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**THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION.** When considering the action you should take, you are recommended to seek independent financial advice from your stockbroker, solicitor, accountant or other professional adviser immediately.

If you have sold all your ordinary shares in British Airways Plc, please send this document together with the enclosed form of proxy to the bank, stockbroker or other agent through whom the sale was effected, for transmission to the purchaser.

A copy of this document, which comprises Listing Particulars relating to British Airways Plc and British Airways Capital Limited in accordance with the Listing Rules made under Section 142 of the Financial Services Act 1986, has been delivered to the Registrar of Companies in England and Wales in accordance with Section 149 of that Act. ✓

Application has been made to the Council of The Stock Exchange for the Convertible Capital Bonds ("the Bonds") and the Preference Shares of British Airways Capital Limited to be admitted to the Official List. It is expected that listing will become effective and that dealings in the Bonds will commence on 2nd October, 1989.

The provisional allotment letters and the Bonds have not been and will not be registered under the United States Securities Act of 1933, as amended, or under the securities laws of any province or territory of Canada and they may not, as part of their distribution, be offered, sold, renounced or delivered, directly or indirectly, in the United States or Canada or to North American persons (each as defined herein).

The consent of the Finance and Economics Committee of the States of Jersey under the Control of Borrowing (Jersey) Order 1958, as amended, has been obtained to the issue of the Bonds and of the Preference Shares of British Airways Capital Limited referred to in this document. It must be distinctly understood that in giving this consent the Committee does not take any responsibility for the financial soundness of any schemes or for the correctness of any statements made or opinions expressed with regard to them.



**BRITISH AIRWAYS** Plc ✓

**Proposed participation  
in the acquisition of UAL Corporation  
and  
rights issue of**

**£320,215,349 9¾ per cent. Convertible Capital Bonds  
of British Airways Capital Limited**



A letter from your Chairman is set out on pages 4 to 11.

Notice of an extraordinary general meeting of British Airways Plc to be held at 9.00 am on Friday, 13th October, 1989 is set out at the end of this document.

A form of proxy for use at the extraordinary general meeting is enclosed and should be returned so as to be received by 9.00 am on Wednesday, 11th October, 1989.

You should retain this document for reference pending receipt of a provisional allotment letter which is expected to be posted to you on Friday, 29th September, 1989.

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## **PROPOSED TIMETABLE FOR RIGHTS ISSUE**

Record date for the rights issue	Wednesday, 20th September, 1989
Despatch of provisional allotment letters	Friday, 29th September, 1989
Dealings in the Convertible Capital Bonds commence, nil paid	Monday, 2nd October, 1989
Latest time for splitting Convertible Capital Bonds, nil paid	3.00 pm, Wednesday, 18th October, 1989
Latest time for acceptance and payment and latest date for registration	3.00 pm, Friday, 20th October, 1989
Despatch of Convertible Capital Bond certificates	1st December, 1989

## DEFINITIONS

The following definitions apply throughout this document unless the context requires otherwise:—

"Airline Acquisition Corp."	a US corporation which will effect the Acquisition of UAL, in which it is proposed that British Airways should subscribe \$750 million for preferred stock, \$250 million of which will be convertible to give British Airways 15 per cent. of the voting common stock of Airline Acquisition Corp. on a fully diluted basis
"UAL"	UAL Corporation
"UAL Group"	UAL and its subsidiaries
"UAL Inc."	United Air Lines Inc.
"UAL Common Stock"	Common Stock, par value \$5 per share, of UAL
"Acquisition of UAL"	the acquisition by Airline Acquisition Corp. of UAL pursuant to Airline Acquisition Corp.'s tender offer to purchase all outstanding shares of UAL Common Stock and the subsequent merger of Airline Acquisition Corp. with and into UAL, or the acquisition by Airline Acquisition Corp. of a substantial proportion of the assets of the UAL Group by way of purchase or otherwise or any merger, consolidation, reorganisation or other business combination pursuant to which the business of UAL, or a substantial proportion thereof, is acquired by Airline Acquisition Corp.
"Extraordinary General Meeting"	the Extraordinary General Meeting of British Airways convened for Friday, 13th October, 1989, and any adjournment thereof
"Resolution"	the Ordinary Resolution contained in the Notice of Extraordinary General Meeting set out at the end of this document
"British Airways", "the Company" or "the Guarantor"	British Airways Plc
"British Airways Group"	the Company and its subsidiaries
"British Airways shares"	ordinary shares of 25p each in British Airways
"new British Airways shares"	British Airways shares for which the Preference Shares are exchangeable
"Bonds" or "Convertible Capital Bonds"	9¾ per cent. Convertible Capital Bonds 2005 of the Issuer, guaranteed on a subordinated basis by the Company, and convertible into Preference Shares of the Issuer, which are to be allotted and issued pursuant to the rights issue at an issue price of 100p per Bond
"the Issuer"	British Airways Capital Limited, a subsidiary of the Company incorporated in Jersey
"Preference Shares"	exchangeable redeemable preference shares of 1p each of the Issuer, guaranteed on a subordinated basis by the Company, to be allotted at a price of 100p each upon the conversion of Bonds and exchangeable for new British Airways shares
"Lazard Brothers"	Lazard Brothers & Co., Limited
"Morgan Stanley"	Morgan Stanley & Co. Incorporated
"United States" or "US"	the United States of America (including the States and the District of Columbia), its territories, its possessions and other areas subject to its jurisdiction
"North American Person"	a citizen or resident of the United States or Canada, a corporation, partnership or other entity created or organised in or under the laws of the United States, an individual person, corporation, partnership or other entity in Canada and an estate or trust the income of which is subject to United States Federal income taxation regardless of its source; provided, however, that the term "North American Person" does not include a branch or agency of a US bank or insurance company that is operating outside the United States for valid business reasons as a locally regulated branch or agency engaged in the banking or insurance business and not solely for the purpose of investing in securities not registered under the United States Securities Act of 1933
"The Stock Exchange"	The International Stock Exchange of the United Kingdom and the Republic of Ireland Limited
"\$"	US dollars.

Directors:  
 Lord King of Wartnaby (*Chairman*)  
 Sir Colin Marshall (*Deputy Chairman and Chief Executive*)  
 D. M. Stevens (*Chief Financial Officer*)  
 M. R. Angus (*Deputy Chairman*)  
 A. M. Davies  
 J. W. Jessop  
 Sir Francis Kennedy  
 H. U. A. Lambert  
 Hon. Charles Price II

**BRITISH AIRWAYS** Plc

Registered Office:  
 Speedbird House,  
 Heathrow Airport (London),  
 Hounslow TW6 2JA,

Registered in England  
 No. 1777777

27th September, 1989

To: the holders of British Airways shares

Dear Shareholder,

## Proposed participation in the Acquisition of UAL and rights issue

### Introduction

On 1st September, 1989 British Airways announced that it had agreed in principle, but subject to shareholders' approval, to invest \$750 million in Airline Acquisition Corp., a US company which proposed to acquire all the UAL Common Stock at a price of \$300 per share. At this price, the UAL Common Stock (including the cancellation of UAL stock options) is valued at \$6.8 billion. In addition to British Airways the participants in Airline Acquisition Corp. will comprise senior management of UAL, including Stephen Wolf, Chairman and Chief Executive Officer, and Jack Pope, Executive Vice President, the Air Line Pilots Association (representing UAL Inc.'s pilots) and certain staff of UAL who will participate through one or more Employee Stock Ownership Plans ("ESOPs"). Organisations representing other groups of UAL employees may also participate.

On 15th September, 1989 it was announced that UAL had entered into a definitive merger agreement with Airline Acquisition Corp., and on 21st September, 1989 Airline Acquisition Corp. commenced a tender offer for all the UAL Common Stock at \$300 per share. The purchase of UAL common stock pursuant to the tender offer is scheduled to occur on 26th October, 1989. Thereafter, Airline Acquisition Corp. intends to merge with and into UAL, with UAL as the surviving corporation. The Board of UAL had earlier received an offer of \$275 per share of UAL Common Stock from Mr. Marvin Davis. On 15th September, 1989 Mr. Davis wrote to the Board of UAL offering to acquire UAL at a price of \$300 per share of UAL Common Stock in the event that Airline Acquisition Corp.'s transaction is not completed.

I am writing to you to explain the reasons for British Airways' proposed participation in the Acquisition of UAL, and the benefits it will bring to British Airways and its shareholders, and to provide you with background information concerning the transaction. In view of the size of the transaction, British Airways' participation in the Acquisition of UAL is conditional on approval by shareholders in general meeting.

On 26th September, 1989 British Airways announced a rights issue to raise approximately £310 million, net of expenses. The rights issue will take the form of Convertible Capital Bonds to be issued by British Airways Capital Limited, a subsidiary of British Airways. The Convertible Capital Bonds will effectively be exchangeable for new British Airways shares on the basis of one new British Airways share for approximately every 5.5 British Airways shares held. Details of the Convertible Capital Bonds are set out below and in Appendix 4. The underwriting of the rights issue has been arranged by Lazard Brothers. Brokers to the issue are Rowe & Pitman Ltd. and UBS Phillips & Drew Securities Limited. It is not conditional on the successful completion of the Acquisition of UAL. This letter also describes the reasons for, and the details of, the rights issue.

## **The Acquisition of UAL**

### **Description of UAL**

UAL, Inc. is the principal subsidiary of UAL, accounting for over 99 per cent. of UAL's operating revenues. UAL has been engaged in air transportation since 1926 and is now one of the world's largest airlines. It is the principal carrier at five major US airports - Chicago, Denver, San Francisco, Seattle and Washington DC - and serves not only most major markets within the US but also Pacific Basin countries and Mexico and Canada. UAL serves over 150 cities in North America and the Pacific Region. In 1988 it carried some 56 million passengers and averaged some 1,760 scheduled departures and some 1,480,000 scheduled miles per day.

UAL's fleet is one of the largest in the world consisting of approximately 420 aircraft. The fleet is being modernised and orders have been placed for 14 Boeing 747-400s, 170 Boeing 737-300s, 90 Boeing 757-200s and 16 Boeing 767-300s.

The use of computer reservation systems has become a key factor in the marketing and distribution of airlines' services. UAL developed the Apollo computer reservation system, which is one of the largest computer reservation systems in the United States. It is used by more than a quarter of the travel agent locations in the United States and has over 53,000 terminals at more than 10,000 locations in over 40 countries. The Apollo system is owned by the Covia Partnership, in which UAL now has a 50 per cent. interest and British Airways an 11 per cent. interest.

In the year ended 31st December, 1988, UAL Group made profits before tax, but after extraordinary profits, of \$989 million on revenues of \$8,982 million. Profits before tax included a \$393 million extraordinary profit on the sale of partnership interests in Covia. At 31st December, 1988, UAL had net assets of \$1,228 million. For the six months ended 30th June, 1989 UAL made profit before tax of \$343 million on revenues of \$4,844 million.

### **Background to and reasons for British Airways' participation in Airline Acquisition Corp.**

In December 1987 British Airways entered into a marketing agreement with UAL to exploit the excellent fit between the companies' route networks. The agreement with UAL encompassed the sharing of facilities at Chicago, Washington DC, Seattle, San Diego and New York airports, the development of mutual interlining and the development of joint selling and marketing activities. The commercial logic of the arrangement centred on the need for British Airways to develop a partnership with a major airline operating in the US, the world's largest air transport market.

UAL's network both in the US and throughout the Pacific region, the fastest growing area for airline traffic, is complementary to British Airways' strong European and transatlantic network. On its own British Airways has access to 17 per cent. of world scheduled international markets; together, British Airways and UAL have access to 38 per cent. of these markets and to 48 per cent. of the total scheduled world market. The investment of British Airways of 26 per cent., and UAL of 28 per cent., in the Galileo computer reservation system marketed in Europe further supports the rationale of seeking to achieve a commercial partnership with a global reach.

The uncertainty surrounding UAL's future following the proposals made by Mr. Marvin Davis clearly presents an opportunity for British Airways to obtain an equity stake which, if it were not taken now, might not be available again. UAL is an attractive investment for British Airways and a first class carrier. UAL will benefit in the future from the additional involvement of its employees.

If the Acquisition of UAL is successfully completed British Airways will hold 15 per cent. of the voting equity of Airline Acquisition Corp. on a fully diluted basis and will have a seat on its board, which it is intended will be taken by Sir Colin Marshall. It is also intended that Stephen Wolf will be invited to join the Board of British Airways as a non-executive Director.

Your Board believes that British Airways' participation in a successful offer for UAL is an important strategic step in developing a partnership from which each airline will benefit increasingly as the air transport industry becomes more and more deregulated and global.

### **Proposed terms of British Airways' participation in Airline Acquisition Corp.**

British Airways has agreed, subject to certain conditions including the approval of its shareholders, to invest \$750 million in Airline Acquisition Corp. in the following mixture of securities:

\$250 million in convertible preferred stock ("Convertible Preferred"), which is convertible at any time into voting common equity (and which prior to conversion has equivalent voting rights to the voting common equity) such that British Airways will hold 15 per cent. of the voting equity of Airline Acquisition Corp.. The Convertible Preferred will have no preference as to dividends but shall participate *pari passu* as to any dividend or other distribution with respect to Airline Acquisition Corp.'s common stock.

\$200 million in preferred stock carrying dividends of 13 per cent. per annum ("the 13 per cent. Securities"). Dividends will be payable in cash, but for the first five years British Airways has agreed to reinvest an equivalent amount in further 13 per cent. Securities at par.

\$300 million in preferred stock carrying dividends of 18 per cent. per annum ("the 18 per cent. Securities"). Dividends will be payable in cash, but, prior to the earlier of the fifth anniversary of issuance or the date of any US distribution of 18 per cent. Securities, British Airways has agreed to reinvest an equivalent amount in further 18 per cent. Securities at par.

It has been agreed by the other participants in Airline Acquisition Corp. that British Airways will enjoy pre-emption and other rights so as to be able to maintain its interest in the fully diluted voting common equity of UAL following the merger at 15 per cent.. British Airways has acknowledged that UAL may from time to time in the future acquire shares in British Airways in the market up to a comparable proportion (subject to such acquisition not compromising British Airways' operating rights) and British Airways would welcome UAL as a shareholder. If either party wishes to acquire more than 15 per cent. of the voting equity of the other it will require the other's consent.

Further details of the financing of British Airways' participation in Airline Acquisition Corp. and of Airline Acquisition Corp.'s tender offer are contained in Appendix 2.

### **Extraordinary General Meeting**

A notice convening the Extraordinary General Meeting for 9.00 am on Friday, 13th October, 1989 is set out at the end of this document. The purpose of the Extraordinary General Meeting is to pass an ordinary resolution to approve British Airways' proposed participation in the Acquisition of UAL and arrangements relating thereto. Only holders of British Airways shares are entitled to attend and vote at the Extraordinary General Meeting.

### **Action to be taken in relation to the Extraordinary General Meeting**

Holders of British Airways shares will find enclosed a form of proxy for use at the Extraordinary General Meeting. You are requested to complete and return the form of proxy in accordance with the instructions thereon so as to be received by the Company's Registrars, Lloyds Bank Plc, Registrar's Department, Goring-by-Sea, Worthing, West Sussex BN12 6DA as soon as possible and in any event so as to be received not later than 9.00 am on Wednesday, 11th October, 1989. Completion and return of a form of proxy will not preclude you from attending and voting in person at the Extraordinary General Meeting should you so wish.

### **The Rights Issue**

#### **Background to and reasons for the rights issue**

Although the proposed investment in Airline Acquisition Corp. could be financed through a combination of the Group's internal resources and available banking facilities, your Board believes that it is in the interests of British Airways' shareholders for British Airways to increase its shareholders' equity base by a substantial amount for the first time in the two and a half years since flotation. This will give the British Airways Group greater flexibility in future financing and maintain the Company's gearing ratio at an appropriate level.

