an effective interest rate to the outstanding liability component. The difference between actual cash interest accrued and interest expense is accreted to the liability component.

The following table allocates the Debentures between debt and equity:

	Cost of borrowing	Debt $	Equity $	Total $
Convertible debentures	9.5%	81,717	4,533	86,250
Transaction costs[1]		(3,776)	(209)	(3,985)
At issuance		77,941	4,324	82,265
Accretion expense		239	-	239
As at December 31, 2009		78,180	4,324	82,504

1) Transaction costs are capitalized and offset with the debt and equity portions of the debentures and amortized over the life of the debentures using the effective interest rate.

For the year ended December 31, 2009, the total interest expense was $1,267, which comprised of accrued interest of $1,028 and interest accretion of $239.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

10 Future income tax

Under the provisions of Bill C-52, Budget Implementation Act, 2007, which received Royal Assent on June 22, 2007, Jazz, as a publicly traded income trust, is considered a specified investment flow-through and will become subject to income taxes commencing January 1, 2011. Prior to 2011, Jazz continues to qualify for special income tax treatment that permits a tax deduction by Jazz for distributions paid to its Unitholders. For accounting purposes, Jazz has computed future income tax based on temporary differences at the substantively enacted tax rate expected to apply when the temporary differences are expected to reverse. For periods prior to January 1, 2011, Jazz has not recognized any current income taxes or future income tax assets or liabilities on temporary differences expected to reverse prior to 2011 as the Trust is committed to distribute to its Unitholders all or virtually all of its taxable income that would otherwise be taxable in Jazz. Based on substantively enacted tax rates in effect at December 31, 2009, Jazz is applying a tax rate of 28.4% for 2011 and 26.9% for 2012 and subsequent years.

The future income tax provision reflects the impact of the new legislation and the tax rate changes and accounts for the entire difference between the amount of the future income tax provision and the statutory income tax dollar amount of $nil.

The tax effects of temporary differences that give rise to significant portions of the future income tax assets and future income tax liabilities at December 31, 2009, that are expected to reverse after 2010, are presented below:

	As at December 31, 2009 $	2008 $
Future income tax assets		
Property and equipment – differences in net book value and undepreciated capital cost	7,862	-
Deferred lease inducements	10,282	10,701
Other	1,068	3,529
	19,212	14,230
Future income tax liabilities		
Intangibles	32,506	31,856
Property and equipment – differences in net book value and undepreciated capital cost	-	5,935
	32,506	37,791
Net future income tax liability	13,294	23,561
Income tax (recovery) expense is comprised of:		
Future income tax recovery, exclusive of the effects of other components below	(8,921)	(8,080)
Future income tax recovery resulting from impairment of goodwill	-	(42,904)
Future income tax recovery related to the change in the taxation rate	(1,346)	-
Net future income tax recovery	(10,267)	(50,984)

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

11 Other long-term liabilities

	As at December 31, 2009 $	2008 $
Accrued other future employee benefits liability (note 19)	8,062	6,991
Deferred operating lease inducements, non-current portion	44,637	49,077
	52,699	56,068

12 Distributions

On July 28, 2009, the Trustees adjusted cash distributions in light of the amendments to the CPA and to otherwise improve liquidity during an uncertain period. Effective with the distribution payment paid in September to Unitholders of record on August 31, 2009, the Board resolved to reduce cash distributions by approximately 40% to $0.60 per Unit annually.

Jazz declared a distribution for the month ended December 31, 2009 of $0.0500 per Unit (December 31, 2008 - $0.0838 per Unit). The distribution of $6,143 (2008 - $10,296) is payable January 15, 2010 to Unitholders of record on December 31, 2009.

Distributions declared, to the Unitholders of record on the last business day of each month, for the period ended December 31, 2009 aggregated to approximately $102,787 and for the same period in 2008 aggregated to approximately $123,552, as follows:

	2009		2008	
	Amount $	Amount per Unit $	Amount $	Amount per Unit $
January	10,296	0.0838	10,296	0.0838
February	10,296	0.0838	10,296	0.0838
March	10,296	0.0838	10,296	0.0838
April	10,296	0.0838	10,296	0.0838
May	10,296	0.0838	10,296	0.0838
June	10,296	0.0838	10,296	0.0838
July	10,296	0.0838	10,296	0.0838
August	6,143	0.0500	10,296	0.0838
September	6,143	0.0500	10,296	0.0838
October	6,143	0.0500	10,296	0.0838
November	6,143	0.0500	10,296	0.0838
December	6,143	0.0500	10,296	0.0838
	102,787	0.8366	123,552	1.0056

13 Units

Jazz may issue an unlimited number of Units for the consideration of, and on the terms and conditions determined by, the Trustees. Each Unit is transferable and represents an equal undivided beneficial interest in any distribution from Jazz. All Units are of the same class and have equal rights and privileges with respect to distributions.

Units are redeemable at any time on demand by the Unitholder. The redemption price per Unit is equal to the lesser of 90.0% of the market price on the date of surrender of the Unit for redemption and 100.0% of the closing market price on the redemption date. The total amount payable in respect of Units tendered for redemption in the same calendar month shall not exceed $50. During the year ended December 31, 2009, Jazz redeemed nil Units (54 Units redeemed for total cash consideration of less than $1 for the year ended December 31, 2008).

