

**Tab 2**

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**Court File No. 09-CL-8456-00CL**

**ONTARIO  
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST**

**IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,  
R.S.C. 1985, c. C-36, AS AMENDED**

**AND IN THE MATTER OF JAMES ROBERT TUCKER, RICHARD HEIS AND  
ALLAN WATSON GRAHAM OF KPMG LLP, AS JOINT ADMINISTRATORS**

Applicants

**AND IN THE MATTER OF AERO INVENTORY (UK) LIMITED  
and AERO INVENTORY Plc**

Respondents

**APPLICATION UNDER SECTIONS 46 AND FOLLOWING OF THE *COMPANIES'*  
*CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, C. C-36, AS AMENDED**

**THIRD REPORT OF KPMG INC. IN ITS CAPACITY AS INFORMATION OFFICER**

**APRIL 26, 2012**

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## INTRODUCTION

1. On November 11, 2009 (the "**Administration Date**"), James Robert Tucker, Richard Heis and Allan Watson Graham of KPMG LLP (collectively, the "**Foreign Representatives**") were appointed Joint Administrators (in such capacity, the "**Joint Administrators**") of Aero Inventory (UK) Limited ("**Aero**") and Aero Inventory plc ("**Aero plc**" and, collectively with Aero, the "**Foreign Debtors**") pursuant to an order of the High Court of Justice of England and Wales (Chancery Division, Companies Court) (as later extended, the "**Administration Order**").
2. On the same date, the Ontario Superior Court of Justice (Commercial List) (the "**Court**") granted an order (the "**Recognition Order**"), *inter alia*, recognizing the UK administration proceedings of the Foreign Debtors (the "**Administration Proceedings**") as "foreign main proceedings" for the purposes of section 47 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "**CCAA**"), recognizing the Foreign Representatives as "foreign representatives" as defined in section 45 of the CCAA and recognizing and enforcing the Administration Order pursuant to section 49 of the CCAA. The Recognition Order also imposed a stay of proceedings in respect of the Foreign Debtors. A copy of the Recognition Order is attached hereto as Appendix "A".
3. Pursuant to the Recognition Order, KPMG Inc. ("**KPMG**") was appointed information officer (in such capacity, the "**Information Officer**").
4. On December 1, 2009, the Court granted an order appointing KPMG Inc. receiver and manager of all of the assets, properties and undertakings of Aero Inventory (Canada) Inc./Aero Inventaire (Canada) Inc. ("**Aero Canada**").
5. On January 22, 2010, Justice Morawetz issued an order temporarily lifting the stay granted in the Recognition Order and authorizing the Foreign Representatives to assign the Foreign Debtors into bankruptcy under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended (the "**BIA**"). The assignment documents were filed with the Office of the Superintendent of Bankruptcy on January 22, 2010 and Certificates of Appointment were issued naming KPMG as trustee in bankruptcy (in such capacity, the "**Trustee**").

6. This is the third report by the Information Officer (the "**Third Report**"). The Information Officer is filing the Third Report in respect of inventory owned by Aero that was held at facilities controlled by Aveos Fleet Performance Inc. ("**Aveos**") or Air Canada prior to its consumption by Aveos and/or Air Canada, as well as inventory that continues to be located at those facilities.

7. Since the Administration Date significant quantities of Aero-owned category 3 consumable and expendable spare aircraft parts (the "**Aero Parts**") have been consumed by Air Canada without payment. The Information Officer files this Third Report in support of a motion for an Order, inter alia:

- (a) that Air Canada shall pay, without set off, for its consumption of Aero Parts from November 11, 2009 onward, as such consumption is determined in accordance with the Algorithm and the Pricing Methodology (each as defined below) and that Air Canada shall make such payments within five (5) business days of delivery of an invoice to Air Canada by Aero.
- (b) that Air Canada shall pay amounts due to Aero as evidenced by the April 15 Invoice (as defined below) within five (5) business days of the date of the Order;
- (c) that all consumption of Aero Parts on and after November 11, 2009 shall be deemed to have occurred in accordance with the Terms of Sale (as defined below); and
- (d) that Air Canada shall cease consumption of Aero Parts immediately unless such consumption occurs in accordance with subparagraphs (a) and (c) above.