In addition to its proposed investment of \$750 million in Airline Acquisition Corp., British Airways is also in the process of negotiating an agreement under which it would acquire a 20 per cent. shareholding in Sabena World Airlines at a cost of approximately £30 million. If the Acquisition of UAL is not successfully completed the money raised will be used to fund this and other developments, whether already in progress or to be commenced in the future.

### Details of the rights issue

British Airways is raising approximately £310 million, net of expenses, through an issue of Convertible Capital Bonds. The Convertible Capital Bonds will entitle a holder, on conversion and exchange, to receive new British Airways shares on the basis of one new British Airways share for every 2.43 Convertible Capital Bonds held.

The Convertible Capital Bonds are being issued by way of rights to the holders of existing British Airways shares on the register at the close of business on 20th September, 1989 on the following basis:

For every 9 British Airways shares then held	4 Convertible Capital Bonds of 100p each
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and so in proportion for any greater or lesser number of British Airways shares held. The Convertible Capital Bonds will effectively be exchangeable for new British Airways shares on the basis of one new British Airways share for approximately every 5.5 British Airways shares held.

The Convertible Capital Bonds will be issued at a price of 100p per Bond. The Bonds, the provisional allotment letters and the new British Airways shares are not being registered under the United States Securities Act of 1933, as amended, or under the securities laws of any province or territory of Canada, and accordingly will not be offered in the United States or Canada or to North American Persons.

The price of 100p per Convertible Capital Bond will be payable in full on acceptance not later than 3.00 p.m. on Friday, 20th October, 1989. Fractions of Convertible Capital Bonds will not be allotted to shareholders but will be aggregated and sold in the market for the benefit of the British Airways Group. It is expected that definitive certificates for the Bonds accepted by the original allottees or their renounees will be posted on 1st December, 1989 at the risk of the persons entitled thereto. Pending the despatch of definitive certificates and following the latest time for registration of renunciations, transfers may be certified against the register.

The Bonds will be convertible at the option of the holder into Preference Shares of the Issuer on 15th June in each of the years 1993 to 2005. Not less than 28 days nor more than 56 days before the conversion date in each of these years, British Airways will give written notice to holders of Bonds informing them of their entitlement to convert and exchange their Bonds. One Preference Share will be allotted on the conversion of each Bond. Preference Shares allotted on the conversion of Bonds by the holder will be immediately exchanged without further action on the part of the holder for new British Airways shares on the basis (subject to adjustment as described in Appendix 4) of approximately 0.4 new British Airways shares for every Preference Share so exchanged (equivalent to 243p worth of Bonds for each new British Airways share). Fractions of new British Airways shares will not be issued on exchange and no cash adjustment will be made.

Until conversion, the Bonds will bear gross interest at the rate of  $9\frac{3}{4}$  per cent. per annum, payable net of basic rate tax semi-annually in arrear on 31st March and 30th September in each year, except that the first payment of interest to be made on 31st March, 1990 will be in respect of the period from and including 20th October, 1989 and will amount to approximately 4.3p per Bond and the final payment of interest to be made on 15th June, 2005 will be in respect of the period from and including 1st April, 2005 and will amount to approximately 2.0p per Bond. New British Airways shares issued on the conversion date in each year will rank for the final dividend payable on the British Airways shares in respect of the year ending on the preceding 31st March.

The maturity date of the Bonds (subject to extension as described in Appendix 4) will be 15th June, 2005. If by that time a holder of Bonds has not converted and exchanged his Bonds for new British Airways shares, conversion and exchange will be effected on the holder's behalf. The new British Airways shares resulting from such a conversion and exchange will then be sold on behalf of the relevant holder and the net cash proceeds remitted, if the net proceeds of the sale of the resulting new British Airways shares (disregarding tax liabilities) would exceed the issue price of the relevant Bonds and accrued interest up to the maturity date. If at the maturity date a holder has not converted and exchanged his Bonds, and if the proceeds of sale of the new British Airways shares (disregarding tax liabilities) would not exceed the issue price of the relevant Bonds and accrued interest, British Airways may nevertheless convert and exchange the Bonds for new British Airways shares, making good the difference between the proceeds of sale of the resulting new British Airways shares and the issue price of the relevant Bonds, plus any accrued interest. If at the maturity date Bonds are not so converted and exchanged, they will be converted into Preference Shares and redeemed by the Issuer. Again, the cash proceeds will be remitted to the person entitled thereto.

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**Despatch of provisional allotment letters**

The rights issue is subject to the Council of The Stock Exchange granting permission for the Bonds to be admitted to the Official List and to listing becoming effective. Provisional allotment letters (in nil paid form) in respect of the Convertible Capital Bonds are expected to be posted on Friday, 29th September, 1989. Dealings in the Bonds are expected to commence, nil paid, on Monday, 2nd October, 1989. Dealing instructions will be set out in the Convertible Capital Bond certificates.

Any enquiries in connection with the provisional allotment letters or transfers of Convertible Capital Bonds should be addressed to Barclays Bank PLC, New Issues, PO Box 123, Fleetway House, 25 Farringdon Street, London EC4A 4HD (telephone number 01-489-1995).

**Procedure for acceptance and payment**

Your provisional allotment letter will set out the holding of British Airways shares on which your entitlement is based and the number of Convertible Capital Bonds which have been provisionally allotted to you and for which you will be entitled to subscribe.

If you wish to take up, in whole or in part, the Bonds which you have been provisionally allotted, you should lodge your provisional allotment letter in accordance with the instructions contained therein with Barclays Bank PLC, New Issues, PO Box 123, Fleetway House, 25 Farringdon Street, London EC4A 4HD. Your provisional allotment letter should be accompanied by a remittance for the full amount of the subscription monies for the Bonds you are taking up and should arrive not later than 3.00 pm on Friday, 20th October, 1989.

**Renunciation and splitting**

The provisional allotment letters will be fully renounceable, save as required by the laws of certain foreign jurisdictions. They may be split up to 3.00 pm on Wednesday, 18th October, 1989 (nil paid) and the latest time for payment in full and registration of renunciation will be 3.00 pm on Friday, 20th October, 1989. After that date transfers of Convertible Capital Bonds will be certified against duly receipted provisional allotment letters until the Convertible Capital Bond certificates are issued on 1st December, 1989. Full instructions will be set out in the provisional allotment letters.

**Procedures in respect of rights not taken up**

If payment in full for the Convertible Capital Bonds is not received by 3.00 pm on Friday, 20th October, 1989 the relevant provisional allotment will be deemed to have been declined and will lapse. However, arrangements have been made with Lazard Brothers for any Convertible Capital Bonds not taken up to be sold in the market by no later than 3.00 pm on Monday, 23rd October, 1989, if a premium over the subscription price and the expenses of sale can be obtained. Any such net proceeds (after the deduction of the subscription price and expenses of sale) will be distributed pro rata among the shareholders to whom such Convertible Capital Bonds were provisionally allotted, by cheque at their risk, except that entitlements of less than £2.50 will not be distributed but will be aggregated and retained for the benefit of the British Airways Group. Shareholders who hold small numbers of shares and who do not wish to take up their rights are likely to incur lower dealing costs by letting their rights lapse rather than by selling them.

**Restrictions on North American persons and other overseas shareholders**

The provisional allotment letters, the Convertible Capital Bonds and the new British Airways shares have not been and will not be registered under the United States Securities Act of 1933, as amended, or under the securities legislation of any province or territory of Canada. Accordingly, provisional allotment letters are not being sent to shareholders whom British Airways knows to be North American persons, wherever they may reside, or to shareholders with registered addresses in the United States or Canada, and failure of a person wishing to take up rights or of an applicant for registration of renunciation to certify that he is not a North American person and is not buying on behalf of a North American person, will result in the forced sale of those Convertible Capital Bonds on behalf of that transferee. The attention of shareholders who are North American persons is drawn to paragraph 13 of Appendix 5 for a description of their rights in connection with the rights issue. Arrangements will be made for the rights of holders of British Airways' American Depository Receipts (amounting to approximately 20 per cent. of the rights issue) and of the other North American shareholders to be sold nil paid in the market on the first day of dealings and for the net cash proceeds to be distributed to them, if a premium over the expenses of sale can be obtained. Amounts of less than £2.50 will not be distributed but will be aggregated and retained for the benefit of the British Airways Group.

The attention of other shareholders who are not resident in, or who have registered addresses outside, the United Kingdom is drawn to paragraph 13 of Appendix 5 for a description of their rights in connection with the rights issue. In cases where overseas shareholders are not provisionally allotted Convertible Capital Bonds or are not able to take up the Convertible Capital Bonds provisionally allotted to them, the arrangements described above will apply.

#### **Restrictions on ownership of British Airways shares**

Rights of British Airways to operate, in particular on international routes, could be withdrawn if British Airways ceased to be substantially owned and effectively controlled by UK nationals. Accordingly, the articles of association of British Airways contain powers which may be used to limit the number or voting rights of shares in which non-UK nationals own interests or, if necessary, to require their compulsory disposal, or to restrict the transferability of shares. As at 19th September, 1989, approximately 32 per cent. of the British Airways shares were Foreign Interest Shares (as described in paragraph 3 of Appendix 5 as "Relevant Shares"). At the time of privatisation your Board stated that they would not generally expect to intervene unless the proportion of Foreign Interest Shares approached 35 per cent. At present, but without limiting their freedom to act to protect the Company's operating rights in the future, the Directors do not believe an intervention to be necessary.

The articles of association also restrict, until 31st January, 1992, the maximum proportion of British Airways' issued share capital in which any person (including connected persons) may be interested to 15 per cent. The relevant provisions of the articles of association are described in more detail in paragraph 3 of Appendix 5.

#### **United Kingdom taxation**

##### **(a) Capital gains tax**

The rights issue will not be treated as falling within the re-organisation provisions of the Capital Gains Tax Act 1979. Accordingly, a shareholder who takes up his rights will be treated as acquiring a new asset for capital gains tax purposes with a base cost equal to the monies applied by him on the subscription of his Convertible Capital Bonds.

The Convertible Capital Bonds will not constitute qualifying corporate bonds for the purposes of the Finance Act 1984 and consequent chargeable gains arising on any disposal will not be exempt from capital gains tax on that basis. If a shareholder sells all or part of the Convertible Capital Bonds allotted to him or his rights thereto, or if he allows his rights to lapse and receives a cash payment in respect thereof, he may, depending upon his circumstances, incur a liability to capital gains tax.

Under present law, the conversion of the Convertible Capital Bonds into Preference Shares, and the exchange of those Preference Shares for new British Airways shares should not give rise to a disposal of the Convertible Capital Bonds for capital gains tax purposes.

##### **(b) Income tax on interest payments**

Payments of interest on the Convertible Capital Bonds will be made under deduction of United Kingdom income tax at the basic rate (currently 25 per cent.) by the Issuer unless the Issuer has previously been directed by the Inland Revenue, in relation to a particular holding of the Convertible Capital Bonds, to make payment free of deduction or subject to a reduced deduction by virtue of relief available to the holder of such Convertible Capital Bonds under the provisions of an applicable double taxation treaty. Such directions will be issued only on prior application to the Commissioners of the Inland Revenue by the shareholder in question.

Notwithstanding that interest is received subject to basic rate income tax deduction, holders of the Convertible Capital Bonds who are resident in the United Kingdom for tax purposes or, whilst non-resident, are carrying on a trade in the United Kingdom through a branch or agency, may, depending on their circumstances, either be liable to pay further United Kingdom tax on the interest received or be entitled to a refund of all or part of the tax deducted at source.

The Issuer will not "gross up" payments of interest to compensate for any withholding tax that it is, or hereafter may be, required to make.

Where Convertible Capital Bondholders are assessable to United Kingdom tax on the interest payable on the Convertible Capital Bonds, the basis of assessment may be affected by the provisions of Chapter II of Part XVII of the Income and Corporation Taxes Act 1988 ("the accrued income scheme") on any transfer of Convertible Capital Bonds or on the death of the holder thereof. Where the accrued income scheme applies, interest accrued for the purposes of those provisions to the date of such an event is chargeable on the transferor and any interest accruing for those purposes after that date is chargeable on the transferee.

**(c) Stamp duty and stamp duty reserve tax**

(i) No stamp duty or stamp duty reserve tax ("SDRT") will be payable on the issue of provisional allotment letters.

(ii) The purchase of rights to Convertible Capital Bonds represented by provisional allotment letters on or before the latest time for registration of renunciation will not be liable to stamp duty, but there will be a liability to SDRT generally at the rate of 50p for every £100 or part of £100 of the consideration paid. Where such a purchase is effected through a stockbroker or other financial intermediary that person will normally account for the liability to SDRT and will indicate that this has been done in any contract note issued to a purchaser. In other cases, the purchaser of the rights to the Convertible Capital Bonds represented by the provisional allotment letter is liable to pay the SDRT and must account to the Inland Revenue.

(iii) The transfer on sale of Convertible Capital Bonds after the last date for registration of renunciation will be liable to *ad valorem* stamp duty or (if an unconditional agreement to transfer such Convertible Capital Bonds is not completed by a duly stamped transfer within two months) SDRT generally in each case at the rate of 50p for every £100 or part of £100 of the consideration paid.

The above is only a guide to the general position. If you are in any doubt as to your tax position, or if you are subject to tax in a jurisdiction other than the United Kingdom, you should consult your professional adviser.

**Current financial and trading prospects of the British Airways Group**

At the announcement of its results for the first quarter, British Airways indicated that a softening of the world economy could affect its ability to sustain growth rates of the recent past. Nevertheless trading has continued to be satisfactory and British Airways has agreed compensation to be paid by Boeing for the late delivery of 747-400 aircraft sufficient to offset the adverse effects of the late deliveries. In addition British Airways announced on 22nd September, 1989 the further reductions in annual pension contributions set out below. Prospects for the future remain encouraging.

R. Watsons & Sons, Actuaries to the two British Airways Pension Schemes have recently completed routine three yearly valuations of the assets and liabilities of the Schemes. The Actuaries have reported the financial position to the Schemes' Trustees and to British Airways. The Actuaries have advised the Trustees that surpluses have arisen such that British Airways' annual contributions to both Schemes can be substantially reduced. In the financial year to March 1990 it is anticipated that the pre-tax profit benefit to British Airways will be some £30 million. Thereafter it is anticipated that there will be a continuing, long term benefit, initially of the order of £50 million each year.

**Financial effects of British Airways' participation in the proposed Acquisition of UAL**

Taking into account the rights issue proceeds and assuming that the balance of funds required for British Airways' participation in the Acquisition of UAL is funded by long term debt, the overall effect on the earnings of British Airways is expected to be broadly neutral in the short term.

In addition to the commercial benefits which will result from the partnership with UAL, the Board of British Airways considers the financial terms of the investment to be acceptable.

**Additional information**

Your attention is drawn to the additional information set out in Appendices 1 to 5.

**Recommendations**

British Airways' participation in the proposed Acquisition of UAL represents a significant strategic move and an important opportunity for the future development of the British Airways Group. Your Directors, who have been advised by Lazard Brothers, and by Morgan Stanley in the United States in connection with the proposed investment in Airline Acquisition Corp., consider that British Airways' participation in the proposed Acquisition of UAL is in the best interests of British Airways and its shareholders. Your Directors therefore unanimously recommend shareholders to vote in favour of the Resolution to be proposed at the extraordinary general meeting as they intend to do in respect of the 86,382 British Airways shares owned or controlled by them.

Your Directors, who have been advised by Lazard Brothers in connection with the rights issue, consider that the rights issue is in the best interests of British Airways and its shareholders.