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

13 Units (continued)

Units outstanding

The issued and outstanding Units are summarized as follows:

Description	December 31, 2009 Number of Units	December 31, 2009 $	December 31, 2008 Number of Units	December 31, 2008 $
Issued for $10 each, net of issue costs of $3,826	25,000,000	246,174	25,000,000	246,174
Issued on February 9, 2007 for $8.55 each	638,223	5,457	638,223	5,457
Issued on March 14, 2007 for $8.03 each	50,000,000	401,500	50,000,000	401,500
Issued on March 30, 2007 for $8.21 each	47,226,920	387,733	47,226,920	387,733
Subtotal	122,865,143	1,040,864	122,865,143	1,040,864
Redemption of Units tendered	(1,131)	(8)	(1,131)	(8)
Issued and outstanding, before the following	122,864,012	1,040,856	122,864,012	1,040,856
Units held to fund unit based compensation plans (note 18)	(869,668)	(5,576)	(749,882)	(6,405)
Total issued and outstanding	121,994,344	1,035,280	122,114,130	1,034,451

Earnings per Unit

The following table provides a breakdown of the numerator and denominator used in the calculation of earnings per Unit and diluted earnings per Unit.

Numerator	As at December 31, 2009 $	As at December 31, 2008 $
Income (loss)	92,638	(9,410)
Interest expense on convertible debentures, net of tax	870	-
Diluted income	93,508	(9,410)

Denominator	As at December 31, 2009	As at December 31, 2008
Weighted average number of Units	121,976,518	122,074,380
Weighted average convertible debenture dilutive Units	2,250,489	-
Weighted average number of diluted Units	124,227,007	122,074,380

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

14 Statement of cash flows - supplementary information

Net changes in non-cash working capital balances related to operations:

	Year ended December 31, 2009 $	2008 $
Decrease (increase) in accounts receivable - trade and other	12,574	10,817
Decrease (increase) in spare parts, materials and supplies	5,395	(8,563)
Decrease (increase) in prepaid expenses	(7,004)	(4,345)
Decrease (increase) in other assets	(11,444)	(396)
Increase (decrease) in accounts payable and accrued liabilities	(15,446)	(7,732)
Increase (decrease) in other long-term liabilities	(2,973)	(8,719)
	(18,898)	(18,938)

15 Economic dependence

The transactions between Air Canada and its subsidiary and Jazz are summarized in the table below:

	Year ended December 31, 2009 $	2008 $
Operating revenue		
Air Canada	1,462,532	1,622,589
Operating expenses		
Air Canada(1)	101,467	111,295
Air Canada Capital Ltd.	98,988	92,583

The following balances with Air Canada and its subsidiary are included in the financial statements:

	As at December 31, 2009 $	2008 $
Accounts receivable		
Air Canada(1)	53,335	58,522
Accounts payable and accrued liabilities		
Air Canada(1)	59,048	73,529
Air Canada Capital Ltd.	8,422	9,405

(1) Includes amounts related to ACGHS Limited Partnership, now a division of Air Canada.

15 Economic dependence (continued)

Capacity Purchase Agreement

Jazz is party to the CPA with Air Canada, under which Air Canada purchases the capacity of certain specified aircraft operated by Jazz under the tradename of “Air Canada Jazz” on routes specified by Air Canada. Under this agreement, Jazz is required to provide Air Canada with the capacity of the specified aircraft, all crews and applicable personnel, aircraft maintenance, and airport operations for such flights. Air Canada determines routes and controls scheduling, sets ticket prices, determines seat inventories, and performs marketing and advertising for these flights. Air Canada retains all revenue derived from the sale of seats to passengers and cargo services and pays Jazz for the capacity provided.

Jazz is paid fees, on a monthly basis, for the capacity provided. These fees consist of a number of variable components based on different metrics, including block hours flown, flight hours, cycles (number of take-offs and landings), number of passengers and number of aircraft covered by the CPA. The rates for these metrics are fixed for annual periods and vary by aircraft type with current rates in effect until December 31, 2011. In addition, Air Canada is required to reimburse Jazz for certain pass-through costs, including fuel, de-icing, navigation, landing and terminal fees, station provisioning costs, station termination costs, passenger liability insurance and certain employee relocation costs. As these costs are required to operate the aircraft provided under the CPA, the reimbursement of these costs are included in revenue. Pass-through costs amounted to $488,374 for the year ended December 31, 2009 (2008 - $668,557).

The fees which are related to controllable costs are paid on the first day of each month based on estimates for that month. Such estimates are reconciled at the end of the month for actual amounts and true-up payments are made no later than the 30th day of the following month. Pass-through costs are reimbursed by Air Canada 30 days following the month in which they were incurred.

Pursuant to the terms of the CPA, Jazz and Air Canada agreed to re-set detailed rates (subject to the terms of the contract, including the controllable target margin requirements) applicable to the period commencing on January 1, 2009 and ending on December 31, 2011. During the first quarter of 2009, Jazz reached an agreement with Air Canada regarding the establishment of new rates for controllable costs that are payable by Air Canada under the CPA for the three-year period ending December 31, 2011. The new rates are retroactive to January 1, 2009.