## **SCOPE**

8. In preparing this report, KPMG has relied on information supplied by the Foreign Debtors. KPMG has not audited, reviewed or otherwise attempted to verify the accuracy or completeness of such information.

## **FACTUAL BACKGROUND**

9. Aero is the main operating company of the group of companies controlled by Aero plc. This group of companies, comprised of the Foreign Debtors, Aero Canada and their international affiliates, supplied parts to the airline industry.

10. Aero's customers are airlines and aerospace maintenance and repair companies that operate in various locations globally.

11. Aero's assets in Canada are primarily composed of category 3 consumable and expendable spare aircraft parts ("**CAT 3 Parts**"). Aero has two primary Canadian customers: Air Canada and Aveos.

12. Parts owned by Aero are physically located on customer premises and customers draw on those parts as needed, subsequently paying Aero for them.

13. All of the inventory owned by Aero in Canada, save for a minimal amount of slow moving inventory located in third party owned warehouse space rented by Aero Canada, is located at various facilities across Canada that are under the control of Aveos and Air Canada. These facilities are located in Montréal, Toronto, Winnipeg and Vancouver.

14. At the time of their appointment, the Joint Administrators, with the Information Officer's assistance, began to attempt to analyze the inventory and consumption records of Aero. The Joint Administrators and the Information Officer realized that Aero had minimal independent inventory and consumption records and that it was almost entirely dependent upon Air Canada and Aveos, as well as the ARTOS computer system controlled by Aveos and Air Canada, for any information regarding Aero's ownership of parts in Canada and Aveos' and Air Canada's consumption of those parts. Further complicating this matter was

the fact that the ARTOS computer system did not differentiate between ownership by Air Canada and Aero for certain CAT 3 Parts.

15. The Agreement for the Supply and Management of Consumable and Expendable Spares between Air Canada and Aero, dated as of December 10, 2008 (the "AC LMA"), demonstrates the degree to which Aero was dependent upon Air Canada for information on inventory ownership and consumption.<sup>1</sup> A copy of this agreement is attached hereto as Appendix "B".

16. At the Administration Date, Aero was the owner of tens of millions of dollars of CAT 3 Parts in the possession of Aveos and Air Canada. On any given day, Air Canada and/or Aveos could unilaterally choose to consume those parts as needed. While such consumption in theory should result in an electronic entry being made in the Aveos/Air Canada controlled ARTOS computer system recording that consumption, there would be no means by which the Joint Administrators could ensure that payment for that consumption would be received.

#### **RELEVANT COURT PROCEEDINGS**

17. As previously noted, the Foreign Representatives obtained the Recognition Order on November 11, 2009. Paragraph 10 of the Recognition Order states:

**THIS COURT ORDERS** that the determination and enforcement of any Person's rights of set-off from and after the effective time of this Order shall be stayed pending further order of this Court and any new purchases of goods from the Foreign Debtors under existing supply contracts or otherwise from and after the effective time of this Order shall be paid by the customers on terms acceptable to the Foreign Representatives without counterclaim or deduction.

18. The Foreign Representatives regarded this provision as necessary in order to prevent Aero's Canadian customers from continuing their consumption of Aero's inventory without payment to Aero in reliance upon claims that they were owed certain pre-Administration Date

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<sup>1</sup> See, for example, sections: 2.1 ("AC Data" and "Consumption"); 4.2 (AC Technologies); 7 (Payment for Material Handling); 10(b) (Additional AC Obligations) of the AC LMA.



debts or damages by the Foreign Debtors against which such prospective consumption could be set off. Due to Aero's business model, the Foreign Representatives were unable to unilaterally prevent such consumption. Imposing "cash on delivery" terms for each transaction would have been ideal but was impossible in the circumstances since Aero's inventory had already been delivered to Aero's customers and the number of individual transactions occurring in any given day were in the range of 4,000 to 5,000, which occurred twenty four hours per day. Paragraph 10 of the Recognition Order provided the best alternative protection in the circumstances.