Yours faithfully

King of Wartnaby

## APPENDIX 1

### FINANCIAL INFORMATION ON UAL GROUP

The following financial information relating to UAL Group has been extracted from the audited Consolidated Financial Statements contained in the relevant UAL annual reports on Form 10-K ("the annual reports") and the unaudited Condensed Consolidated Financial Statements contained in UAL's quarterly report on Form 10-Q for the quarter ended 30th June, 1989 filed with the United States Securities and Exchange Commission ("SEC"). The Consolidated Financial Statements contained in such annual reports comprise Statements of Consolidated Operations, Consolidated Cash Flows and Consolidated Non-Redeemable Preferred Stock, Common Stock and Other Shareholders' Equity for the most recent three financial years and Statements of Consolidated Financial Position as at the most recent two financial year ends, and the notes thereto as required by the applicable accounting regulations of the SEC.

In 1987 and 1988, UAL sold its non-airline operations. In accordance with US generally accepted accounting principles, UAL reported the results of these operations as discontinued operations in the year of disposal and restated the results of its operations for prior years on a similar basis. The information set out below has therefore been extracted from the most recent annual reports which include financial years prior to the years of disposal of these operations. However, on this basis, no annual report is available in which the results for 1984 have been restated.

The annual reports of UAL state that the Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles and under the accounting policies set out below. US generally accepted accounting principles and UAL's accounting policies differ in certain respects from United Kingdom standard accounting practice and from British Airways' accounting policies, particularly as regards deferred taxation, property and fleet valuations, pension costs and extraordinary items. Without access to the accounting records of UAL however, it is not possible to restate the following financial information in accordance with either UK standard accounting practice or British Airways' accounting policies.

Statements of Consolidated Operations for each of the five years ended 31st December, 1988 and for the six months ended 30th June, 1988 and 1989, Statements of Consolidated Financial Position as at each of 31st December, 1987 and 1988, Statements of Consolidated Cash Flows for each of the three years ended 31st December, 1988 and Statements of Consolidated Non-Redeemable Preferred Stock, Common Stock and Other Shareholders' Equity for each of the three years ended 31st December, 1988, together with the related notes as at each of 31st December, 1987 and 1988 and for each of the three years ended 31st December, 1988, are set out below.

#### 1. Statements of Consolidated Operations

	Year ended 31st December,					Six months ended 30th June,	
	1984 \$000	1985 \$000	1986 \$000	1987 \$000	1988 \$000	1988 \$000	1989 \$000
<b>Airline operating revenues:</b>							
Passenger	5,412,972	4,430,238	5,958,144	6,855,750	7,723,139	3,707,516	4,242,645
Cargo	363,021	270,766	413,532	488,828	509,639	252,789	254,732
Contract services and other	442,727	590,605	747,533	960,394	748,965	387,724	346,938
	<u>6,218,720</u>	<u>5,291,609</u>	<u>7,119,209</u>	<u>8,304,972</u>	<u>8,981,743</u>	<u>4,348,029</u>	<u>4,844,315</u>
<b>Non-airline operating revenues (Note 1):</b>	748,879	—	—	—	—	—	—
<b>Operating revenues:</b>	<u>6,967,599</u>	<u>5,291,609</u>	<u>7,119,209</u>	<u>8,304,972</u>	<u>8,981,743</u>	<u>4,348,029</u>	<u>4,844,315</u>
<b>Operating expenses (Note 1):</b>							
Salaries and related costs		2,030,216	2,557,673	2,777,618	2,837,599	1,390,812	1,548,357
Aircraft fuel	1,368,099	1,143,568	1,099,441	1,243,579	1,179,571	616,996	650,432
Traffic commissions		418,524	714,667	907,049	1,101,755	528,397	647,064
Depreciation and amortisation	445,623	424,093	502,313	550,515	518,387	258,918	260,264
Purchased services		304,678	436,663	480,443	648,189	284,851	296,597
Rentals and landing fees		171,778	283,174	336,751	408,228	188,085	258,808
Maintenance materials and supplies		161,513	224,698	251,452	267,922	135,010	158,671
Food and beverages		105,475	156,661	183,001	193,367	97,499	97,889
Advertising and promotion		151,171	207,207	174,914	206,493	93,246	95,134
Personnel expenses		99,828	147,268	159,123	158,351	78,389	87,070
Other (Note 2)	4,510,551	523,421	699,050	993,239	796,953	428,271	379,697
	<u>6,324,273</u>	<u>5,534,265</u>	<u>7,028,815</u>	<u>8,057,684</u>	<u>8,316,815</u>	<u>4,160,474</u>	<u>4,479,983</u>
<b>Earnings (loss) from operations (Note 1)</b>	<u>643,326</u>	<u>(242,656)</u>	<u>90,394</u>	<u>247,288</u>	<u>664,928</u>	<u>247,555</u>	<u>364,332</u>

	Year ended 31st December,					Six months ended 30th June,	
	1984 \$000	1985 \$000	1986 \$000	1987 \$000	1988 \$000	1988 \$000	1989 \$000
<b>Earnings (loss) from operations (Note 1)</b>	643,326	(242,656)	90,394	247,288	664,928	247,555	364,332
<b>Other deductions (income) (Note 1):</b>							
Interest expense	154,072	159,340	223,273	257,536	245,306	117,020	121,540
Interest capitalised	(11,452)	(1,967)	(11,925)	(16,399)	(30,983)	(14,709)	(24,564)
Interest income	(39,262)	(37,128)	(19,833)	(51,733)	(100,873)	(56,656)	(52,847)
Equity in earnings of Covia Partnership	—	—	—	—	(87,460)	(61,515)	(26,140)
Gain on sale of Covia Partnership interests	—	—	—	—	(393,006)	—	—
Gain on reversion of pension plan assets	—	(136,835)	—	—	—	—	—
Other, net including foreign exchange losses	58,393	(16,793)	126,574	70,469	43,156	20,936	3,320
	161,751	(33,383)	318,089	259,873	(323,860)	5,076	21,309
<b>Earnings (loss) from operations before income taxes (Note 1)</b>	481,575	(209,273)	(227,695)	(12,585)	988,788	242,479	343,023
<b>Provision (credit) for income taxes (Note 1)</b>	220,700	(113,939)	(114,860)	(8,391)	388,874	90,390	136,523
<b>Earnings (loss) from operations (Note 1)</b>	260,875	(95,334)	(112,835)	(4,194)	599,914	152,089	206,500
<b>Discontinued operations:</b>							
Earnings from discontinued operations, less income taxes	—	29,115	124,435	68,817	457	457	—
Gain on sales of discontinued operations, less income taxes	—	17,536	—	270,494	523,929	548,478	—
Extraordinary items (Note 3)	21,513	—	—	—	—	—	—
<b>Net earnings (loss)</b>	282,388	(48,683)	11,600	335,117	1,124,300	701,024	206,500
<b>Net earnings (loss) per share, primary (Note 1):</b>							
Continuing operations	\$ 7.46	\$ (3.43)	\$ (2.50)	\$ (0.08)	\$ 20.20	\$ 4.14	\$ 9.55
Discontinued operations	—	1.34	2.75	6.10	17.67	14.98	—
	7.46	(2.09)	0.25	6.02	37.87	19.12	9.55
<b>Net earnings (loss) per share, fully diluted (Note 1):</b>							
Continuing operations	6.93	(3.43)	(2.50)	0.25	20.20	4.08	9.37
Discontinued operations	—	1.34	2.75	5.51	17.67	14.71	—
	6.93	(2.09)	0.25	5.76	37.87	18.79	9.37
<b>Dividends per share:</b>							
Prior preferred	5.50	5.50	5.50	5.50	5.50	—	—
Series A preferred	0.10	—	—	—	—	—	—
Series B preferred	2.40	2.40	2.40	—	—	—	—
Common	0.50	1.00	1.00	0.75	—	—	—

## Notes:—

- As noted above, a Statement of Consolidated Operations for 1984, restated to reflect UAL's non-airline operations sold in 1987 and 1988 as discontinued operations, is not available. However, the table of Selected Financial Data included in UAL's annual report for the year ended 31st December, 1988 shows the following amounts for the year ended 31st December, 1984 for continuing operations:—

Operating revenues	\$000
Earnings	6,218,720
	237,983
	\$
Earnings per share:	
Primary	6.18
Fully diluted	5.84

In addition, in this table operating revenues for 1985 are shown as \$5,306,035,000.

- The Consolidated Financial Statements for the year ended 31st December, 1984 do not provide the detailed analysis of "Operating expenses" shown in the subsequent four years. "Other" operating expenses in 1984 comprise the amounts categorised in the Statement of Consolidated Operations as "Sales and advertising", "General and administrative" and "Operations, exclusive of expenses listed separately".
- The extraordinary item related to a gain on deferrals of debt and obligation under capital lease less a provision for deferred income taxes of \$20,300,000.

## 2. Statements of Consolidated Financial Position

	As at 31st December,	
	1987 \$000	1988 \$000
<b>Assets</b>		
<b>Current assets:</b>		
Cash and cash equivalents	2,208,019	1,086,824
Receivables, less allowance for doubtful accounts (1987 - \$19,140; 1988 - \$13,549)	836,473	742,991
Aircraft fuel, spare parts and supplies, less obsolescence allowance (1987 - \$73,810; 1988 - \$53,389)	221,744	175,225
Prepaid expenses and other	217,123	166,220
	<u>3,483,359</u>	<u>2,171,260</u>
<b>Net assets of discontinued operations</b>	426,747	—
<b>Operating property and equipment:</b>		
<b>Owned</b>		
Flight equipment	5,485,230	5,550,217
Advances on flight equipment purchase contracts	168,541	324,108
Other property and equipment	1,670,755	1,386,749
	<u>7,324,526</u>	<u>7,261,074</u>
Accumulated depreciation and amortisation	(3,623,576)	(3,618,177)
	<u>3,700,950</u>	<u>3,642,897</u>
<b>Capital leases</b>		
Flight equipment	541,944	420,452
Other property and equipment	101,190	101,015
	<u>643,134</u>	<u>521,467</u>
Accumulated amortisation	(316,981)	(223,113)
	<u>326,153</u>	<u>298,354</u>
	<u>4,027,103</u>	<u>3,941,251</u>
<b>Other assets:</b>		
Intangibles, less accumulated amortisation (1987 - \$207,217; 1988 - \$289,712)	287,096	200,948
Deferred income taxes	—	27,246
Other	164,342	360,030
	<u>451,438</u>	<u>588,224</u>
<b>Total Assets</b>	<u>8,388,647</u>	<u>6,700,735</u>
<b>Liabilities and Shareholders' Equity</b>		
<b>Current liabilities:</b>		
Short term borrowings	1,010,311	446,164
Long term debt maturing within one year	27,233	67,278
Current obligations under capital leases	19,965	18,113
Advance ticket sales	581,333	599,669
Accounts payable	486,071	519,297
Accrued salaries, wages and benefits	536,292	579,271
Accrued income taxes	238,967	149,327
Other accrued liabilities	483,289	489,979
	<u>3,383,461</u>	<u>2,869,098</u>
<b>Long term debt</b>	1,280,851	1,648,939
<b>Long term obligations under capital leases</b>	430,742	411,282
<b>Other liabilities and deferred credits:</b>		
Deferred pension liability	297,560	297,101
Deferred income taxes	21,134	—
Other liabilities and deferred credits	49,791	245,696
	<u>368,485</u>	<u>542,797</u>
<b>Redeemable preferred stock:</b>		
5½% cumulative prior preferred stock, \$100 par value	3,021	2,544
<b>Common stock and other shareholders' equity:</b>		
Common stock, \$5 par value; authorised, 125,000,000 shares; issued, 58,470,707 shares in 1987 and 23,333,154 shares in 1988	292,354	116,666
Additional capital invested	1,678,306	29,265
Retained earnings	1,073,760	1,202,477
Common stock held in treasury - 1,730,400 shares	(122,333)	(122,333)
	<u>2,922,087</u>	<u>1,226,075</u>
<b>Total Liabilities and Shareholders' Equity</b>	<u>8,388,647</u>	<u>6,700,735</u>

## 3. Statements of Consolidated Cash Flows

	Year ended 31st December,		
	1986 \$000	1987 \$000	1988 \$000
Cash and cash equivalents at beginning of year	593,345	102,420	2,208,019
<b>Cash flows from operating activities:</b>			
Earnings (loss) from continuing operations	(112,835)	(4,194)	599,914
Adjustments to reconcile to net cash provided by operating activities:			
Deferred pension expense	75,091	42,602	(459)
Depreciation and amortisation	502,313	550,515	518,387
Foreign exchange losses	128,595	43,167	—
Provision (credit) for deferred income taxes	(45,434)	(26,905)	(32,613)
Gain on sale of Covia Partnership interests	—	—	(393,006)
Decrease (increase) in receivables	(71,819)	(40,741)	36,152
Decrease (increase) in other current assets	(55,399)	3,148	35,119
Increase in advance ticket sales	130,937	20,011	18,336
Increase (decrease) in accrued income taxes	23,885	210,140	(89,640)
Increase in accounts payable and other accrued liabilities	198,389	321,101	99,078
Other, net	38,595	63,517	(19,437)
	812,318	1,182,361	771,831
<b>Cash flows from investing activities:</b>			
Additions to property and equipment	(1,059,975)	(986,961)	(1,372,489)
Proceeds on disposition of property and equipment	2,859	148,797	1,011,948
Proceeds on disposition of Covia Partnership interests	—	—	493,000
Increase in intangibles	(430,177)	(13,430)	—
Other, net	(6,018)	13,739	(420)
	(1,493,311)	(837,855)	132,039
<b>Cash flows from financing activities:</b>			
Issuance of long term debt	186,116	336,799	1,843,462
Reduction of long term debt	(876,287)	(127,856)	(1,423,763)
Issuance of common stock	526,538	304,025	—
Purchase of common stock	—	(122,333)	(2,841,500)
Dividends paid	(45,515)	(41,892)	(171)
Increase (decrease) in short term borrowings	314,605	262,613	(550,797)
Other, net	(29,629)	(7,449)	(391)
	75,828	603,907	(2,973,160)
<b>Cash flows from discontinued operations:</b>			
Addition of Hilton International	—	(835,746)	—
Proceeds on disposition of subsidiaries	—	1,953,179	948,095
Other, net	114,240	39,753	—
	114,240	1,157,186	948,095
<b>Increase (decrease) in cash and equivalents</b>	<b>(490,925)</b>	<b>2,105,599</b>	<b>(1,121,195)</b>
<b>Cash and cash equivalents at end of year</b>	<b>102,420</b>	<b>2,208,019</b>	<b>1,086,824</b>
<b>Cash paid during the year for:</b>			
Interest of continuing operations (net of amounts capitalised)	238,555	235,332	217,234
Income taxes on earnings (loss) from continuing operations	5,713	68,921	436,588
Income taxes on gain on sales of discontinued operations	—	—	404,209

#### 4. Statements of Consolidated Non-Redeemable Preferred Stock, Common Stock and Other Shareholders' Equity

	Preferred Stock \$000	Common Stock \$000	Additional Capital Invested \$000	Retained Earnings \$000	Treasury Stock \$000	Total \$000
Balance as at 31st December, 1985	230,601	176,566	578,258	814,450	—	1,799,875
Year ended 31st December, 1986:						
Net earnings	—	—	—	11,600	—	11,600
Cash dividends declared:						
Prior preferred	—	—	—	(206)	—	(206)
Series B preferred	—	—	—	(6)	—	(6)
Common	—	—	—	(45,303)	—	(45,303)
Issuance of common	—	47,000	479,538	—	—	526,538
Exercises of stock options	—	393	2,906	—	—	3,299
Redemption of Series B preferred	(1,543)	—	(1,965)	—	—	(3,508)
Conversion of Series B preferred	(229,058)	27,159	201,858	—	—	(41)
Balance as at 31st December, 1986	—	251,118	1,260,595	780,535	—	2,292,248
Year ended 31st December, 1987:						
Net earnings	—	—	—	335,117	—	335,117
Cash dividends declared:						
Prior preferred	—	—	—	(195)	—	(195)
Common	—	—	—	(41,697)	—	(41,697)
Issuance of common	—	40,043	405,718	—	—	445,761
Exercises of stock options	—	1,193	11,995	—	—	13,188
Redemption of prior preferred	—	—	(2)	—	—	(2)
Purchase of treasury stock	—	—	—	—	(122,333)	(122,333)
Balance as at 31st December, 1987	—	292,354	1,678,306	1,073,760	(122,333)	2,922,087
Year ended 31st December, 1988:						
Net earnings	—	—	—	1,124,300	—	1,124,300
Cash dividends declared:						
Prior preferred	—	—	—	(171)	—	(171)
Purchase and retirement of common	—	(177,500)	(1,691,839)	(972,161)	—	(2,841,500)
Exercises of stock options	—	1,812	19,550	—	—	21,362
Redemption of prior preferred	—	—	(3)	—	—	(3)
Capitalisation of retained earnings	—	—	23,251	(23,251)	—	—
Balance as at 31st December, 1988	—	116,666	29,265	1,202,477	(122,333)	1,226,075

#### 5. Notes to Consolidated Financial Statements

##### (a) Summary of Significant Accounting Policies

**Consolidation.** The consolidated financial statements include the accounts of UAL and all of its majority-owned subsidiaries. All significant intercompany transactions are eliminated. Investments in affiliates are carried on the equity basis.