Jazz is also paid certain performance incentive payments on a quarterly basis related to on-time performance, controllable flight completion, baggage handling performance and other customer satisfaction criteria. Rates under the CPA were established so as to achieve a controllable target margin of 14.32% for Jazz, effective January 1, 2009 (for the years 2006 to 2008, the target margin was 14.09%), excluding incentive and pass-through revenue, and before the deduction of incentive compensation expense paid to employees as a result of performance achievements on the CPA services provided to Air Canada.

Amendments to the CPA

On July 28, 2009, Jazz and Air Canada agreed to amend the terms of the CPA in response to uncertainty in the airline industry and Air Canada’s need to implement cost reduction initiatives. On September 22, 2009, Jazz and Air Canada executed the CPA Amending Agreement to formally reflect certain amendments to the CPA, including the following.

The CPA Amending Agreement extends the initial term of the CPA from December 31, 2015 to December 31, 2020 and provides greater certainty regarding the number of annual Block Hours to be scheduled for flying by Jazz. Block Hours are calculated by adding the number of minutes elapsing from the time the chocks are removed from the wheels of an aircraft until the chocks are next again returned to the wheels of the aircraft, divided by 60 (“Block Hours”). Under the CPA Amending Agreement, Air Canada agreed to use reasonable commercial efforts to provide a minimum of 375,000 total annual Block Hours to Jazz, as measured by the sum of the twelve monthly schedules delivered by Air Canada to Jazz for a calendar year (the “Annual Delivered Block Hours”). In addition, Air Canada and Jazz agreed that the minimum average daily utilization per aircraft, as stated in Block Hours, will not result in less than 339,000 annual Block Hours (the minimum average daily utilization guarantee or “MADUG”), notwithstanding the temporary reduction in the number of Covered Aircraft to 123 aircraft and the subsequent permanent reduction in the number of Covered Aircraft to 125, subject to Air Canada’s one-time right to revise the MADUG in the circumstances described below.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

15 Economic dependence (continued)

The CPA Amending Agreement also amended the Rates established for the rate period commencing January 1, 2009 and ending on December 31, 2011 (the "2009-2011 Rate Period"). The Rates negotiated and reflected in the Rate Amending Agreement were established to enable Jazz to achieve a Controllable Target Margin of 14.32%, corresponding to a Controllable Target Mark-Up of 16.72% on Jazz's Controllable Costs. However, pursuant to the terms of the CPA Amending Agreement, Air Canada and Jazz agreed that the Controllable Mark-Up of 16.72% shall only apply as of and from January 1, 2009 through to July 31, 2009. Effective commencing August 1, 2009, an agreed set of revised Rates became effective, under which Jazz achieves a Controllable Target Margin of 11.11%, excluding incentive and pass-through revenue, and before the deduction of incentive compensation expense paid to employees as a result of performance achievements on the CPA services provided to Air Canada, corresponding to a Controllable Mark-Up of 12.50% on Jazz's Controllable Costs.

The CPA Amending Agreement also provides for adjustments to the Controllable Mark-Up in certain circumstances. Commencing January 1, 2010, if the Annual Delivered Block Hours are less than 375,000 Block Hours, the Controllable Mark-Up will be increased, to a maximum of 16.72%, to compensate Jazz for increased unit costs and lost margin due to the reduction in flying. If, on the other hand, the Annual Delivered Block Hours are greater than 375,000 Block Hours, the Controllable Mark-Up of 12.50% shall only apply to Jazz's fixed controllable charges and the Controllable Mark-Up of 12.50% shall be reduced to 5% on Jazz's variable controllable charges for Block Hours in excess of 375,000.

The CPA Amending Agreement provides for changes to the long range fleet plan, reflecting the agreement of Air Canada and Jazz to renew the fleet of Covered Aircraft. Air Canada and Jazz agreed that the fleet of Covered Aircraft shall be reduced from 133 aircraft to a guaranteed minimum number of 125 aircraft (the "Guaranteed Minimum Number of Covered Aircraft"). The reduction in Covered Aircraft to the Guaranteed Minimum Number of Covered Aircraft shall commence with the return of eight CRJ 200 and two CRJ 100 aircraft upon the expiry of the subleases for such aircraft. Following the return of these aircraft the fleet of Covered Aircraft shall be temporarily reduced to 123 aircraft.

Pursuant to the terms of the CPA Amending Agreement, Air Canada and Jazz also agreed, effective as of August 1, 2009, to treat the rent charged to Jazz for five of the CRJ 100 aircraft as a Pass-Through Cost. Jazz and Air Canada have also agreed to use commercially reasonable efforts to agree by March 31, 2010 to terms and conditions relating to deploying up to eight CRJ 100 aircraft ("Swing Aircraft"). If an agreement is reached, Air Canada may commence the use of such Swing Aircraft to operate Scheduled Flights commencing in 2011, following the delivery of a third new turboprop aircraft to Jazz. The rent to be charged for the Swing Aircraft shall also be treated as a Pass-Through Cost. All or some of these Swing Aircraft may be removed from Jazz's fleet by Air Canada. The Swing Aircraft in Jazz's fleet from time to time, if any, are in addition to the Guaranteed Minimum Number of Covered Aircraft.