19. The endorsement of the Honourable Justice Newbould dated November 12, 2009, a copy of which is attached hereto as Appendix "C", discusses the intent of Paragraph 10.

20. On January 27, 2010, Air Canada gave notice that it would request that this Court vary the Recognition Order by striking out Paragraph 10 thereof. Attached hereto as Appendix "D" is the Notice of Motion served by Air Canada.

21. On March 19, 2012, Aveos (Aero's other primary Canadian customer) commenced proceedings under the CCAA in the Quebec Superior Court. Aveos has consumed significant quantities of Aero Parts post-Administration Date as well. However, that consumption is not a subject that this Third Report will cover.

#### **ALGORITHM**

22. The task of identifying Aero Parts in Canada and distinguishing them from Air Canada's and Aveos' own inventory has been challenging. Because Aero was never in physical possession of its Canadian inventory it had no means, even prior to the Administration Date, to ensure that its parts were segregated from Air Canada's and Aveos' parts.

23. The Aero Parts located in Canada are not physically segregated from inventory owned by Aveos or Air Canada.

24. The Aero Parts, Air Canada parts and Aveos parts are largely fungible and generally do not bear any marks identifying ownership.

25. As discussed below in the section titled "Invoices Previously Rendered By Aero", significant efforts were made by Aero to develop independent inventory data which recognized Air Canada's ownership of certain CAT 3 Parts. However, this process achieved limited success in the absence of integral information from Aveos and Air Canada.

26. A sophisticated set of computer programs was required to provide Aero with the information it needed to untangle its inventory from the Aveos and Air Canada stock and to determine how much of Aero's inventory had been consumed by Aveos and Air Canada. Aero required the cooperation of Aveos and Air Canada to develop these programs as Aero did not have sufficient information and resources to undertake this process independently.

27. On November 10, 2010, the Information Officer and Air Canada, along with their respective legal counsel, met at Air Canada's facilities in Montreal to discuss a process to determine ownership and consumption of Aero Parts, as well as Air Canada's inventory and Aveos' inventory. At that meeting, Air Canada first introduced the concept of a computer algorithm to determine ownership and consumption of CAT 3 Parts as between Aveos, Air Canada and Aero (the "**Algorithm**"). The Algorithm would rely upon ARTOS daily data feeds.

28. Aveos, Air Canada and Aero spent several months finalizing the Algorithm, which has been completed. The final version of the business principles applicable to the Algorithm were substantially completed by April of 2011 on a without prejudice basis. The final version of the business principles document is attached hereto as Confidential Appendix "E".

#### **AGREEMENT ON THE ALGORITHM**

29. On March 9, 2012, an agreement was reached between Air Canada and Aero (the "**March 9 Agreement**"), which is evidenced by an endorsement of Justice Morawetz of the Ontario Court, which states, in part, as follows:

Air Canada and Aero Inventory (UK) Limited (in administration) advise that they hereby agree to the following:

- (a) The [Algorithm], based upon Business Rules Document version 2.1, is the agreed upon means by which Air Canada and [Aero]

will track consumption and ownership of Category 3 Consumable and Expendable Spare Parts ("CAT 3 Parts") at any particular date on or after October 1, 2009...

(c) The balance of Aero-owned CAT 3 Parts at Air Canada's and Aveos' facilities as at September 30, 2009 is as reflected in the files delivered to Air Canada in connection with the March 1 letter delivered by KPMG Inc., in its capacity as information officer of Aero Inventory (UK) Limited (in administration), to Air Canada, among others (the "March 1 Letter").

(d) The balance of Aero-owned CAT 3 Parts as at November 11, 2009 (by facility) and as at March 1, 2012 (by facility and bin location) are as reflected in the files delivered to Air Canada in connection with the March 1 Letter and the March 7 email from Francois Gagnon to Anton Vidgen and Norma Carey, respectively.

A copy of the endorsement of Justice Morawetz is attached hereto as Appendix "F".