In 1988, UAL adopted the provisions of Statement of Financial Accounting Standards No. 94, "Consolidation of All Majority-Owned Subsidiaries." Accordingly, the accounts of UAL Leasing, Inc. ("UAL Leasing"), a wholly-owned finance subsidiary which had previously been carried on the equity basis, are now included in UAL's consolidated financial statements. Prior year consolidated financial statements have been restated to reflect this change.

**Airline Revenues.** Passenger fares and cargo revenues are recorded as operating revenues when the transportation is furnished. The value of unused passenger tickets is included in current liabilities.

**Foreign Currency Transactions.** Losses or gains on Japanese yen-denominated debt (substantially unrealised), forward exchange contracts and foreign currency call options are charged or credited directly to income.

**Cash and Cash Equivalents.** Cash in excess of operating requirements is invested in highly liquid, income producing investments generally having maturities of three months or less. These investments are stated at cost, which approximates market value.

**Aircraft Fuel, Spare Parts and Supplies.** Aircraft fuel and maintenance and operating supplies are stated at average cost. Flight equipment spare parts are stated at average cost less obsolescence allowance.

**Operating Property and Equipment.** Owned operating property and equipment is stated at cost. Leased property under capital leases, and the related obligation for future minimum lease payments, are initially recorded at an amount equal to the then present value of those lease payments.

Depreciation and amortisation of owned depreciable assets is based on the straight-line method over their estimated service lives. Leasehold improvements are amortised over the remaining period of the lease or the estimated service life of the related asset, whichever is less. Aircraft are depreciated to estimated salvage values, generally over lives of 10 to 20 years; buildings are depreciated over lives of 25 to 45 years; and other property and equipment are depreciated over lives of 3 to 15 years.

Properties under capital leases are amortised on the straight-line method over the life of the lease. Lease terms are 12 to 19 years for aircraft and flight simulators and 15 to 40 years for buildings. Lease amortisation is included in depreciation and amortisation expense.

Gains or losses on disposition of individual units of owned property and equipment are reflected in earnings. Maintenance and repairs, including the cost of minor replacements, are charged to maintenance expense accounts. Costs of additions to and renewals of units of property are charged to property and equipment accounts.

**Intangibles.** Intangibles resulting from the 1986 purchase of assets from Pan American World Airways Inc. are, for the most part, being amortised over five years.

**Income Taxes.** Deferred income taxes are provided to recognise the effects of timing differences, i.e., those items of income and expense which affect income for tax purposes in a period different from that in which they affect income for accounting and reporting purposes. As a result, income tax expense recorded for any period represents the total tax applicable to the income reported in the financial statements for that period, regardless of when such taxes are actually paid.

Investment tax credit benefits are recognised in earnings in the period the qualified property is placed into service, using the "flow-through" method - first to the extent applicable against income tax expense on pretax accounting income or as carrybacks against prior years' tax liabilities and, second, as to any unused remainder, against income tax expense by reducing existing net deferred tax credits to the extent that those deferred tax credits are expected to reverse during the investment tax credit carryover period. As investment tax credits are utilised on the federal income tax return, such amounts are restored to deferred income taxes.

**Mileage Plus Awards.** UAL Inc. accrues the estimated incremental cost of providing free travel awards earned under its Mileage Plus frequent flyer programme.

*(b) Foreign Exchange Losses*

In August 1987, UAL hedged all Japanese yen-denominated debt through the purchase of forward exchange contracts and foreign currency call options. These arrangements expired during February 1988 and were replaced by foreign currency call options. Expiration dates of the foreign currency options range from 5th January, 1989 to 12th April, 1989. UAL anticipates entering into new hedge arrangements as the previous arrangements expire.

*(c) The Covia Partnership*

On 5th August, 1988, UAL Inc. consummated the sale of 50 per cent. of its voting interests in the Covia Partnership, the entity that owns the Apollo computer reservation system, to affiliates of Alitalia-Linee Aeree S.p.A., British Airways Plc, KLM Royal Dutch Airlines, Swissair Swiss Air Transport Company Ltd. and USAir Group Inc. for an aggregate purchase price of \$493.0 million in cash after deducting direct selling expenses. The sale resulted in a non-recurring pretax gain of \$393.0 million which is reflected on the statement of consolidated operations in "Other deductions (income)." The sale had the effect of increasing net earnings for 1988 by \$223.4 million, \$7.53 per share.

UAL Inc.'s continuing interest in the Covia Partnership is being accounted for under the equity method of accounting. Accordingly, UAL's consolidated financial statements have been restated to reflect the equity method of accounting for 1988 periods prior to 5th August, 1988. The consolidated financial statements for 1987 and 1986 have not been restated as the Covia Partnership was not organised as a separate entity until 2nd January, 1988, and therefore no reliable financial data is available for prior years.

UAL Inc. has operating agreements with the Covia Partnership under which UAL Inc. provides certain computer support services for, and purchases computer reservation services, communications and other information services from, the Covia Partnership. Revenues derived from the sale of services to the Covia Partnership amounted to approximately \$67.0 million in 1988. The cost to UAL Inc. of services purchased from the Covia Partnership amounted to approximately \$176.0 million.

*(d) Cash and Cash Equivalents*

Cash and cash equivalents were as follows as at 31st December:—

	1987	1988
	\$000	\$000
Cash	14,699	47,228
Repurchase agreements	861,796	10,179
US government securities	559,741	98,006
Eurodollar certificates of deposit	160,272	323,840
Commercial paper	155,455	301,307
Bankers' acceptances	47,739	306,264
Other	408,317	—
	<u>2,208,019</u>	<u>1,086,824</u>

UAL actively employs repurchase agreements in its investments programme. The exposure to loss as a result of their use is minimised because UAL takes delivery of the underlying collateral.

*(e) UAL Leasing*

Summarised earnings data of UAL Leasing is as follows:—

	1986	1987	1988
	\$000	\$000	\$000
Revenues	22,372	23,308	21,083
Expenses	19,281	31,004	46,073
Foreign exchange losses	40,037	19,735	—
	<u>(36,946)</u>	<u>(27,431)</u>	<u>(24,990)</u>
Pretax loss	(12,798)	(7,601)	(2,448)
Provision(credit) for income taxes	<u>(24,148)</u>	<u>(19,830)</u>	<u>(22,542)</u>
Net loss			

UAL Leasing's summarised financial position as at 31st December was as follows:—

	1987	1988
	\$000	\$000
Cash and marketable securities	40,160	34,050
Receivables from affiliates	63,644	64,677
Other receivables	21,698	9
Net investment in direct financing lease	86,536	84,819
Flight equipment leased to UAL Inc., net	21,149	19,631
<b>Total assets</b>	<b>233,187</b>	<b>203,186</b>
Deferred purchase certificates, 7.1% and 7.2%, due 1991 to 2001 (38,756,900 Japanese yen)	320,305	310,105
Other liabilities	10,172	8,833
Parent company's investment*	(97,290)	(115,752)
<b>Total liabilities and parent company's investment</b>	<b>233,187</b>	<b>203,186</b>

\* Includes (\$54.1 million) and (\$50.0 million) at 31st December, 1987 and 1988, respectively, representing the excess of UAL Leasing's purchase price of aircraft acquired from UAL Inc. over UAL Inc.'s book value of such aircraft at the date of sale, less subsequent amortisation.

(f) Short Term Borrowings

Short term borrowings as at 31st December are summarised below:—

	1987	1988
	\$000	\$000
Notes payable to others	296,961	446,164
Notes payable to banks	13,350	—
Convertible notes	700,000	—
	<b>1,010,311</b>	<b>446,164</b>

United Airlines Credit Corporation ("UACC"), a wholly-owned consolidated subsidiary of UAL Inc. makes short term borrowings to obtain funds for the purchase of certain accounts receivable from UAL Inc. At 31st December, 1988, purchased receivables amounting to \$447.9 million were pledged by UACC to secure repayment of \$446.2 million of such outstanding borrowings, bearing an average interest rate of 8.9 per cent. Effective 1st November, 1988, the maximum available amount of borrowings under this arrangement, was increased from \$300.0 million to \$450.0 million.

On 12th May, 1987, UAL issued \$700.0 million of 7.52 per cent. convertible notes to The Boeing Company. The notes were convertible into UAL common stock or into a new series of UAL preferred stock. On 5th January, 1988, UAL repaid the convertible notes in full, plus a prepayment premium of \$50.0 million.

(g) Income Taxes

The provisions (credits) for income taxes on earnings or losses from continuing operations are summarised as follows:—

	1986	1987	1988
	\$000	\$000	\$000
<b>Current:</b>			
Federal	(70,526)	5,500	340,982
State	1,100	13,014	80,505
	<b>(69,426)</b>	<b>18,514</b>	<b>421,487</b>
<b>Deferred:</b>			
Federal	(41,202)	(19,787)	(28,495)
State	(4,232)	(7,118)	(4,118)
	<b>(45,434)</b>	<b>(26,905)</b>	<b>(32,613)</b>
	<b>(114,860)</b>	<b>(8,391)</b>	<b>388,874</b>

Income tax provisions (credits) differed from "expected" amounts computed at the statutory federal income tax rate, as follows:—

	1986	1987	1988
	\$000	\$000	\$000
Income tax provision (credit) at statutory rate	(104,740)	(5,034)	336,188
Investment tax credits, net of recaptures	(20,139)	(39,343)	(25,597)
Tax basis adjustments relating to investment tax credits	9,790	18,808	12,067
State income taxes, net of federal income tax benefit	(1,693)	3,512	51,384
Non-deductible employee meals	—	6,040	5,440
Other, net	1,922	7,626	9,392
<b>Income tax provision (credit), as reported</b>	<b>(114,860)</b>	<b>(8,391)</b>	<b>388,874</b>

The Tax Reform Act of 1986 repealed investment tax credits, except for certain qualifying aircraft. UAL Inc. accepted delivery of its last qualifying aircraft in 1988. The Tax Reform Act also reduced the statutory corporate federal income tax rate from 46 per cent. in 1986 to 40 per cent. in 1987 and 34 per cent. in 1988 and subsequent years.

The components of the provisions (credits) for deferred income taxes from continuing operations were as follows:—

	1986	1987	1988
	\$000	\$000	\$000
Deferred tax provision (credit) for timing differences:			
Gain on sale and lease back transactions	—	(10,427)	(62,526)
Depreciation and capitalised interest	46,456	17,966	50,785
Foreign exchange gains and losses	(46,557)	(19,940)	(44,179)
Pension expense	(48,471)	(27,148)	29,142
Other employee benefits	(6,345)	(26,245)	(25,659)
Transfers of tax benefits	5,165	11,919	5,701
Litigation provision	4,641	15,527	1,771
Other, net	(10,113)	(7,365)	285
Tax basis adjustments relating to investment tax credits	(55,224)	(45,713)	(44,680)
	9,790	18,808	12,067
	(45,434)	(26,905)	(32,613)

In December 1987, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 96, "Accounting for Income Taxes," which requires an asset and liability approach for financial accounting and reporting for income taxes. Companies are required to adopt the new standard no later than 1990, with early adoption being permitted, and previously issued financial statements may be restated to conform with the provisions of the statement. UAL has not determined whether it will implement the early adoption or restatement provisions of this standard, nor can UAL reasonably estimate at this time the effects that adoption will have on its financial statements due to uncertainties related to transactions which may occur in 1989.

#### (h) Long Term Debt

A summary of long term debt, excluding current maturities, as at 31st December is as follows (interest rates are as at 31st December, 1988):—

	1987	1988
Secured notes, 7.02% to 11.54%, averaging 9.5%, due 1989 to 1997	\$000	\$000
Equipment trust certificates, 11.75% to 12.65%, averaging 12.1%, due 1989 to 1999	211,400	276,595
Deferred purchase certificates, 7.1% and 7.2%, due 1991 to 2001 (102,795,403 Japanese yen)	57,770	48,453
Senior subordinated notes, 12.5% and 13%, due 1995 and 1998	849,549	822,495
Promissory notes	—	500,000
Other	160,000	—
	2,132	1,396
	1,280,851	1,648,939

In March 1988, UAL Inc. entered into an agreement with a group of banks obtaining up to \$2.435 billion of financing through an eight year \$1.235 billion term loan facility, a five year \$600.0 million letter of credit facility and a \$600.0 million revolving credit facility. UAL Inc.'s previous \$750.0 million revolving credit agreement was cancelled when the financing discussed above was completed.

The credit agreement requires UAL Inc.'s obligations thereunder to be guaranteed by UAL and secured by a pledge of a substantial portion of UAL Inc.'s assets, and it places substantial restrictions on future activities of UAL Inc. and UAL. It restricts the creation of negative pledges; amendments or changes of certain terms of outstanding indebtedness; the incurrence of liens, mortgages or other encumbrances; the use of proceeds from the sale or other disposition of assets; investments; the incurrence of contingent obligations; dividends; payments with respect to repurchase of subordinated debt and capital stock; mergers and consolidations; the incurrence of debt and guarantees; certain transactions between UAL Inc. and UAL and their shareholders and affiliates; certain sale and lease back transactions; and the conduct of business of UAL and UAL Leasing. The agreement also requires UAL Inc. and UAL to satisfy certain financial tests, including a fixed charge coverage test and a leverage test. Under the agreement, UAL is required to make an equity contribution to UAL Inc. equal to the net proceeds of any debt or equity securities issued by UAL, and UAL Inc. is unable to pay dividends to UAL, with certain exceptions. In addition, the agreement requires the repayment of any outstanding loans under certain circumstances, including the sale of assets, the issuance of debt or equity securities, and the occurrence of excess cash flows, as defined. Under the dividend restrictions, UAL is unable to pay dividends to its common shareholders.

In March 1988, UAL Inc. borrowed \$1.235 billion under the term loan facility of this agreement and repaid \$160.0 million of existing promissory notes. In June 1988, UAL Inc. issued \$150.0 million of 12½ per cent. senior subordinated notes due 1995 and \$350.0 million of 13 per cent. senior subordinated notes due 1998. The net proceeds from the sale of these notes and other funds were used to repay the borrowings outstanding under the term loan facility.