Margin adjustment

As a result of the CPA Amending Agreement, subject to the adjustments described above, the controllable target margin has been reduced from 14.32% to 11.11% effective August 1, 2009. With respect to each calendar year after 2009, during the remaining term of the CPA, if the annual margin for flights provided under the CPA is greater than 11.11%, Jazz will pay Air Canada an amount equal to 50% of the dollar value of the margin exceeding 11.11%. Margin represents the total operating revenue from scheduled flights under the CPA less expenses incurred related to such flights, including employee incentive compensation expense; however, it excludes incentive and pass-through revenue. This margin adjustment for the year ended December 31, 2009 of $nil (2008 - $nil) is accounted for as a reduction of revenue.

Master Services Agreement

Under the Master Services Agreement dated September 24, 2004, between Jazz and Air Canada, Air Canada provides certain services to Jazz for a fee. These services include Insurance and Tax Services, Corporate Real Estate Services, Environmental Affairs Services and Legal Services.

The Master Services Agreement will continue in effect until the termination or expiration of the CPA, but individual services can be terminated earlier in accordance with the terms of the Master Services Agreement.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

15 Economic dependence (continued)

Other

Air Canada provides certain supplies from third parties, primarily fuel, to Jazz and subsequently collects payment from Jazz. As these transactions and balances merely represent a method of settlement for transactions in the normal course of business, they have not been separately disclosed. Air Canada ground handling services (formerly ACGHS Limited Partnership) a division of Air Canada provides ground handling services.

Substantially all of the trade receivable from Air Canada relates to outstanding balances under the CPA.

The balances in accounts payable and accrued liabilities are payable on normal trade terms and have arisen from the services provided by the applicable party.

16 Commitments

Jazz is committed to the following future minimum lease payments under operating leases for flight equipment and base facilities that have initial or remaining non-cancellable terms in excess of one year.

		As at December 31, 2009	
		Other third parties $	Air Canada and its subsidiaries $
Year ending December 31,	2010	12,764	113,834
	2011	9,168	94,419
	2012	5,865	88,489
	2013	4,863	86,600
	2014	4,455	86,223
	Thereafter	27,823	555,062

A significant portion of the lease payments is payable in US dollars.

Certain of the aircraft lease agreements have been entered into by Air Canada Capital Ltd. or Air Canada with head lessors and subleased to Jazz. Future minimum lease payments that will arise under these leases are listed in the above table under the heading “Air Canada and its subsidiaries”.

17 Post-employment expenses

Jazz has recorded pension and other post-employment future benefit expenses for the year ended December 31, 2009 of $15,937 (2008 - $18,049).

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

18 Unit based compensation

The details of Units held under unit based compensation plans discussed in note 2 are as follows:

	December 31, 2009		December 31, 2008	
	Initial LTIP	Ongoing LTIP	Initial LTIP	Ongoing LTIP
Number of Units granted	638,223	995,892	638,223	472,542
Number of Units forfeited	(64,201)	(126,224)	(64,201)	(59,259)
	574,022	869,668	574,022	413,283
Number of Units vested	(574,022)	-	(237,423)	-
Number of Units outstanding, end of year	-	869,668	336,599	413,283
Weighted average remaining life (years)	-	1.27	nil	1.55
Cost of units purchased during the year (1)	-	$2,268	$ -	$2,178
Weighted average fair value per Unit on date of grant	-	$6.41	$8.55	$8.14
Compensation expense for the year	-	$1,917	$1,850	$1,224

(1) The cost of Units purchased under the Ongoing LTIP is not materially different from their fair value at the date they were granted.

During the year ended 2009, Jazz granted 523,350 Units (2008 - 271,104 Units) under the Ongoing LTIP. The weighted average fair value of these Units was $4.33 (2008 - $8.03).

19 Pension and other future employee benefits

Jazz maintains several registered defined contributions pension plans for eligible employees and a registered defined benefit plan for Pilots, which effective May 24, 2007, are consolidated in these financial statements. Jazz is the plan sponsor for these plans under the Pension Benefits Standard Act, 1985 (Canada). In addition, Jazz maintains an unregistered supplementary defined benefit pension plan which is partially funded for certain employees. Contributions to the supplementary pension plan started being made in December 2007. The registered and supplementary defined benefit pension plans provide benefits upon retirement, termination or death based on the member's years of service and the final average earnings for a specified period.

Jazz also maintains Other (non-pension) Employee Future Benefits. The Other Employee Future Benefits include medical and dental benefits provided to the employees on long-term disability and Workplace Safety Insurance Board ("WSIB"). These benefits cease to be provided when the employee reaches age 65. The sick leave gratuity benefits represent the payout of sick leave accruals upon or just prior to retirement for eligible employees. The self-insured WSIB benefits are in respect of self-insured benefits provided to Ontario employees.