30. Based upon the March 9 Agreement, there can be no remaining dispute as between Air Canada and Aero regarding the quantity of Aero Parts consumed by Air Canada on or after October 1, 2009. These quantities are definitively determined by the Algorithm.

31. On April 13, 2012, Aveos and Aero executed an agreement the terms of which substantially mirror the terms of the March 9 Agreement (the "**Aveos Agreement**"). A copy of the Aveos Agreement is attached hereto as Appendix "G".

32. The Aveos Agreement eliminates any concern that Aveos will assert at some point in the future that it owned any CAT 3 Parts determined by the Algorithm to have been owned by Aero or that Aveos will assert that Air Canada's consumption of Aero Parts is not as determined by the Algorithm.

### **CONSUMPTION TO DATE**

33. Beginning on the Administration Date, the Joint Administrators and their counsel immediately took steps to notify customers, such as Air Canada, of the terms of the Recognition Order and outlined the terms upon which customers would be permitted to continue consuming Aero Parts. A letter from the Joint Administrators' counsel enclosing the Recognition Order is attached hereto as Appendix "H". A letter dated November 11, 2009

from the Joint Administrators to Air Canada regarding continued consumption is attached hereto as Appendix "I".

34. Air Canada wrote as follows to the Joint Administrators on November 11, 2009:

We acknowledge receipt of your letter of today and your decision to re-negotiate the terms of our procurement contract with Aero Inventory. We agree that we should meet to discuss any future procurement arrangement between Air Canada and Aero Inventory. In the interim, we will comply with the administration and other court orders applicable to us.

A copy of this letter is attached as Appendix "J" hereto.

35. Following the commencement of the Administration Proceedings, the Joint Administrators filed financing change statements in applicable personal property security registration systems in Quebec, Ontario, Manitoba and British Columbia regarding particular inventory that was subject to an October 2009 bulk sale of inventory from Aero to Air Canada. This was done out of an abundance of caution.

36. On November 23, 2009, Air Canada wrote to the Joint Administrators stating, among other things, that as a result of these PPSA filings "the Debtor Companies are in default of [a] fundamental term of the Parts Purchase Agreement" and that Air Canada would exercise its right to withhold payment on account of Aero Parts that it purchased. The Joint Administrators and Aero have not acknowledged that any such right to withhold payment exists. A copy of this correspondence from Air Canada is attached as Appendix "K" hereto.

37. On January 27, 2010, counsel to the Information Officer received court materials from Air Canada in which Air Canada proposed to seek an order varying the provisions of the Recognition Order to strike out Paragraph 10. That motion has not been scheduled by Air Canada over the past two years. Delay in scheduling that motion was not problematic for Aero so long as Air Canada did not consume Aero's inventory. Now that the Algorithm has been agreed to and there is clear evidence of the precise amounts of Aero's inventory that Air Canada has consumed, as detailed below, this matter must be dealt with.

### **INVOICES PREVIOUSLY RENDERED BY AERO**

38. As of the Administration Date, Aero had only issued invoices to Air Canada for consumption up to September 30, 2009. Once the Joint Administrators had updated Aero's records to the point that they could deliver invoices that they believed recognized Air Canada's ownership of certain CAT 3 Parts and were accurate based upon their limited information, Aero generated invoices for the period of October 1, 2009 onward. Specifically, on July 13, 2010 Aero, through the Information Officer, delivered invoices to Air Canada for:

- (a) Consumption from October 1, 2009 to November 10, 2009;
- (b) Consumption from November 11, 2009 to January 31, 2010; and
- (c) Transactions associated with a Consumable and Expendable Spare Parts Purchase and Sale Agreement dated October 23, 2009 (being the bulk sales referenced in Paragraph 35).

These invoices were never acknowledged by Air Canada and payment was never received. A copy of the letter enclosing the above invoices is attached hereto as Appendix "L".

39. On August 9, 2010 and August 17, 2010, Aero, through the Information Officer, provided Air Canada with invoices for consumption from February 1, 2010 to May 31, 2010 (inclusive). Copies of the correspondence containing these invoices is attached hereto as Appendix "M". Once again, these invoices were never acknowledged by Air Canada and payment was never received.