During March 1988, letters of credit aggregating \$440.7 million were issued under the letter of credit facility to replace all those previously outstanding. In November 1988, additional letters of credit aggregating \$146.6 million were issued. A commitment fee of ¼ per cent. per annum is payable on the total letter of credit commitment.

Under the revolving credit facility, \$600.0 million of credit is available through March 1991, with any outstanding borrowings at that date payable in equal semi-annual instalments through March 1992. A commitment fee of ½ per cent. per annum is payable on the unused available credit under the revolving credit facility. Borrowings under the revolving credit facility would bear interest, payable not less than quarterly, at an annual rate equal to, at the option of UAL Inc., either (1) ½ of 1 per cent. over the greater of Manufacturers Hanover Trust Company's reference rate or ½ of 1 per cent. over the federal funds rate, (2) 1½ per cent. over the two, three or six month London interbank (Eurodollar) offered rate or (3) 1¾ per cent. over the 60, 90 or 180 day certificate of deposit rate. As at 31st December, 1988, the entire amount of the \$600.0 million revolving credit facility was available.

In December 1988, UAL Inc. entered into a standby credit facility agreement with a group of banks to be used solely to finance the purchase or long term lease of aircraft. The agreement provides for up to \$1.0 billion in financing and is available until 31st December, 1992. A commitment fee of .1875 of 1 per cent. per annum is payable on the unused available credit under the standby credit facility. Borrowings under the standby credit facility would bear interest, subject to UAL Inc.'s credit rating at the time of draw-down, at a minimum of ¾ of 1 per cent. over, at UAL Inc.'s option, the 90 day or 180 day London interbank offered rate. Borrowings under this agreement would have a maximum term of 18½ years and be secured by the aircraft financed. As at 31st December, 1988, all \$1.0 billion of financing under this agreement was available for borrowing.

Maturities of long term debt for each of the four years after 1989 were: 1990 - \$62.8 million; 1991 - \$119.4 million; 1992 - \$128.6 million; and 1993 - \$90.9 million.

Various assets of UAL Inc. principally aircraft, having an aggregate book value of approximately \$2.1 billion at 31st December, 1988, were pledged under various loan agreements and equipment trust certificates or to assure performance of certain lease obligations.

In 1984 UAL and UAL Inc. completed "in-substance defeasances" of their 5 per cent. and 4¾ per cent. subordinated debentures and UAL Inc. completed an "in-substance defeasance" of a portion of its 8¼ per cent. secured notes by placing US Government obligations, maturing as to principal and interest in amounts sufficient to make all payments due with respect to such debt, in an irrevocable trust. As at 31st December, 1988, the total principal amount of such indebtedness that was considered to be extinguished, and therefore excluded from consolidated long term debt, was \$65.1 million.

*(i) Lease Obligations*

As at 31st December, 1988, UAL Inc. leased 83 of its aircraft, 24 of which were capital leases and 5 of which were leased from UAL Leasing under operating leases. The majority of these leases have terms of 18 years, and expiration dates range from 1989 through to 2011. Under the terms of leases for 76 of the aircraft, UAL Inc. has the right of first refusal to purchase, at the end of the lease term, certain aircraft at fair market value and others at either fair market value or a percentage of cost. Other leases include airport passenger terminal space, aircraft hangars and related maintenance facilities, cargo terminals, flight kitchens, real estate, office and computer equipment and vehicles.

Future minimum lease payments as at 31st December, 1988, under capital leases and under non-cancellable operating leases having initial or remaining lease terms of more than one year are shown below:—

	Operating Leases	Capital Leases
Payable during:	\$000	\$000
1989	308,617	59,747
1990	344,287	62,915
1991	334,519	64,889
1992	325,259	66,237
1993	295,054	66,152
After 1993	5,131,786	390,994
Total minimum lease payments	<u>6,739,522</u>	<u>710,934</u>
Imputed interest (at rates of 5.3% to 12.2%)		(281,539)
Present value of minimum lease payments		<u>429,395</u>
Current portion		(18,113)
Long term obligations under capital leases		<u>411,282</u>

Amounts charged to rent expense, net of minor amounts of sub-lease rentals, were \$172.4 million in 1986, \$211.0 million in 1987 and \$275.1 million 1988.

*(j) Redeemable Preferred Stock*

There were 33,638 and 28,474 shares of 5½ per cent. cumulative prior preferred stock authorised and outstanding at 31st December, 1987, and 1988, respectively. Each share is entitled to one vote and is redeemable at any time at the option of UAL at \$100 per share. During 1987 and 1988, 3,801 and 5,164 shares, respectively, were redeemed through purchases. Redemption of 3,034 shares is required by 1st June, 1989, 4,770 shares annually by 1st June, 1990 to 1994 and 1,590 shares by 1st June, 1995.

*(k) Non-Redeemable Preferred Stock, Common Stock and Other Shareholders' Equity*

In December 1985, UAL called its Series B preferred stock for redemption in January 1986. In January 1986, 9,279,437 Series B preferred shares were converted into 5,431,719 shares of common stock and 62,518 shares were redeemed (at a price of \$26.05 per share, plus accumulated dividends of \$.10 per share).

On 29th March, 1988, pursuant to a self-tender offer, UAL purchased 35,500,000 shares of its common stock at \$80 per share in cash. UAL subsequently retired these shares and capitalised \$23.3 million of retained earnings. As a result of the retirement of these shares, and the issuance of 362,447 shares on exercises of stock options, common stock issued decreased by 35,137,553 shares in 1988.

Common stock issued increased by 8,247,019 shares in 1987 (2,508,609 issued in the Hilton International acquisition in March 1987, 5,500,000 sold at \$56.50 per share in April 1987 and 238,410 on exercises of stock options) and by 14,910,498 shares in 1986 (4,400,000 sold at \$56.75 per share in February 1986, 5,000,000 sold at \$58.00 per share in October 1986, 5,431,719 on conversions of Series B preferred stock and 78,779 on exercises of stock options).

During 1987, UAL purchased 1,730,400 of its common shares through open market transactions at a cost of \$122.3 million.

On 31st December, 1986, UAL issued a dividend of one preferred share purchase right for each outstanding share of common stock. Each right, when it becomes exercisable, will entitle the holder to buy from UAL one one-hundredth of a share of Series C junior participating preferred stock, without par value, for \$185 (subject to antidilution provisions). Holders of Series C preferred stock are entitled to 100 votes for each share. The rights will become exercisable upon the earlier of (1) ten days after a person or group has acquired 20 per cent. or more of UAL's common stock or (2) ten days following the public announcement of an offer to acquire 30 per cent. or more of UAL's common stock. If UAL is involved in a merger or a self-dealing transaction with an acquirer at any time after the rights become exercisable, each right will entitle its holder to buy common stock of the acquiring company or UAL (depending on which entity survives) having a market value of twice the exercise price of the right. UAL has the right to redeem the rights for \$.05 per right prior to the time they become exercisable. The rights expire on 31st December, 1996.

*(l) Stock Options*

UAL's 1981 Incentive Stock Option Programme, as amended (the "1981 Plan"), permits the issuance of up to 3,300,000 shares of common stock pursuant to grants of "incentive stock options" under the Internal Revenue Code and to grants of non-statutory stock options or stock appreciation rights ("SARs"). The option price for all stock options, and the base from which appreciation of stock appreciation rights is to be measured, will be 100 per cent. of market value of common stock at the dates of grant. Under the 1981 Plan, options for 667,379 shares of common stock were outstanding at 31st December, 1987. During 1988, options for 773,900 shares were granted, at prices from \$69.00 to \$107.75 per share, options for 465,616 shares were exercised, at prices from \$16.75 to \$58.25 per share, and options for 91,008 shares were terminated. At 31st December, 1988, options for 889,655 shares, at prices from \$42.125 to \$107.75 per share, were outstanding (222,835 of which were exercisable). The expiration dates for such outstanding options ranged from 24th October, 1994 to 12th December, 1998. As at 31st December, 1988, options granted under the 1981 Plan were held by 142 officers and key employees. As at 31st December, 1988, additional options or SARs could be granted with respect to 893,596 shares under the 1981 Plan.

During 1988 and 1986, SARs were granted in tandem with non statutory stock options. On exercise of these SARs, holders will receive in cash 100 per cent. of the appreciation in fair market value of the shares subject to the SAR. The estimated payment value of SARs is being charged to earnings over the vesting period. Such charge amounted to \$1.0 million in 1986, \$8.2 million in 1987 and \$11.5 million in 1988. As at 31st December, 1988, 493,154 SARs were outstanding at prices of \$48.50 to \$83.313 per share.

In 1988, the remaining 10,000 non statutory stock options outstanding under UAL's 1969 Incentive Stock Option Plan were exercised at a price of \$40.50 per share.

In connection with exercises of stock options in 1986, 1987 and 1988, 3,895 shares, 1,000 shares and 1,000 shares, respectively, of outstanding UAL common stock were tendered to UAL by optionees and were resold.

During 1988, UAL adopted the 1988 Restricted Stock Plan (the "1988 Plan") under which officers and key employees may be awarded up to 500,000 shares of common stock through March 1998. Vesting of the shares will occur over a period not to exceed ten years. At 31st December, 1988, no shares of common stock had been awarded under the 1988 Plan.

*(m) Retirement Plans*

UAL Inc. has various retirement plans which cover substantially all employees. Defined benefit plans covering certain employees (primarily union ground employees) provide benefits of stated amounts for specified periods of service, while defined benefit plans for other employees provide benefits based on employees' years of service and average compensation for a specified period of time before retirement. Pension costs are funded, for the most part, at the minimum level required by the Employee Retirement Income Security Act of 1974. There are also defined contribution plans for certain groups of employees (primarily airline pilots), company contributions for which are a percentage of participants' earnings or a percentage of participants' contributions.

The following table sets forth the plans' funded status and amounts recognised in the statement of consolidated financial position as at 31st December:

	1987		1988	
	Assets Exceed Accumulated Benefits \$'000	Accumulated Benefits Exceed Assets \$'000	Assets Exceed Accumulated Benefits \$'000	Accumulated Benefits Exceed Assets \$'000
Actuarial present value of accumulated benefit obligation <sup>(1)</sup>	1,002,799	189,751	1,125,837	272,074
Actuarial present value of projected benefit obligation <sup>(2)</sup>	1,299,704	384,672	1,478,961	412,083
Plan assets at fair value	1,536,310	90,060	1,653,346	168,836
Projected benefit obligation in excess of (less than) plan assets	(236,606)	294,612	(174,385)	243,247
Unrecognised net gain (loss)	253,187	28,663	212,039	64,638
Prior service cost not yet recognised in net periodic pension cost	(28,257)	(77,608)	(26,399)	(72,335)
Remaining unrecognised net asset from 1st January, 1985	139,135	5,076	125,352	4,664
Adjustment required to recognise minimum liability <sup>(3)</sup>	—	—	—	—
Pension liability recognised in the statement of consolidated financial position	127,459	250,743	136,607	240,214

(1) For the valuation of pension obligations as at 31st December, 1987 and 1988, the weighted average discount rate used was 10.5 per cent. Substantially all of the accumulated benefit obligation is vested.

(2) As permitted, UAL Inc. has determined not to recognise an additional minimum pension liability as at 31st December, 1988 for plans where accumulated benefits exceed assets.

Plan assets were invested approximately as follows as at 31st December:

	1987 %	1988 %
Cash equivalents and short term governmental and corporate instruments	9	10
Long term governmental and corporate instruments	40	39
Common stock	39	43
Real estate and other investments	12	8
	<u>100</u>	<u>100</u>

The net periodic pension cost of UAL Inc.'s defined benefit plans included the following components:

	1986 \$000	1987 \$000	1988 \$000
Service costs - benefits earned during the year	109,818	124,723	98,996
Interest cost on projected benefit obligation	131,710	156,328	172,339
Actual return on plan assets	(119,848)	(93,431)	(183,355)
Net amortisation and deferral	(21,361)	(60,361)	(14,213)
Net periodic pension cost	<u>100,319</u>	<u>127,259</u>	<u>73,767</u>
Significant assumptions used:			
Weighted average discount rate	9.0%	8.5%	10.5%
Rate of increase in future compensation levels	6.5%	6.0%	6.75%
Expected long term rate of return on assets	9.0%	9.5%	11.0%

Total pension expense for all retirement plans (including defined contribution plans) was \$155.8 million in 1986, \$187.8 million in 1987 and \$133.4 million in 1988.

(n) *Post-retirement benefits*

UAL Inc. provides certain life insurance and health care benefits for substantially all retired employees. The estimated cost of life insurance benefits is accrued and funded over the working lives of those employees expected to qualify for such benefits. The cost of health care benefits is recognised as claims are paid. The total cost of these post-retirement benefits was \$17.2 million in 1986, \$19.4 million in 1987 and \$22.8 million in 1988.

(o) *Contingencies and Commitments*

The companies have certain contingencies resulting from litigation and claims incident to the ordinary course of business. These include several lawsuits brought against UAL Inc. by a number of other air carriers alleging violation of the anti-trust laws and other laws in the operation of UAL Inc.'s computer reservations systems. Legal counsel believes that UAL Inc. will be able to successfully defend these lawsuits. Management believes, after considering a number of factors, including (but not limited to) the views of legal counsel, the nature of contingencies to which the companies are subject and the prior experience of the companies, that the ultimate disposition of these contingencies is not expected to materially affect UAL Inc.'s consolidated financial position.

Consolidated commitments as at 31st December, 1988 for the purchase of property and equipment, principally aircraft, approximated \$4.490 billion, after deducting advance payments. An estimated \$1.670 billion of these commitments will be spent during 1989, \$1.910 billion in 1990, \$570.0 million in 1991 and \$340.0 million in 1992. The major commitments are for the purchase of 61 B-737-300 aircraft, 30 B-757-200 aircraft and 15 B-747-400 aircraft. The B-737-300s and B-757-200s are to be delivered through 1990 and 1991, respectively. The B-747-400s will be delivered by 1992, with 4 scheduled to be delivered in 1989.

As at 31st December, 1988 UAL had guaranteed \$61.4 million of airport lease revenue bonds (including accrued interest) and UAL Inc. had guaranteed \$38.3 million of indebtedness of affiliates.

Special facility revenue bonds have been issued by certain other municipalities to build or improve airport facilities leased by UAL Inc.. Under the lease agreements, UAL Inc. is required to make rental payments sufficient in amount to pay when due the principal and interest on the bonds. As at 31st December, 1988, \$516.4 million principal amount of such bonds was outstanding. Payment of UAL Inc.'s obligations is secured through standby letters of credit issued under UAL Inc.'s credit agreement.

Transfers of the tax benefits of accelerated depreciation and investment tax credits associated with the acquisition of certain equipment have been made previously by UAL Inc. to various tax lessors through tax lease transactions. Proceeds from tax benefit transfers were recognised as income in the year the lease transactions were consummated. The subject equipment is being depreciated for book purposes. UAL Inc. has agreed to indemnify (guaranteed in some cases by UAL) the tax lessors against loss of such benefits in certain circumstances and has agreed to indemnify others for loss of tax benefits in limited circumstances for certain used aircraft purchased by UAL Inc. subject to previous tax lease transactions.

Certain tax lessors have required that letters of credit be issued in their favour by financial institutions as security for UAL Inc.'s indemnity obligations under the leases. The outstanding balance of such letters of credit totalled \$91.9 million as at 31st December, 1988. At that date, UAL Inc. had granted mortgages on aircraft and engines having a total book value of \$243.9 million as security for indemnity obligations under tax leases and letters of credit.

*(p) Foreign Operations*

UAL Inc. conducts operations in various foreign countries, principally in the Pacific. Operating revenues from foreign operations were approximately \$960.0 million in 1986, \$1.360 billion in 1987 and \$1.790 billion in 1988.