The total expense for Jazz's defined contribution plans including two pension plans sponsored by an employee group and a union respectively, for which Jazz is obligated to make defined contributions only, for the year ended December 31, 2009 is $7,301, and for the year ended December 31, 2008 is $7,097.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

19 Pension and other future employee benefits (continued)

Total cash payments made by Jazz in 2009 for registered pension plans were $21,408, which includes cash payments for the Registered Defined Benefit Plan of $14,486 (year December 31, 2008 - $18,797; $11,962 for the Registered Defined Benefit Plan). Total cash payments made in 2009 for the Other Employee Future Benefits were $1,204.

The most recent actuarial valuations of the defined pension benefit plans for funding purposes were as of January 1, 2009 and the next funding valuation will be as of January 1, 2010.

Information about Jazz's defined benefit plans and other future employee benefits in aggregate, is as follows:

	Pension Benefits		Other Future Employee Benefits	
	2009 $	2008 $	2009 $	2008 $
Change in benefit obligation				
Benefit obligation, beginning of year	99,005	105,308	7,986	5,946
Current service cost	6,133	8,963	1,573	1,410
Interest cost	7,635	6,712	611	368
Plan participants' contributions	5,819	6,284	-	-
Benefits paid	(2,914)	(2,297)	(1,205)	(733)
Actuarial loss (gain)	10,778	(25,965)	674	995
Benefit obligation, end of year	126,456	99,005	9,639	7,986
Change in plan assets				
Fair market value of plan assets, beginning of year	92,243	90,147	-	-
Actual return on plan assets	15,293	(21,317)	-	-
Employer contribution	17,281	19,427	1,205	733
Plan participants' contributions	5,819	6,283	-	-
Benefits paid	(2,914)	(2,297)	(1,205)	(733)
Fair market value of plan assets, end of year	127,722	92,243	-	-
Funded status, end of year	1,266	(6,762)	(9,639)	(7,986)
Unamortized net actuarial loss	10,050	7,158	1,577	995
Accrued benefit asset (liability)	11,316 [1]	396 [1]	(8,062) [2]	(6,991) [2]

(1) The accrued benefit asset is included in other assets.
(2) The accrued benefit liability is included in other long-term liabilities.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

19 Pension and other future employee benefits (continued)

Plan assets consist of the following:

	Pension Benefits 2009	Pension Benefits 2008
Canadian equity	34%	35%
Debt securities	37%	33%
International equity	24%	28%
Short-term and other	5%	4%
	100%	100%

The plan's assets are invested in a balanced fund and include no significant investment in Jazz, at the measurement date.

Weighted average assumptions used to determine the accrued benefit liability:

	Pension 2009	Pension 2008	Other Future Employee Benefits 2009	Other Future Employee Benefits 2008
Discount rate to determine accrued benefit obligations	6.76%	7.10%	5.75%	7.10%
Discount rate to determine the pension and benefit cost	7.10%	5.75%	7.10%	5.60%
Rate of compensation increase	4.00 - 5.00%	4.00 - 5.00%	2.30%	1.30%
Expected return on plan assets	7.10%	6.40%	n/a	n/a
Health care inflation - Select to determine accrued benefit obligation	n/a	n/a	7.9%	6.5%
Health care inflation - Select to determine pension and benefit cost	n/a	n/a	6.5%	7.1%

The health care inflation assumption was graded down in and after 2012 to 4.5% per annum

Jazz's net defined benefit pension plan and other future employee benefits expense is as follows:

	Pension 2009 $	Pension 2008 $	Other Future Employee Benefits 2009 $	Other Future Employee Benefits 2008 $
Components of expense				
Current service cost (including provision for plan expenses)	6,133	8,963	1,573	1,410
Interest cost	7,635	6,712	611	368
Actual return on plan assets	(15,293)	21,317	-	-
Actuarial (gain) loss	10,778	(25,965)	674	995
Costs arising in the period	9,253	11,027	2,858	2,773
Differences between costs arising in the period and costs recognized in the period in respect of:				
Return on plan assets	7,789	(27,772)	-	-
Actuarial (gain) loss	(10,682)	25,996	(582)	(995)
Net periodic pension and benefit cost recognized	6,360	9,251	2,276	1,778

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

20 Capital disclosures

Jazz's capital consists of cash, cash equivalents, long-term debt, convertible debentures and Unitholders' Equity (excluding accumulated other comprehensive income).

Jazz's objective when managing capital is to maximize long-term Unitholder value by:

- maintaining a flexible capital structure that optimizes the cost of capital at acceptable risk and preserves the ability to meet financial obligations; and
- providing a return to Unitholders by delivering monthly cash distributions.

In managing its capital structure, Jazz monitors performance throughout the year to ensure anticipated cash distributions, working capital requirements and maintenance capital expenditures are funded from operations, available cash on deposit and, where applicable, bank borrowings. Jazz will make adjustments to its capital structure to meet the objectives of the broader corporate strategy or in response to changes in economic conditions and risk. In order to maintain or adjust the capital structure, Jazz may adjust the amount of cash distributions to Unitholders, issue debt and/or issue, redeem or repurchase units.