40. The above invoices were rendered based upon the best information available to Aero at the time. In absence of cooperation from Aveos and Air Canada in this regard, which did not become available until the Algorithm discussions commenced in November of 2010, Aero had only limited inventory data to rely upon.

41. Based upon the calculations in the Algorithm, it is now clear that the invoices provided to Air Canada and referenced above contained certain errors.<sup>2</sup> Air Canada has not made any payments pursuant to these invoices and Aero recognized that these invoices needed to be corrected and re-issued and has done so based upon the information contained in the Algorithm.

### **PRICING OF CONSUMED INVENTORY**

42. The Joint Administrators believe that pricing for post-Administration Date consumption should be the same as pre-Administration Date consumption under the AC LMA. However, in light of the complexity of the pricing mechanisms in the AC LMA, a proxy for AC LMA pricing will be needed. Reference to the AC LMA shows that no fewer than six pages of provisions are dedicated to pricing determinations, which require ongoing proactive steps to be taken by Air Canada and Aero that are not practical in the current circumstances.<sup>3</sup>

43. The Joint Administrators believe that utilizing the ARTOS calculated "average inventory price" (which is readily determinable and verifiable)<sup>4</sup> and applying an 11.17% premium would be the best proxy to use (the "**Pricing Methodology**"). The Pricing Methodology was determined through a historical review of prices charged by Aero to Air Canada under the AC LMA for consumption of particular parts as compared to the ARTOS calculated "average inventory price" for those parts at the date of consumption. This comparison for the period from May 1, 2009 to September 30, 2009<sup>5</sup> showed that pricing under the AC LMA was on average 11.17% higher than the ARTOS calculated "average

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<sup>2</sup> The source of the errors contained in the invoices resulted from an improper interpretation of certain transaction codes in the ARTOS system.

<sup>3</sup> See sections 21 through 23 of the AC LMA.

<sup>4</sup> The Joint Administrators understand that ARTOS "average inventory price" represents the cost of a particular part to Aero plus the freight charges associated with that part.

<sup>5</sup> Invoices were only rendered directly by Aero to Air Canada for consumption pre-Administration Date during the period from May 1, 2009 to September 30, 2009. Prior to May 1, 2009, invoices for Air Canada consumption were delivered by Aero to Aveos for processing by Aveos.

inventory price". To the Joint Administrators' knowledge, Air Canada did not dispute the pricing contained in the invoices delivered by Aero for consumption from May 1, 2009 to September 30, 2009. A copy of the calculations used in the Pricing Methodology is attached hereto as Appendix "N".

44. The Joint Administrators recognize that the pricing proposed above differs from the pricing offered to Aveos under a Settlement and Labour Supply Agreement entered into in December of 2010 with Aveos. However, that agreement was entered into in the context of a settlement of a variety of matters, involved the payment by Aveos and its affiliate, Aeromantenimiento, S.A., for certain pre-Administration Date consumption, a 75% partial payment of estimated consumption on or after July 1, 2010 pending resolution of inventory ownership, and also involved a detailed parts uplift plan in which Aveos would have an integral role. The commercial circumstances of the Aveos agreement were entirely different from the current circumstances with Air Canada.

45. Air Canada was invited to enter into a dialogue on pricing issues on April 4, 2012, as shown in correspondence attached hereto as Appendix "O".

46. A meeting was held to discuss, among other things, pricing issues with Air Canada on April 16, 2012. No resolution on pricing matters was reached.

47. Air Canada has indicated that a discounted price for consumption should be charged as Air Canada has not had the benefit of certain services under the AC LMA, which it says accounted for a portion of the pricing under the AC LMA. Aero has not been informed of a quantification of the discount that Air Canada is seeking.