*(q) Discontinued Operations*

On 31st January, 1988, UAL consummated the sale of Westin to Caesar Park Hotel Investment, Inc., a unit of Aoki Corporation of Japan and the Robert M. Bass Group, for \$1.350 billion in cash.

On 31st March, 1987, UAL acquired all of the outstanding capital stock of Hilton International from a liquidating trust for stockholders of Transworld Corporation for \$835.7 million in cash and 2,508,609 shares of UAL common stock valued at \$56.50 per share. Short term borrowings of \$800.0 million were issued in connection with the Hilton International acquisition, and were repaid during 1987.

On 14th October, 1987, UAL consummated the sale of Hilton International to Ladbroke Group PLC, for \$1.070 billion in cash and on 30th December, 1987, UAL consummated the sale of Hertz to Park Ridge Corporation for \$1.3 billion in cash.

The results of discontinued operations are included in UAL's consolidated earnings for the periods they were owned. Their summarised results were as follows:

	1986	1987	1988
Operating revenues	\$000	\$000	\$000
Operating expenses	2,091,092	2,720,238	32,902
Other deductions, net	1,757,174	2,440,185	30,846
	28,721	127,384	1,790
Pretax earnings	305,197	152,669	266
Income taxes -			
Current	108,259	80,159	(486)
Deferred	72,503	3,693	295
Earnings from discontinued operations	124,435	68,817	457

The net assets of discontinued operations, net of intercompany eliminations, as at 31st December, 1987 are summarised as follows:

	\$000
Current assets	179,911
Operating property and equipment, net	570,641
Other assets	96,601
Total assets	847,153
Current liabilities	(196,904)
Long term debt and capital leases	(128,283)
Other liabilities and deferred credits	(95,219)
Net assets	426,747

The provisions (credits) for income taxes on the gain on sales of discontinued operations are summarised as follows:

	1987	1988
	\$000	\$000
Current	256,517	349,200
Deferred	(34,086)	(25,710)
	222,431	323,490

*(r) Net Earnings (Loss) Per Share*

Primary net earnings (loss) per share are based on average common shares outstanding - 45,209,253 in 1986, 55,631,820 in 1987 and 29,681,394 in 1988. Such per-share data are after providing for preferred stock dividends of \$212,000 in 1986, \$195,000 in 1987 and \$171,000 in 1988.

Fully diluted net earnings per share for 1987 are based on 61,596,885 shares. This amount represents the shares used for the primary calculation plus average shares assumed issued at the beginning of the year for exercises of dilutive stock options and at the date of issuance for conversion of 7.52 per cent. convertible notes. Such per-share data are after providing for dividends on the 5½ per cent. cumulative prior preferred stock and elimination of net interest expense on the 7.52 per cent. convertible notes. The assumed conversion of outstanding Series B preferred stock or the exercise of stock options would not have a dilutive effect on per-share results for the years 1986 or 1988.

The decrease in the average number of common shares outstanding in 1988 resulted from UAL's purchase of 35,500,000 shares of its common stock on 29th March, 1988. On a pro forma basis, if the self-tender offer had been completed on 1st January, 1988, the average number of common shares outstanding would have been 21,489,085 for 1988. Assuming completion of the self-tender offer on 1st January, 1988 and excluding the gain on the sale of Covia Partnership interests (see (c) The Covia Partnership), pro forma 1988 earnings per share from continuing operations would have been \$16.26.

## APPENDIX 2

### FINANCIAL INFORMATION ON AIRLINE ACQUISITION CORP.'S TENDER OFFER

The tender offer by Airline Acquisition Corp. for UAL will be financed with a combination of preferred and common equity and the remainder in bank debt. The tender offer financing will be applied as to \$6,545 million in the purchase of UAL common stock, as to \$240 million in the cancellation of UAL stock options and as to approximately \$400 million in expenses in connection with, and prepaid interest on financing for, the tender offer. British Airways is contributing \$750 million in cash for preferred equity in Airline Acquisition Corp.. The ESOPs will borrow the funds required to purchase common equity or convertible preferred stock from Airline Acquisition Corp., which will in turn obtain these funds through bank borrowings. As set out in note (vi) below, Airline Acquisition Corp. has received a commitment pertaining to a \$5.9 billion loan facility to be used to fund the ESOPs' stock purchase as well as to refinance existing indebtedness and tender offer borrowings and to finance the conversion of UAL common shares outstanding after the tender offer into the right to receive \$300 per share in the merger.

Further details on the various sources of financing are as follows:—

#### (i) Common Stock

The senior management of UAL will purchase 1 per cent. of Airline Acquisition Corp.'s common stock on a fully diluted basis for \$15 million and receive an option to purchase an additional 9 per cent. on a fully diluted basis (exercisable at \$15 million per each additional 1 per cent. of the original option). The ESOPs will receive either Airline Acquisition Corp. common stock, convertible preferred stock (which will vote with the common equity prior to conversion) or a combination thereof; such stake will entitle the ESOPs to 75 per cent. of Airline Acquisition Corp.'s voting equity on a fully diluted basis. The ESOPs will obtain the funds to purchase this stock through a loan from Airline Acquisition Corp. of bank borrowings made by Airline Acquisition Corp.

#### (ii) Convertible Preferred

British Airways will not be able to sell its holding of Convertible Preferred for a period of five years, unless a public offering of Airline Acquisition Corp.'s equity securities has occurred or unless any person, entity or group (other than the ESOPs) acquires 50 per cent. or more of Airline Acquisition Corp.'s voting securities. The Convertible Preferred will rank subordinate to all Airline Acquisition Corp. debt and equity securities other than its common stock.

#### (iii) 13 per cent. Securities

The 13 per cent. Securities will rank subordinate to all existing and future debt of Airline Acquisition Corp., to the Bridge Preferred or Pilot Preferred (as defined below) and to the 18 per cent. Securities. The 13 per cent. Securities may not be transferred except to an entity controlled by British Airways. The 13 per cent. Securities will be redeemed at par plus any accrued but unpaid dividends on the twelfth anniversary of their issue and may be redeemed at par at the option of the Board of Airline Acquisition Corp. at any time. The 13 per cent. Securities are exchangeable in whole at Airline Acquisition Corp.'s option into a debt security of Airline Acquisition Corp., provided that the holder will be compensated for any tax payable in respect of the gain, if any, realised upon such exchange, and that such exchange will have a neutral effect on the holder's after-tax return, under any applicable US, UK or other tax laws.

#### (iv) 18 per cent. Securities

British Airways may sell the 18 per cent. Securities, subject to Airline Acquisition Corp. Board approval (which shall not be unreasonably withheld), during the first two years after issue and without such approval at any time thereafter. In the event that British Airways decides to sell the 18 per cent. Securities, the dividend rate will be reset so as to render them marketable at par, subject to the rate not exceeding 21 per cent.. British Airways shall have a call on warrants representing up to 2 per cent. of Airline Acquisition Corp.'s fully diluted voting common equity (which warrants shall not be dilutive to British Airways' 15 per cent. voting equity stake); such warrants shall be issued only as and if needed to achieve marketability of the 18 per cent. Securities at par within the 21 per cent. dividend rate limitation, shall be issued to and exercisable by US persons only and shall become exercisable only in the event of a public offering of Airline Acquisition Corp. common equity securities. The 18 per cent. Securities are exchangeable in whole at Airline Acquisition Corp.'s option into a debt security of Airline Acquisition Corp., provided that the holder will be compensated for any tax payable in respect of gain, if any, realised upon such exchange, and that such exchange will have a neutral effect on the holder's after-tax return, under any applicable US, UK or other tax laws. The 18 per cent. Securities may be redeemed by Airline Acquisition Corp. at par plus any accrued but unpaid dividends at any time after 1st April, 1991 while they are held by British Airways and will be redeemed on the twelfth anniversary of their issue. The 18 per cent. Securities will rank subordinate to all existing and future debt of Airline Acquisition Corp. and to the Bridge Preferred or Pilot Preferred (as defined below).

#### (v) Bridge Preferred/Pilot Preferred

Airline Acquisition Corp. and Salomon Brothers Holding Company Inc. ("SBHC") have entered into a commitment letter pursuant to which SBHC has committed to purchase (or cause an affiliate to purchase), if requested to do so, up to \$200 million of preferred stock of Airline Acquisition Corp. or UAL (the "Bridge Preferred"), together with warrants (the "Bridge Warrants") to purchase up to four per cent. of Airline Acquisition Corp.'s common stock on a fully diluted basis otherwise being made available to the UAL pilots. Such funds will be used to provide an interim financing source for the funds expected to be provided ultimately from the purchase by a UAL pilots' pension fund at the individual direction of the pilot beneficiaries of \$200 million (or such greater amount as may be necessary to redeem the Bridge Preferred) of market rate preferred stock of Airline Acquisition Corp. (the "Pilot Preferred").

The Bridge Preferred will initially have a dividend rate of 16 per cent. per annum. Upon the first anniversary of the Bridge Preferred, the dividend rate will be reset within a range of 12 per cent. to 21 per cent. so that, if the Bridge Preferred and the Bridge Warrants were then to be sold by SBHC as a unit, SBHC would realise net proceeds of \$200 million (plus accrued and unpaid dividends).

Until the fifth anniversary of the original issuance of the Bridge Preferred, dividends may, at the issuer's option, be paid in cash or additional shares of Bridge Preferred. To the extent that, during such period, dividends are not paid currently in cash, they will be required to be paid in additional shares of Bridge Preferred. Following such five year period, dividends may be paid only in cash. The Bridge Preferred will be entitled to a liquidation preference equal to face amount plus accrued and unpaid dividends. At any time on or prior to 11th June, 1990, the Bridge Preferred may be redeemed by the issuer at face amount plus accrued and unpaid dividends. Alternatively, the issuer's right of redemption during this period may be

structured as a call on the Bridge Preferred, at face amount, by the pilots, with the accrued and unpaid dividends to be paid by the issuer. After 11th June, 1990, the Bridge Preferred may not be redeemed until the commencement of the eighth year after issuance, and then may be redeemed only at a declining premium (plus accrued and unpaid dividends).

The issuer will be required to redeem all of the Bridge Preferred which remains outstanding upon the twelfth anniversary of issuance at a redemption price equal to the face amount of the Bridge Preferred plus accrued and unpaid dividends.

The Bridge Preferred will be senior to all classes of the preferred stock of Airline Acquisition Corp. or the surviving corporation. The terms of the Bridge Preferred will provide that no preferred stock may be issued by Airline Acquisition Corp. or the surviving corporation which ranks senior in right of payment to the Bridge Preferred.

The Bridge Warrants will be exercisable at any time, in whole or in part for 10 years after issuance, for up to four per cent. of the fully diluted Airline Acquisition Corp. common stock. Prior to 11th June, 1990, the Bridge Warrants are subject to call (without consideration) by the pilots based on the amount of the Bridge Preferred redeemed.

Prior to 11th June, 1990, up to \$150 million face amount of the Bridge Preferred and up to 75 per cent. of the Bridge Warrants may be transferred by SBHC. Thereafter, there will be no restrictions on transfer of the Bridge Preferred or the Bridge Warrants, except that all transfers shall be subject to the requirements of applicable law and no transfer will be made, by SBHC or any transferee, if such transfer would cause the issuer to be subject to the periodic reporting requirements of the US Securities Exchange Act of 1934.

(vi) Bank debt

The bank financing will comprise two separate facilities. The first, for up to \$6.4 billion, will be used to fund the purchase of UAL common stock pursuant to Airline Acquisition Corp.'s tender offer and for the payment of interest, fees and expenses in connection therewith. This facility will be repaid in full at the earlier of (i) 180 days after the first purchase of UAL common stock pursuant to the tender offer and (ii) the effective time of the merger of Airline Acquisition Corp. and UAL. The second facility will comprise \$5.9 billion, divided into a term loan to refinance certain existing indebtedness and loans under the first facility and to finance the merger and a term loan to be on-lent by Airline Acquisition Corp. to the ESOPs to enable them to purchase common or convertible preferred stock in Airline Acquisition Corp. In addition Airline Acquisition Corp. will have available to it after the merger a revolving working capital facility of \$1.3 billion.

## APPENDIX 3

### PRO FORMA STATEMENT OF COMBINED NET ASSETS

The following is a pro forma statement of the net assets of British Airways Group extracted from the audited consolidated balance sheet as at 31st March, 1989 after the proposed investment in Airline Acquisition Corp.. It is provided for illustrative purposes only on the basis that the funding is provided as to £320 million out of the proceeds of the rights issue and as to the remainder by long term debt.

	British Airways Group 31st March, 1989 £m	Proposed investment in Airline Acquisition Corp. £m	Pro forma British Airways Group after investment in Airline Acquisition Corp. £m
<b>Fixed assets</b>			
<i>Tangible assets</i>	2,467	—	2,467
<i>Investments</i>	111	484	595
	<u>2,578</u>	<u>484</u>	<u>3,062</u>
<b>Current assets</b>			
<i>Stocks</i>	32	—	32
<i>Debtors</i>	796	—	796
<i>Cash and short term loans and deposits</i>	88	—	88
	<u>916</u>	<u>—</u>	<u>916</u>
<b>Creditors: amounts falling due within one year</b>	(1,748)	—	(1,748)
<b>Net current liabilities</b>	<u>(832)</u>	<u>—</u>	<u>(832)</u>
<b>Total assets less current liabilities</b>	1,746	484	2,230
<b>Creditors: amounts falling due after more than one year</b>	(896)	(164)	(1,060)
<b>Provisions for liabilities and charges</b>	(100)	—	(100)
<b>Net assets</b>	<u>750</u>	<u>320</u>	<u>1,070</u>

**Notes:**

- (i) US \$ amounts in respect of British Airways' proposed investment in Airline Acquisition Corp. have been translated at \$1.55 to £1.
- (ii) No adjustment has been made to reflect the trading activities of British Airways Group since the date of its latest audited consolidated balance sheet or the costs incurred in connection with the proposed investment in Airline Acquisition Corp..
- (iii) The above presentation reflects the fact that the Bonds will be included within shareholders' equity in British Airways' consolidated accounts.

## APPENDIX 4

### THE CONVERTIBLE CAPITAL BONDS, THE PREFERENCE SHARES AND THE DEED POLL

#### A. CONDITIONS OF THE BONDS

The £320,215,349 9¾ per cent. Convertible Capital Bonds 2005 ("the Bonds") will be constituted by a trust deed to be dated on or about 27th September, 1989 ("the Trust Deed") made between British Airways Capital Limited ("the Issuer"), British Airways Plc ("the Guarantor") and The Law Debenture Trust Corporation p.l.c. ("the Trustee", which expression includes its successors as trustee under the Trust Deed). The issue of the Bonds was authorised by a resolution of the Board of Directors of the Issuer passed on 29th September, 1989. The giving of the subordinated guarantee of the Bonds was authorised by a resolution of the Board of Directors of the Guarantor passed on 26th September, 1989.

The Trustee will act as trustee for the holders of the Bonds ("the Bondholders") in accordance with the provisions of the Trust Deed. Copies of the Trust Deed, the Articles of Association of the Issuer ("the Articles of the Issuer"), the Deed Poll (referred to below) and the registrar's agreement ("the Registrar's Agreement") to be dated on or about 27th September, 1989 and made between the Issuer, the Guarantor, the Trustee and the registrar specified below ("the Registrar", which expression shall include its successors as such) will be available, together with the Articles of Association for the time being of the Guarantor ("the Articles of the Guarantor"), for inspection by Bondholders at the principal office for the time being of the Trustee, being at the date hereof at Princes House, 95 Gresham Street, London EC2V 7LY.