The amount of cash distributions is determined by reference to available operating cash flows, net of property and equipment acquisition costs and adjustments made with reference to the definition of distributable cash in the limited partnership agreement.

Jazz monitors capital using a number of financial metrics, including (but not limited to):

- The Leverage Ratio defined as long-term debt (1) to earnings before interest, taxes, depreciation, amortization, and other non-operating income and expense (EBITDA);
- The Coverage Ratio defined as EBITDA to interest expense (defined as interest on capital leases, security deposits and the credit facility); and
- Minimum Cash Balance.

Jazz's measure of distributable cash and EBITDA may not be comparable to similar measures presented by other entities.

The following table illustrates the financial ratios calculated on a trailing twelve-month basis:

	Measure Targets	2009	2008
Leverage Ratio	<2.0x	1.40	0.79
Coverage Ratio	>3.5x	15.40	15.72
Minimum Cash Balance (2)	$60,000	n/a	$131,876

(1) Debt includes amounts related to term facility, promissory note from the Partnership to Jazz (eliminated upon consolidation), letters of credit and capital leases.
(2) This is a continuous measurement covenant. Jazz has been in compliance since the related agreement was entered into during the fourth quarter of 2007. During the fourth quarter of 2009, Jazz renegotiated the terms of the two aircraft leases under the common terms agreement that contained the minimum cash balance covenant and as a result, the minimum cash balance covenant is no longer applicable. A cash deposit equal to six months of lease payments has been lodged for each of the two leased aircraft.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

20 Capital disclosures (continued)

As a result of the Canadian income trust taxation legislation passed in June 2007 and effective January 1, 2011, Jazz is subject to certain capital growth restrictions referred to as "normal growth" equity rules. These rules limit the amount of Unitholders' capital that can be issued by Jazz in 2010, based on Jazz's market capitalization on October 31, 2006.

On December 4, 2008, the Department of Finance (Canada) announced an acceleration of the safe harbour amounts for 2009 and 2010, such that after December 4, 2008, they became immediately available. The safe harbour rules remained cumulative such that after December 4, 2008, the maximum amount that could be issued by a SIFT under the safe harbour rules is 100% of its October 31, 2006 market capitalization, less the value of any units issued after October 31, 2006 (other than any issuances of units that would not be subject to the Normal Growth Guidelines).

As a result of the issuance of the $86,250 in convertible debentures in the fourth quarter of 2009, Jazz's normal growth capital allowed in 2010 is $145,750 (2009 - $232,000)

If the maximum equity growth allowed is exceeded, Jazz may be subject to taxation prior to 2011.

In addition to growth capital restrictions, Jazz monitors its ownership levels, to the extent possible given the practical limitations, regarding beneficial ownership information. The Trust Indenture, under which Jazz was created, provides that no more than 49.9% of the Units of Jazz can be held by non-residents of Canada. The potential impact to Jazz of breaching this threshold could be the loss of mutual fund trust status, and being subject to taxation for the entire fiscal year in which the breach occurred. On the basis of information supplied by the transfer agent, at December 31, 2009, Jazz's best estimate of the ownership level by non-residents was 17% (2008 - 13%).

21 Financial instruments

Jazz's financial instruments consist of cash and cash equivalents, accounts receivable, promissory note receivable, ABCP, accounts payable and accrued liabilities, obligations under capital leases, long-term debt and convertible debentures.

Jazz, through its financial assets and liabilities, has exposure to the following risks from its use of financial instruments: interest rate risk, credit risk, liquidity risk and currency risk. Senior management monitors risk levels and reviews risk management activities as they determine to be necessary.

Interest rate risk

Investments included in Jazz's cash and cash equivalents earn interest at prevailing and fluctuating market rates, as Jazz's objective is to maintain these balances in highly liquid investments. As at December 31, 2009, Jazz's investments consisted of bankers acceptances and bankers deposit notes issued by four schedule 1 banks and one R-1 high rated schedule 2 bank as well as a fully cashable GIC issued by a Schedule 1 bank. Jazz is exposed to interest rate fluctuation risk as a result of variable interest rates on its long-term debt. Jazz uses interest rate swaps to hedge its exposure to changes in interest rates, swapping its credit facility variable interest rate payments for fixed interest rate payments. Jazz has elected to designate its interest rate swaps as cash flow hedges and currently has no intention of settling these contracts early. Jazz entered into interest rate swap agreements with a third party in respect of $115,000 of debt which has effectively resulted in a fixed interest rate of 5.98% until February 2, 2010. If Jazz had settled these contracts at December 31, 2009, a payment of $802 by Jazz would have resulted.

A 1% change in the interest rate would not have a significant impact on the net income of Jazz.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

21 Financial instruments (continued)

Credit risk

In accordance with its investment policy, Jazz invests excess cash in Government of Canada treasury bills, short-term Canadian and provincial government debt, bankers' acceptance notes, term deposits of Schedule 1 Banks and Schedule 2 Banks rated R-1 high, and commercial paper rated R-1 high. Jazz manages the credit risk on cash and cash equivalents by ensuring that the counter-parties are governments, banks and corporations with high credit-ratings assigned by international credit-rating agencies. Given the disruption in the third party sponsored ABCP market, Jazz amended its investment policy during the third quarter of 2007 to prohibit investment in all third party and bank sponsored ABCP. With respect to investments in ABCP, refer to discussion below.