#### **TERMS OF SALE**

48. The Information Officer understands from the Joint Administrators that companies in administration proceedings in the United Kingdom typically sell assets on an "as is, where is" basis, similar to the manner in which such sales would occur in Canada if undertaken by a receiver or trustee in bankruptcy. The Joint Administrators believe that such "as is, where is" terms, as more particularly set out in Appendix "P" hereto (the "**Terms of Sale**"), are a reasonable basis upon which to sell all of the Aero Parts that have been consumed on or after

the Administration Date by Aero's customers in Canada . This is consistent with the original terms of sale proposed by the Joint Administrators to Air Canada in its November 11, 2009 letter found at Appendix "I". The Joint Administrators further believe that these sale terms are appropriate in a circumstance where Aero has not been in possession of the property that it is selling.

#### **AIR CANADA CONSUMPTION**

49. Based upon the Algorithm, the Joint Administrators believe that between November 11, 2009 and February 29, 2012 Air Canada consumed US\$6.352 million<sup>6</sup> of Aero Parts (before taxes) valued at ARTOS "average inventory price" ("AIP"). Correspondence summarizing this information was sent to Air Canada on April 4, 2012. A copy of this correspondence is attached hereto as Appendix "P". If the Pricing Methodology were applied, the value of that consumption would be approximately US\$7.062 million (before taxes).

50. During the month of March additional Air Canada consumption occurred, which is valued by Aero at US\$134,286 (before taxes) at AIP, or US\$149,286 (before taxes) using the Pricing Methodology.

51. During the period from April 1 to April 15 of 2012, additional Air Canada consumption amounted to US\$53,259 (before taxes) at AIP, or US\$59,207 (before taxes) using the Pricing Methodology.

52. Correspondence summarizing the consumption in March and April of 2012 was sent to Air Canada on April 10, 2012 and April 26, 2012. Copies of that correspondence are attached hereto as Appendix "Q".

53. The foregoing consumption figures are based upon the Algorithm, which has been agreed upon by Air Canada. Enclosed herewith is a confidential disc containing the Algorithm outputs evidencing the above described consumption from November 11, 2009 to April 15, 2012, including data on AIP. Also attached hereto as Appendix "R" is an invoice

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<sup>6</sup> Converted from Canadian Dollars using the average monthly exchange rate for the relevant period according to the Bank of Canada.



for Air Canada's consumption of Aero Parts during the period from November 11, 2009 to April 15, 2012 (the "**April 15 Invoice**"). The April 15 Invoice has been provided to Air Canada.

### **SET OFF**

54. Air Canada has previously provided notice that it would be seeking to vary the Recognition Order by eliminating Paragraph 10 thereof, presumably for the purposes of asserting set off in respect of amounts that it would owe for consumption of Aero Parts following the Administration Date.

55. The matter has not been scheduled for hearing by Air Canada. In the meantime, Air Canada has consumed over \$7 million worth of Aero Parts.

56. If the Recognition Order is varied as requested by Air Canada and if Air Canada is also permitted to set-off against its post-Administration Date consumption, the precise outcome that the Joint Administrators sought to guard against when they requested that Paragraph 10 be included in the Recognition Order would occur.

57. If Air Canada had successfully brought its motion to vary the Recognition Order on a timely basis, and if Aero had previously been able to obtain the evidence of Air Canada's consumption that is now provided by the Algorithm, the Joint Administrators would have had the opportunity to seek relief from this Honourable Court. However, this matter did not proceed in that fashion and the Joint Administrators no longer have the opportunity to seek that relief which they otherwise would have sought. Aero's inventory has now been significantly depleted by Air Canada's continued consumption.

### **FUTURE CONSUMPTION BY AIR CANADA**

58. There is currently no agreement between Air Canada and Aero for the future consumption of Aero Parts by Air Canada.

59. On numerous occasions Aero has requested that Air Canada cease consuming Aero Parts. See, for example, the following correspondence:

- (a) On November 11, 2009, the Joint Administrators wrote to Air Canada proposing terms upon which consumption could continue, failing which consumption must cease. A copy of this letter is attached as Appendix "I" hereto;
- (b) On April 9, 2010, the Information Officer sent correspondence on behalf of the Joint Administrators to Air Canada in which the Information Officer sought to confirm Air Canada's previous representations that effective November 11, 2009 Air Canada ceased to draw on Aero Parts. A copy of this letter is attached as Appendix "S" hereto;
- (c) On July 9, 2010, the Information Officer, on behalf of the Joint Administrators, sent correspondence to Air Canada requesting that it immediately stop consuming Aero Parts and requesting Air Canada to provide written confirmation thereof. A copy of the letter sent by the Information Officer is attached hereto as Appendix "T";
- (d) On July 26, 2010, counsel to the Joint Administrators wrote to counsel for Air Canada. A copy of that correspondence is attached hereto as Appendix "U"; and
- (e) On August 5, 2010, Canadian counsel to the Joint Administrators requested information from Air Canada on the particulars of whether it continued to use Aero Parts. A copy of the letter from August 5, 2010 is attached hereto as Appendix "V".

60. Whereas the Information Officer has been told by Air Canada in the past that Air Canada has ceased consumption of Aero Parts, this appears to be incorrect. See for example:

- (a) The letter from Air Canada dated November 11, 2009, a copy of which is attached hereto as Appendix "J";
- (b) An email from Air Canada's counsel on November 27, 2009, a copy of which is attached hereto as Appendix "W";

- (c) The endorsement of the Honourable Justice Newbould dated December 1, 2009, a copy of which is attached hereto as Appendix "X"; and
- (d) The letter from the Information Officer to Air Canada dated April 10, 2012, a copy of which is attached hereto as Appendix "Q".

61. In the circumstances, the Joint Administrators believe that the only method to ensure that consumption of Aero Parts by Air Canada ceases is the granting of an order specifically prohibiting Air Canada from further consuming Aero Parts, or requiring payment for that consumption immediately in cash without set off.

62. There may have been an initial need for Air Canada to consume Aero Parts because of long lead times to order certain parts. However, this should have been resolved by Air Canada over the past two years. Therefore, the prejudice that may result from preventing further consumption of Aero Parts should be minimal.

#### **PROPOSED RESOLUTION**

63. Payment for existing consumption and prevention of ongoing consumption are the two matters on which this Honourable Court's assistance is sought at the current time.

64. Aero is prepared, in reliance upon the information contained in the Algorithm, to invoice Air Canada for Air Canada's consumption of Aero Parts from November 11, 2009 onwards. Pricing would be determined by the Pricing Methodology. The Terms of Sale would be applied. Air Canada would pay invoices rendered by Aero within five (5) business days of receipt.

65. Air Canada would be precluded from consuming Aero Parts in the future, unless that consumption occurs in accordance with paragraph 64 above.

#### **SEALING OF CONFIDENTIAL MATERIAL**

The Information Officer will file a certain confidential disc and confidential appendices (the "**Confidential Material**") with the Court in connection with the Foreign Representatives' motion. The Confidential Material will contain, among other things, certain highly sensitive

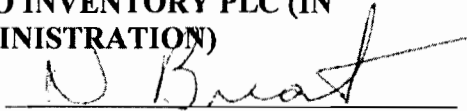
records of the inventory and consumption of each of Aero, Air Canada and Aveos at various points in time. The disclosure of this sensitive commercial information to the public generally could be damaging to the businesses of Air Canada, Aveos and Aero.

In addition to the relief enumerated above, the Foreign Representatives and the Information Officer believe that it is appropriate in the circumstances to request that the Confidential Material be the subject of a sealing order.

All of which is respectfully submitted this 26th day of April, 2012.

**KPMG INC.  
INFORMATION OFFICER OF  
AERO INVENTORY (UK) LIMITED  
(IN ADMINISTRATION) AND  
AERO INVENTORY PLC (IN  
ADMINISTRATION)**

Per:



Nicholas Brearton  
President

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT,  
R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF JAMES ROBERT TUCKER, RICHARD HEIS AND  
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Court File No. 09-CL-8456-00CL

**ONTARIO**  
**SUPERIOR COURT OF JUSTICE**  
**COMMERCIAL LIST**

Proceeding commenced at Toronto

**THIRD REPORT OF KPMG INC.**  
**IN ITS CAPACITY AS**  
**INFORMATION OFFICER**

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