The Bonds are convertible into fully paid Exchangeable Redeemable Preference Shares ("the Preference Shares") in the Issuer having a nominal value of 1p each and a paid-up value equal to 100p (being the "Issue Price", as defined in Condition 1(b) of the Bonds), guaranteed on a subordinated basis by the Guarantor, which shall be issued subject to and in accordance with the Articles of the Issuer.

The Preference Shares are exchangeable into fully paid Ordinary Shares of 25p each in the Guarantor ("Ordinary Shares") in accordance with the rights attaching to the Preference Shares and the terms of a Deed Poll to be executed by the Guarantor on or about 27th September, 1989 ("the Deed Poll").

The effective rate for any such exchange will, subject to adjustment in various circumstances as set out in the Articles of the Issuer and as summarised below, be 0.411523 Ordinary Shares for every Preference Share so exchanged.

In addition, the Bonds may, at the Guarantor's option and subject to the appropriate approvals and resolutions of the shareholders of the Guarantor having been obtained, be required to be exchanged into fully paid cumulative convertible redeemable preference shares in the Guarantor having a nominal value of 1p each ("Guarantor Preference Shares") which shall be issued at a price equal to the Issue Price, and subject to and in accordance with the Articles of the Guarantor. Guarantor Preference Shares will be convertible into Ordinary Shares on terms corresponding to the conversion and exchange rights attaching to the Bonds and will yield, by reference to the price at which they are issued, the same amount (including any tax credit attributable thereto to which an individual resident for United Kingdom tax purposes in the United Kingdom at the relevant time would have been entitled) per annum as represents the yield (before tax) on the Issue Price of the Bonds immediately prior to the exchange thereof for Guarantor Preference Shares. The remaining terms of the Guarantor Preference Shares shall, so far as applicable, be consistent with those of the Bonds and otherwise shall be as agreed at the relevant time between the Guarantor and a merchant bank in the City of London (selected by the Guarantor and approved by the Trustee, such approval not to be unreasonably withheld or delayed) as appropriate for an issue of cumulative convertible redeemable preference shares by a company incorporated in England and having a financial standing comparable with that of the Guarantor at the relevant time.

Certain of the statements below are summaries of and are subject to the detailed provisions of the Trust Deed, the Articles of the Issuer, the Articles of the Guarantor, the Deed Poll and the Registrar's Agreement. Bondholders will be entitled to the benefit of, will be bound by, and will be deemed to have notice of, all the provisions of the Trust Deed, the Articles of the Issuer, the Articles of the Guarantor, the Deed Poll and the Registrar's Agreement.

#### 1. Status, Form, Title and Transfers

##### (a) Status

The Bonds will constitute direct, unsecured obligations of the Issuer and will rank *pari passu* without any preference among themselves.

##### (b) Form

The Bonds will be in registered form. The Bonds will have no nominal value and will be issued at a price of 100p per Bond ("the Issue Price"). The principal amount secured by each Bond will be the Issue Price, on which interest will be payable in accordance with Condition 4, although the right to repayment thereof and the application of the proceeds is subject to these Conditions.

##### (c) Title

Title to the Bonds will pass by transfer and registration as described in Condition 1(d). The Issuer will cause to be kept at the specified office in the United Kingdom of the Registrar a register ("the Register") on which shall be entered the names and addresses of the holders of the Bonds and the particulars of the Bonds held by them and of all transfers of Bonds. The Issuer will procure that, as soon as practicable after the Issue Date (as defined in Condition 4(a)) and in any event not later than 1st December, 1989, the Register is duly made up in respect of the initial subscribers and purchasers of the Bonds and definitive certificates for the Bonds will be despatched on 1st December, 1989. Except as ordered by a court of competent jurisdiction or as required by law, the Issuer, the Guarantor, the Trustee and the Registrar shall be entitled to treat the registered holder of a Bond as the absolute owner thereof (whether or not overdue and notwithstanding any notice of ownership or writing thereon or any notice of loss or theft or of any trust or other interest therein). References herein to "holders" of Bonds, and to "Bondholders", shall be construed accordingly.

## (d) Transfers

Subject to the provisions of the Trust Deed and the Registrar's Agreement, Bonds may be transferred in whole but not in part only by delivery of the certificate or certificates for the Bonds to be transferred, together with a form of transfer in usual or common form or in any other form which the Issuer may approve, duly completed and executed by the transferor, at the specified office of the Registrar.

Upon the transfer of any Bonds a certificate for the Bonds transferred will, within 14 days of receipt of the relevant form of transfer be mailed (uninsured and at the risk of the holder entitled thereto) to such address as may be specified in such form of transfer. Where some only of the Bonds comprised in a certificate are transferred the old certificate shall be cancelled and a new certificate for the balance of such Bonds issued in lieu thereof without charge.

Transfers will be effected without charge by or on behalf of the Issuer or the Registrar, but upon payment (or the giving of such indemnity as the Registrar may require in respect) of any tax or other governmental charges which may be imposed in relation to it.

Neither the Issuer nor the Registrar will be required to register the transfer of any Bond during the period of 7 days prior to any Record Date (as defined in Condition 14) or a Required Conversion Date, a Required Exchange Date, or in respect of which Conversion and Exchange Rights or Conversion and Redemption Rights shall have been exercised.

## 2. Notification of beneficial ownership

The Guarantor shall be entitled by notice in writing (a "Bond Disclosure Notice") to require any Bondholder from time to time or any other person appearing to be interested or appearing to have been interested in the Bonds to provide the information as set out in Article 43(A) of the Articles of the Guarantor as if that Article applied to the Bonds. If a Bondholder shall fail to comply with any such requirement then until the Bondholder shall comply with such requirement to the satisfaction of the Guarantor:—

- (a) the provisions of Article 68 of the Articles of the Guarantor shall apply to the person who becomes registered in respect of the Ordinary Shares issued on the exchange of Preference Shares following the conversion of the Bonds to which the relevant Bond Disclosure Notice relates, in relation to such Ordinary Shares, as if such Bond Disclosure Notice were a Disclosure Notice (as defined in Article 43(A) of the Articles of the Guarantor);
- (b) the holder of the relevant Bonds shall not be entitled to receive any payment of interest on the Bonds; and
- (c) the holder of the relevant Bonds shall not be entitled to exercise Conversion and Exchange Rights pursuant to Condition 5(b).

See paragraph 3(g) of Appendix 5 for a summary of the relevant provisions of the Articles of the Guarantor.

## 3. Subordinated Guarantee

## (a) Guarantee

The Guarantor will, in the Trust Deed, unconditionally and irrevocably guarantee the due and punctual payment of all sums payable on or in respect of the Bonds under these Conditions (including, without limitation, interest thereon and any sums payable pursuant to Conditions 9 or 10). Such obligations will constitute a direct and unsecured obligation of the Guarantor, subordinated in accordance with Condition 3(b).

## (b) Subordination of Guarantee

If an order is made or an effective resolution is passed for the winding-up of the Guarantor, the Guarantor shall, to the extent required to make payment under the guarantee referred to in Condition 3(a), make payment only of such amounts as would have been payable if the holders of the outstanding Bonds had, on the day preceding the commencement of the winding-up, become holders of shares in the Guarantor of a class having a right to receive (*pari passu* with the holders of any other class or classes of securities which following the issue of the Bonds may be issued by the Guarantor or any subsidiary of the Guarantor with the benefit of a guarantee of the Guarantor subordinated on a similar basis) in a winding-up of the Guarantor (in priority to the holders of all other classes of shares in the Guarantor, issued or to be issued) an amount equal to the redemption monies which would have been payable if the Bonds had been converted at the date of commencement of the winding-up and the interest expressed to be payable in respect of the Bonds up to the date of commencement of the winding-up.

## 4. Interest

- (a) Each Bond shall bear interest at the rate of 9¾ per cent. per annum (or such other rate as may be specified from time to time pursuant to Condition 12) on the Issue Price. Such interest shall be paid semi-annually in arrears on 31st March and 30th September (each an "Interest Payment Date") in each year, save that the first payment of interest to be made on 31st March, 1990 will be in respect of the period from and including 20th October, 1989 ("the Issue Date") up to but excluding 31st March, 1990 and will amount to 4,327,397p per Bond and the final payment of interest to be made (subject as provided in Clause 12) on 15th June, 2005 will be in respect of the period from and including 31st March, 2005 and will amount to 2,030,137p per Bond. If any Interest Payment Date would otherwise fall on a Saturday, Sunday or a day which is a public holiday in England, such Interest Payment Date shall be the first date prior to such date which is not of such description.
- (b) Interest will cease to accrue on each Bond in respect of which Conversion and Exchange Rights are exercised on the relevant Conversion Date (as defined in Condition 5(b)) and will be paid within 7 days of the relevant date.
- (c) Where Conversion and Redemption Rights are exercised in respect of a Bond pursuant to Condition 13(a) or Condition 13(b) (and notwithstanding that the provisions of Condition 9 or 10 may apply thereto) or upon an exercise of a Guarantor Exchange Right, interest shall accrue on such Bond up to the Current Maturity Date, the Maturity Date or, as the case may be, the Required Exchange Date and will be paid within 7 days of the relevant date.
- (d) Interest will cease to accrue on each Bond on its due date for redemption or repayment unless redemption or repayment is improperly withheld or refused or default is otherwise made in payment thereof. In such event, interest will continue to accrue (as well after as before any judgment of a competent court) up to but excluding the date on which payment in full of the redemption or repayment monies in respect thereof is made.
- (e) The amount of any interest accruing in respect of a period shall be calculated on the basis of a 365-day year and the number of days elapsed.

## 5. Conversion and Exchange

### (a) Conversion and Exchange Rights

Subject to and in accordance with the provisions of this Condition, the holder of each Bond shall have the right (a "Conversion and Exchange Right") to convert such Bond into a Preference Share which shall automatically be exchanged for Ordinary Shares pursuant to the Articles of the Issuer and the Deed Poll and as provided herein.

### (b) Exercise of Conversion and Exchange Rights by Bondholders

- (i) A Bondholder will be entitled, subject as provided in paragraph (ii) below, to exercise Conversion and Exchange Rights as of 15th June ("the Annual Conversion Date") in the year 1993 and in each of the following years up to and including the year 2005 or up to and including any later year in which the Maturity Date (as defined in Condition 12) falls. Conversion and Exchange Rights may be exercised pursuant to this paragraph (i) during the period of 28 days ending on the relevant Annual Conversion Date, except where such date is also the Maturity Date when the relevant period shall commence 28 days and end 7 days prior to the Maturity Date.
- (ii) If an offer is made to the holders of Ordinary Shares (or all such holders other than the offeror and/or any associate of the offeror (as defined in Section 430(E)(4) of the Companies Act 1985 of Great Britain)) to acquire the whole or any part of the issued ordinary share capital of the Guarantor, or if any person proposes a scheme with regard to such acquisition and (such offer or scheme having become or been declared unconditional in all respects) the Issuer or the Guarantor becomes aware that the right to cast more than 50 per cent. of the votes which may ordinarily be cast on a poll at a general meeting of the Guarantor has or will become unconditionally vested in the offeror and/or associate as aforesaid (a "Relevant Event"), the Issuer or the Guarantor shall give written notice thereof (which shall include notice of all or any prior adjustments to the Exchange Rate (as described in the Articles of the Issuer) made prior to the date of such notice or in consequence of the Relevant Event pursuant to the Articles of the Issuer) to all Bondholders within 14 days of the first day on which it becomes so aware ("the Relevant Date") and each Bondholder shall be entitled to exercise Conversion and Exchange Rights as of the Relevant Date. Conversion and Exchange Rights may be exercised pursuant to this paragraph (ii) during the period of 42 days from the date of notice of the Relevant Event being given to Bondholders as aforesaid.

Each period during which Bondholders may exercise Conversion and Exchange Rights pursuant to this Condition 5(b) is herein referred to as a "Conversion Period".

The date as of which Conversion and Exchange Rights may be exercised by Bondholders pursuant to this Condition 5(b), and in the case of the exercise of Required Conversion and Exchange Rights, the Relevant Required Conversion Date (in each case as defined in Condition 5(e)), and, in the case of the exercise of Conversion and Exchange Rights by the Trustee pursuant to Condition 5(g), the Maturity Date, is herein referred to as a "Conversion Date", provided that if any Conversion Date would otherwise fall on a Saturday, Sunday or a day which is a public holiday in England, such Conversion Date shall be the first day following such date which is not of such description.

### (c) Allotment of Preference Shares

If Conversion and Exchange Rights or Required Conversion and Exchange Rights (as defined in Condition 5(e)) are exercised in respect of any Bond, such Bond shall be converted on the relevant Conversion Date into one fully paid Preference Share, which shall be allotted at a price of 100p (comprising payment in full of the nominal amount thereof of 1p and of the premium on issue thereof of 99p) in accordance with the Articles of the Issuer, credited as fully paid. One Preference Share shall be allotted on exercise of such Rights in respect of each Bond.

### (d) Ordinary Shares

By exercising a Conversion and Exchange Right, a Bondholder (or in the case of Condition 5(g), the Trustee) will be deemed, subject to and in accordance with the Articles of the Issuer and the Deed Poll, also to have exercised the Share Exchange Right (as defined in the Articles of the Issuer) applicable to the Preference Share arising on the exercise of such Conversion and Exchange Right, and the Issuer will procure that such Preference Share is exchanged, in accordance with the Articles of the Issuer and the Deed Poll, for Ordinary Shares. Ordinary Shares issued as of a Conversion Date in any year shall rank for any dividends declared or paid on the Ordinary Shares by reference to a record date on or prior to the relevant Conversion Date.

### (e) Required Conversion and Exchange by the Issuer

If immediately after any Annual Conversion Date 75 per cent. or more of the Bonds shall have been converted or redeemed, the Issuer shall (subject to the provisions of Condition 8 and to any applicable law) have the right (a "Required Conversion and Exchange Right") by not more than 56 days nor less than 28 days notice in writing to the Bondholders (a "Required Conversion Notice") expiring not earlier than 15th June, 1993 and not later than the Current Maturity Date, given not later than 28 days after such Annual Conversion Date (or any subsequent Annual Conversion Date), to convert all, but not some only, of the Bonds, as of the date of expiry of the Required Conversion Notice ("the Required Conversion Date") but with effect from the Annual Conversion Date following which the Required Conversion Notice was given, into Preference Shares, and the Share Exchange Rights in respect of all Preference Shares allotted on any such Required Conversion Date shall be deemed to have been exercised forthwith upon such allotment, and the Issuer will procure that such Preference Shares are accordingly exchanged, in accordance with the Articles of the Issuer and the Deed Poll, for Ordinary Shares. A Required Conversion Notice shall be irrevocable.

### (f) Procedure for Exercise of Conversion and Exchange Rights

A Conversion and Exchange Right may be exercised by a Bondholder delivering the certificate or certificates relating to the relevant Bond to the specified office of the Registrar, with the notice of conversion and exchange (a "Conversion and Exchange Notice") and the registration declaration (a "Nationality Declaration") as set out on the reverse thereof and/or a notice or declaration in such other form as may be as otherwise prescribed from time to time by the Issuer duly completed and signed at any time during the relevant Conversion Period together with such other information (if any) as the Issuer or the Guarantor may require to prove the title of the person exercising the Conversion and Exchange Right or as to the matters referred to in the Nationality Declaration. Conversion and Exchange Rights shall be exercised subject in each case to any applicable fiscal or other laws or regulations applicable at the place aforesaid.

Where Conversion and Exchange Rights are exercised in respect of some only of the Bonds comprised in a certificate, the old certificate shall be cancelled and a new certificate for the balance of such Bonds issued in lieu thereof without charge.

A Conversion and Exchange Notice once delivered shall be irrevocable.