The amount of accounts receivable disclosed in the balance sheet of $59,044 is net of allowances for bad debts of $32, estimated by management based on prior experience and its assessment of the current economic environment and the specific debtor. Approximately $53,335 of receivables are with one company, Air Canada. Accordingly, Jazz is directly affected by the financial and operational strength of Air Canada. Jazz does not believe it is subject to any significant concentration of credit risk other than with Air Canada.

Liquidity risk

Jazz's objective is to maintain sufficient liquidity to meet liabilities when due, as well as to demonstrate compliance with liquidity covenants included in financing contracts. Jazz monitors its cash balances and cash flows generated from operations to meet its liquidity requirements. As at December 31, 2009, Jazz had available $31,759 in unutilized balance of the credit facilities and cash and cash equivalents of $223,559. As at December 31, 2009, Jazz had authorized credit facilities of $150,000 and drawings of $115,000, against the facilities. Letters of credit totalling approximately $3,241 (December 31, 2008 - $3,382) have been issued as security for groundhandling and airport fee contracts, lease payments on rental space and aircraft, and certain employee benefits. The letters of credit are drawn against the unutilized balance of the credit facilities.

Currency risk

Jazz receives revenue and incurs expenses in US and Canadian currency, and as such, is subject to fluctuations as a result of foreign exchange rate variations. Jazz manages its exposure to currency risk by billing for its services within the CPA in the underlying currency related to the expenditure. Accordingly, the primary exposure results from balance sheet fluctuations of US denominated cash, accounts receivable, accounts payable, and in particular, obligations under capital leases, which are long-term and so are subject to larger unrealized gains or losses. Jazz minimizes its currency risk by maintaining a balance of US dollars which is used to pay down US denominated liabilities and replenishes the balance through US denominated revenues. The amount of US dollar denominated assets was $63,118 and US denominated liabilities was $59,693 at December 31, 2009. A 1¢ change in the US exchange rate would result in a change in the unrealized gain or loss of approximately $34.

Fair value of financial instruments

The carrying amounts reported in the balance sheet for accounts receivable, and accounts payable and accrued liabilities approximate fair values based on the immediate or short-term maturities of these financial instruments. Due to current market conditions and related increases in risk premiums on credit facilities, management has estimated the fair value of the credit facilities at December 31, 2009 to be $115,000. The fair value of convertible debentures are determined by adding the market premium at December 31, 2009 to the amortized cost base. Financial assets included in the balance sheet include ABCP with an estimated fair value of $1,053 (see below for discussion on determination of fair value of ABCP).

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

21 Financial instruments (continued)

Carrying amounts and fair values

The fair values of financial assets and liabilities, together with the carrying amounts included in the consolidated balance sheets, are as follows:

	December 31, 2009		December 31, 2008	
	Carrying Amount $	Fair Value $	Carrying Amount $	Fair Value $
Financial assets				
Held for trading, carried at fair value				
Cash and cash equivalents	223,559	223,559	131,876	131,876
Asset backed commercial paper	1,053	1,053	2,009	2,009
Loans and receivables, carried at amortized cost				
Accounts receivable (1)	55,518	55,518	69,475	69,475
Promissory note	-	-	419	419
Financial liabilities				
Other financial liabilities, carried at amortized cost				
Accounts payable and accrued liabilities (includes current portion of obligations under capital leases) (1)	171,833	171,833	181,199	181,199
Distributions payable	6,143	6,143	10,296	10,296
Long-term debt	114,706	115,000	114,729	110,000
Obligations under capital leases	15,097	15,097	20,581	20,581
Convertible debentures	78,180	80,142	-	-

(1) Assets and liabilities, such as commodity taxes, that are not contractual and that arise as a result of statutory requirements imposed by governments, do not meet the definition of financial assets or financial liabilities and are therefore excluded.

Fair value hierarchy

Financial instruments recorded at fair value on the balance sheet are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 – valuation based on quoted prices observed in active markets for identical assets or liabilities.

Level 2 – valuation techniques based on inputs that are quoted prices of similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; inputs other than quoted prices used in a valuation model that are observable for that instrument; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 – valuation techniques with significant unobservable market inputs.

A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

21 Financial instruments (continued)

The following table presents the financial instruments recorded at fair value in the consolidated balance sheet as at December 31, 2009, classified using the fair value hierarchy described above:

	Level 1 $	Level 2 $	Level 3 $
Financial assets			
Cash and cash equivalents	223,559	-	-
Asset backed commercial paper	-	-	1,053
Total	223,559	-	1,053

The ABCP classified as level three is a financial security that currently has no active trading market. Valuation is done based on limited available market information, maturity dates and expected return of capital on a discounted basis. During the year ended December 31, 2009, a valuation gain of $650 (2008 - loss of $2,985) was recorded.

22 Contingencies

The Jazz Declaration of Trust provides that the Trustees will act honestly and in good faith with a view to the best interest of Jazz and in connection with that duty, will exercise the degree of care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances. The Jazz Declaration of Trust provides that each Trustee will be entitled to indemnification from Jazz in respect of the exercise of the Trust's power and the discharge of the Trustee's duties, provided that the Trustee acted honestly and in good faith with a view to the best interests of all Unitholders, or in the case of a criminal or administrative action proceeding that is enforced by a monetary penalty, where the Trustee had reasonable grounds for believing that his/her conduct was lawful. The Trustees are covered by directors' and officers' liability insurance. No claims with respect to such occurrences have been made and, as such, no amount has been recorded in these financial statements with respect to these indemnifications.

In February 2006, Jazz commenced proceedings before the Ontario Superior Court of Justice against the Toronto Port Authority ("TPA"). Porter Airlines Inc. ("Porter") and other defendants (collectively with Porter, the "Porter Defendants") after Jazz became aware that it would be excluded from operating flights from Toronto City Centre (Island) Airport (the "TCCA"). On October 26, 2007, Porter counter-claimed against Jazz and Air Canada alleging various violations of competition law, including that Jazz and Air Canada's commercial relationship contravenes Canadian competition laws, and claiming $850,000 in damages. Concurrently with the Ontario Superior Court of Justice proceedings, Jazz commenced judicial review proceedings against the TPA before the Federal Court of Canada relating to Jazz's access to the TCCA. The Porter Defendants were granted intervener and party status in these proceedings. In January of 2008, Porter filed a defence and counterclaim against Jazz and Air Canada making allegations and seeking damages similar to those in the Ontario Superior Court counterclaim. On October 16, 2009, Jazz discontinued its action in the Ontario Superior Court against the Porter Defendants and the TPA. On the same date, the counterclaim filed by Porter in the Ontario Superior against Jazz and Air Canada was stayed pending the outcome of the proceeding in Federal Court. Jazz is continuing its proceeding in the Federal Court of Canada against the TPA, in which the Porter Defendants intervened and have been made parties. Jazz maintains that Porter's counterclaims in both jurisdictions are without merit. The counterclaims are currently being vigorously contested by Jazz in court. If Jazz is not successful in the Federal Court of Canada action, it will not have fair and equal access to the TCCA. If Jazz is not successful in defending the counter-claims, it could be subject to a material damages award.

Various other lawsuits and claims that have arisen in the normal course of business are pending by and against Jazz and provisions have been recorded where appropriate. It is the opinion of management that final determination of these claims will not have a material adverse effect on the financial position or the results of Jazz.

(expressed in thousands of Canadian dollars, except Units and per Unit amount)

22 Contingencies (continued)

Jazz GP has agreed to indemnify its directors and officers against certain costs and damages incurred by the directors and officers as a result of lawsuits or any other judicial, administrative or investigative proceeding in which the directors and officers are sued as a result of their service. The directors and officers are covered by directors' and officers' liability insurance. No amount has been recorded in these financial statements with respect to the indemnification agreements.

Jazz enters into real estate leases or operating agreements, which grant a license to Jazz to use certain premises and/or operate at certain airports, in substantially all of the cities that it serves. It is common in such commercial lease transactions for Jazz as the lessee to agree to indemnify the lessor and other related third parties for tort liabilities that arise out of or relate to Jazz use or occupancy of the leased or licensed premises. In certain cases, this indemnity extends to related liabilities arising from the negligence of the indemnified parties, but generally excludes any liabilities caused by their gross negligence or willful misconduct. In addition, Jazz typically indemnifies such parties for any environmental liability that arises out of or relates to its use or occupancy of the leased or licensed premises.

In aircraft and engine financing or leasing agreements, Jazz typically indemnifies the financing parties, trustees acting on their behalf and other related parties and/or lessors against liabilities that arise from the manufacture, design, ownership, financing, use, operation and maintenance of the aircraft and engines and for tort liability, whether or not these liabilities arise out of or relate to the negligence of these indemnified parties, but generally excludes any liabilities caused by their gross negligence or willful misconduct. In addition, in aircraft and engine financing or leasing transactions, including those structured as leveraged leases, Jazz typically provides indemnities in respect of certain tax consequences.

When Jazz, as a customer, enters into technical service agreements with service providers, primarily service providers who operate an airline as their main business, Jazz has from time to time agreed to indemnify the service provider against liabilities that arise from third party claims, whether or not these liabilities arise out of or relate to the negligence of the service provider, but generally excluding liabilities that arise from the service provider's gross negligence or willful misconduct.

The maximum amount payable, if any, under the foregoing indemnities cannot be reasonably estimated. Jazz carries or is otherwise the beneficiary of various insurance policies in respect of various risks applicable to the business (including in respect of tort liability and certain contractual indemnities).

23 Subsequent event

The credit facilities matured on February 1, 2010 and all amounts owing thereunder were repaid and the related security was released. As a result, Jazz has all of its assets unencumbered (excluding $3,312 in cash encumbered in support of issued letters of credit) and available to support future debt financing. Jazz has sufficient liquidity to operate its business after such repayment, which was funded out of cash and cash equivalents with a payment of $115,000. The letters of credit remain outstanding and have been cash collateralized.