(g) Exercise of Conversion and Exchange Rights by the Trustee immediately prior to Maturity Date

The Trust Deed provides that the Trustee shall (but without any responsibility for any loss occasioned thereby), within the period commencing on (but excluding) the date 7 days prior to and expiring on the day before the Maturity Date, exercise as of the Maturity Date the Conversion and Exchange Rights in respect of such of the outstanding Bonds ("Unconverted Bonds") as have not been the subject of the exercise of Conversion and Exchange Rights pursuant to Condition 5(b) or of Required Conversion and Exchange Rights or of a Guarantor's Exchange Right prior to such date, if (i) the Trustee is satisfied, or is advised by a merchant bank in the City of London selected by the Trustee, that the net proceeds of a sale of the Ordinary Shares arising from such exercise (disregarding any liability (other than a liability of the Trustee) to taxation consequent thereon) would be likely to exceed the aggregate of the interest otherwise payable on the Bonds and the redemption monies that would otherwise be payable on the Preference Shares arising as the result of the exercise of Conversion and Redemption Rights (as defined below) in respect of such Bonds on the Maturity Date pursuant to Condition 13(a) and (ii) all (if any) necessary consents have been obtained. The Ordinary Shares allotted on such exercise shall be allotted to the holders of the Unconverted Bonds but shall then be sold by the Trustee on behalf of the holder or person entitled thereto and payment of the net proceeds of sale shall be remitted to the holder or person entitled thereto in accordance with Condition 14 within one month after the Maturity Date.

(h) Taxes etc.

On the exercise of Conversion and Exchange Rights or Conversion and Redemption Rights or on any sale of Ordinary Shares being made pursuant to Condition 5(g) by or on behalf of a Bondholder or other person, such Bondholder or other person must pay all taxes and stamp, issue and registration duties (if any) arising in respect thereof (other than any taxes or capital or stamp duties or stamp duty reserve tax payable in the United Kingdom or the Island of Jersey in respect of the issue of Preference Shares on such exercise, which shall be payable by the Guarantor) and such Bondholder or other person must pay all if any taxes arising by reference to any disposal or deemed disposal of a Bond in connection with such exercise. Neither the Issuer nor the Guarantor nor any of their respective agents will impose any charge on conversion of Bonds.

6. Preference Shares

- (a) Preference Shares allotted pursuant to these Conditions will be fully paid and, save as referred to in the Articles of the Issuer, rank *pari passu* with all (if any) fully paid Preference Shares then in issue.
- (b) Whilst any Bond remains outstanding, the Guarantor shall procure that no alteration is made to the nominal value of the Preference Shares (whether by consolidation, sub-division or otherwise).
- (c) Preference Shares will be allotted as of the relevant Conversion Date (in the case of an exercise of Conversion and Exchange Rights by a Bondholder or by the Trustee or in the case of the exercise of Required Conversion and Exchange Rights by the Issuer) or the Maturity Date or Current Maturity Date (in the case of an exercise of Conversion and Redemption Rights) and will be allotted in the name of the holder of the Bond completing the relevant Conversion and Exchange Notice or his nominee (in the case of an exercise of Conversion and Exchange Rights by a Bondholder) or the Trustee, or as the Trustee may direct (in the case of an exercise of Conversion and Exchange Rights by the Trustee or the exercise of Conversion and Redemption Rights) or on behalf of the relevant Bondholder in the case of a Required Conversion and Exchange.

7. Exchange into Guarantor Preference Shares by the Guarantor

- (a) Subject to Condition 8, the Guarantor shall have the right (a "Guarantor's Exchange Right") by giving notice (a "Guarantor Exchange Notice") pursuant to Condition 7(b) to require the exchange of all, but not some only, of the outstanding Bonds for Guarantor Preference Shares, subject to all necessary approvals and resolutions of the shareholders of the Guarantor having been obtained.
- (b) A Guarantor Exchange Notice shall be given by the Guarantor to each of the holders of Bonds for the time being outstanding not less than 60 nor more than 90 days prior to the date on which a Guarantor Exchange Right is to be exercised ("the Required Exchange Date"). Such notice, once given, shall (subject as provided in Condition 8) be irrevocable and shall specify the Required Exchange Date.
- (c) On the Required Exchange Date each Bond shall be redeemed at its Issue Price and an amount equal to the Issue Price of that Bond shall be applied in paying up in full a Guarantor Preference Share of 1p par value, which shall be allotted and issued at a price equal to the Issue Price. One Guarantor Preference Share shall be allotted on exchange of each Bond.
- (d) The terms of the Guarantor Preference Shares relating to conversion into Ordinary Shares and in relation to redemption at Maturity shall correspond, so far as applicable, to the relevant Conditions of the Bonds and terms of the Preference Shares and otherwise shall be as agreed at the relevant time between the Guarantor and a merchant bank in the City of London (selected by the Guarantor and approved by the Trustee, such approval not to be unreasonably withheld or delayed) as appropriate for an issue of cumulative convertible redeemable preference shares by a company incorporated in England and having a financial standing comparable with that of the Guarantor at the relevant time.

8. Restrictions on Required Conversion and Exchange and Guarantor's Exchange Right

Notwithstanding anything to the contrary contained in these Conditions:—

- (a) neither a Guarantor Exchange Notice nor a Required Conversion Notice may be given if an Event of Default or Potential Event of Default shall have occurred and be continuing, and if an Event of Default or Potential Event of Default shall occur after a Guarantor Exchange Notice or Required Conversion Notice shall have been given and prior to the Required Exchange Date or the Required Conversion Date, as the case may be, then such notice shall automatically be revoked and the relevant exchange or conversion shall not take place;
- (b) neither a Required Conversion Notice nor a Guarantor Exchange Notice may be given specifying a Required Conversion Date or, as the case may be, Required Exchange Date falling during any Conversion Period, and any such notice given shall be invalid and any such notice given during a Conversion Period but specifying a Required Conversion Date or, as the case may be, a Required Exchange Date falling after the expiry of a Conversion Period shall be without prejudice to the exercise of Conversion and Exchange Rights or, as the case may be, Conversion and Redemption Rights during the relevant Conversion Period pursuant to these Conditions; and

- (c) neither a Guarantor Exchange Notice nor a Required Conversion Notice may be given at any time after an offer or scheme (in each case as referred to in Condition 5(b)(ii)) has been announced until such time as such offer shall have been declared unconditional in all respects or shall have lapsed or have been withdrawn or, as the case may be, such scheme shall have been duly adopted or withdrawn or cancelled and any such notice given during any such period, or prior thereto but specifying a Required Exchange Date or, as the case may be, a Required Conversion Date falling during such period, shall be invalid.

As used in these Conditions:--

- (i) "Event of Default" means any of the events specified in paragraphs (i) to (vii) of Condition 16;  
(ii) "Potential Event of Default" means any event or circumstance which with the giving of notice, the lapse of time, the issue of a certificate or the fulfilment of any other condition provided in Condition 16 would constitute an Event of Default.

#### 9. Underwritten Bond Purchase

The Issuer may give notice to the Bondholders at the same time as giving notice to the Bondholders pursuant to Condition 12, stating that it has entered into arrangements to procure the purchase by a third party or third parties of all or up to a stated number of any Bonds in respect of which the Conversion and Redemption Rights may be sought to be exercised pursuant to Condition 13(b) at a price not less than the Issue Price. Such notice shall, subject as provided below, be irrevocable and shall oblige the Issuer to procure each such purchase (and in default thereof itself to purchase) and each Bondholder seeking to exercise Conversion and Redemption Rights in respect of any Bonds pursuant to Condition 13(b) to sell such Bonds to the relevant purchaser without the Bondholder taking any action other than would have been required were the Bonds to have been converted pursuant to Condition 13(b). Bonds purchased pursuant to this Condition shall not be redeemed and converted pursuant to Condition 13(b) notwithstanding that the relevant Bondholder may have sought to exercise Conversion and Redemption Rights in respect thereof.

Any such notice shall also contain details of the price at which such purchase is to be effected, the name of the person or persons who will purchase or underwrite the purchase of the Bonds and details of any circumstances ("Relevant Circumstances") in which, pursuant to the terms of the arrangements, the relevant person or persons may be relieved of their obligations to make such purchase, the basis of selection of Bonds to be purchased if the arrangements may not apply to all relevant Bonds, the aggregate of all fees and expenses payable to such person or persons by the Issuer or Guarantor or any other person in respect of the purchase, the terms of any indemnity, buy back or equivalent arrangements given to or agreed with such person or persons by the Issuer, the Guarantor or any other person and the arrangements in relation to payment of such purchase price to the Bondholders (which arrangements shall be *mutatis mutandis* as provided in Condition 14 and shall be such as to result in no delay in payments to Bondholders).

If, as a result of the occurrence of a Relevant Circumstance, the relevant person or persons shall be relieved of their obligations as aforesaid, or if for any other reason whatsoever, any Bonds are not purchased as contemplated above, then the notice given pursuant to this Condition shall be deemed not to have been given in respect of such Bonds.

#### 10. Underwritten Share Placement

The Guarantor may (subject to any necessary approvals and resolutions of the shareholders of the Guarantor being in force and effect) on and with effect from the Maturity Date deem Share Exchange Rights to have been exercised in respect of all or a stated number of the Preference Shares that will arise pursuant to the exercise of Conversion and Redemption Rights on such date pursuant to Condition 13(a), having entered into arrangements (which arrangements shall be such as to result in no delay in payments to Bondholders) for the Ordinary Shares to be issued to be placed on behalf of or purchased from the relevant Bondholders. The relevant Bondholders shall not be obliged to take any action in respect thereof. The proceeds from such placing or purchase shall be paid in cash by the Guarantor to the relevant Bondholders in the manner provided in Condition 14 up to an amount equal to the amount which would otherwise have been payable on redemption of such Preference Shares so arising and the Guarantor may retain any excess. If such proceeds (net of expenses) are less than such amount, the shortfall shall be paid in cash by the Guarantor to the relevant Bondholders together with such proceeds as a single payment. If for any reason whatsoever any Ordinary Shares are not placed or purchased as provided above, then the notice given pursuant to this Condition shall be deemed not to have been given in respect of the relevant Bonds.

#### 11. Purchases

The Guarantor or any of its subsidiaries (including the Issuer) may, subject to any relevant laws or regulations, at any time purchase Bonds at any price, except that, if the Bonds are then listed on The Stock Exchange, (a) in the case of a purchase by tender, tenders will be available to all the holders of Bonds alike and (b) such price, exclusive of expenses and accrued interest, shall not exceed (i) in the case of a purchase in the open market or by tender (as aforesaid), the average of the middle-market quotations of the Bonds on The Stock Exchange (as derived from The Stock Exchange Daily Official List) for the last 10 dealing days preceding the date of purchase or (if higher), in the case of a purchase in the open market only, the market price on the date of purchase, provided that such market price is not more than 105 per cent. of such average and (ii) in the case of a purchase by private treaty, 120 per cent. of the middle-market quotation of the Bonds on The Stock Exchange (as derived from The Stock Exchange Daily Official List) for the last dealing day preceding the date of purchase.

#### 12. Extension of Maturity

The Issuer shall be entitled, by notice in writing (which shall be irrevocable) given to all the Bondholders at any time while any Bond remains outstanding, from time to time (so that such notice may be given on more than one occasion) to extend the maturity of the Bonds to 15th June in any year after 2005. The date for the time being fixed for the maturity of the Bonds is herein called "the Maturity Date". However, no such notice may be given more than 56 nor less than 28 days prior to the date ("the Current Maturity Date") which is, immediately prior to the giving of such notice, the Maturity Date. In giving any such notice, the Issuer shall be entitled to specify that with effect from the Current Maturity Date interest shall accrue on the Bonds at such rate, which may be greater or less than the rate of interest then in effect, as may have been agreed by a merchant bank in the City of London (selected by the Issuer and approved by the Trustee, such approval not to be unreasonably withheld or delayed) to render the rate of interest payable on the Bonds (taking into account the value of the conversion and exchange rights) with effect from the Current Maturity Date reasonably comparable with then current market rates, and which shall be specified in such notice. In the absence of any such specification, interest shall continue to accrue at the rate in effect immediately prior to the giving of such notice. Such notice shall provide for Bondholders to have the right to notify the Issuer in writing, within the period commencing on the date on which the notice is given and expiring on the date 7 days prior to the Current Maturity Date, that the Bonds to which such notice relates shall not be Bonds in respect of which Conversion and Redemption Rights are to be deemed to have been exercised as of the Current Maturity Date pursuant to Condition 13(b). Any such notice given by a Bondholder shall be irrevocable.

### 13. Conversion and Redemption

#### (a) Deemed Exercise of Conversion and Redemption Rights on Maturity Date

The holder of each outstanding Bond will be deemed to have exercised the right (a "Conversion and Redemption Right") to convert such Bond into a Preference Share on and with effect from the Maturity Date, unless prior thereto Conversion and Exchange Rights, Required Conversion and Exchange Rights or a Guarantor's Exchange Right shall have been exercised (including without limitation Conversion and Exchange Rights exercised by the Trustee pursuant to Condition 5(g)) in respect thereof as provided herein. Upon Conversion and Redemption Rights being so exercised in respect of any Bond, such Bond shall be redeemed on the Maturity Date at its Issue Price and the proceeds of redemption shall be applied in paying up in full the subscription price of 100p of a Preference Share (comprising payment in full of the nominal amount thereof of 1p and the premium on issue thereof of 99p) which shall accordingly be allocated in accordance with the Articles, credited as fully paid. One Preference Share shall be allotted on the exercise of such Rights in respect of each Bond.

Subject to Condition 10, the Preference Shares allotted upon such exercise shall forthwith be redeemed by the Issuer at a price of 100p per Preference Share in accordance with the rights attaching thereto.

#### (b) Conversion and Redemption on Extension of Maturity

If the Issuer shall give notice pursuant to Condition 12, a Bondholder will be deemed to have exercised, as of the Current Maturity Date, the Conversion and Redemption Rights in respect of all or any of the Bonds registered in his name unless on or prior to the date 7 days prior to the Current Maturity Date he shall have notified the Issuer as described in Condition 12 and subject as provided below and to Condition 9 the Preference Shares allotted upon any such conversion shall be redeemed at a price of 100p per Preference Share in accordance with the rights attaching thereto. An exercise of Conversion and Redemption Rights shall be irrevocable.

#### (c) Cancellation

Subject to Condition 9, all Bonds redeemed, converted or purchased shall be cancelled forthwith by or on behalf of the Issuer and may not be re-issued or re-sold.

### 14. Payments

(a) All sums payable in respect of a Bond, whether of amounts payable on redemption of the Bonds or interest or pursuant to Condition 9 or 10 or otherwise) shall be paid by sterling cheque or warrant drawn on a Town Clearing Branch of a bank in the City of London and sent by post addressed to the holder appearing on the Register at the close of business on the seventh day prior to the date on which the relevant payment is due ("the Record Date") at his registered address or, in the case of joint holders, addressed to the holder whose name stands first in the Register in respect of such Bond at his address as appearing in the Register or addressed to such person and at such address as the holder or joint holders may in writing direct. Every cheque or warrant shall, unless the holder or joint holders otherwise direct, be made payable to the order of the holder or, in the case of joint holders, to the order of the holder whose name stands first on the Register, and shall be sent at his or their risk and payment of the cheque or warrant by the bank on which it is drawn shall constitute a good discharge to the Issuer. Any one or two or more joint holders may give effective receipts for any such sum payable in respect of the Bonds held by them. Where a person is entitled by transmission to a Bond, any such sum payable in respect of the Bonds may be paid as if he were a holder of the Bond and his address noted in the Register was his registered address.

(b) No monies payable by the Issuer on or in respect of any Bond shall, save as otherwise provided in the Conditions, bear interest against the Issuer.

(c) Any interest or other sum payable on any Bonds unclaimed after a period of 12 years from the date when it became due for payment shall be forfeited and shall revert to the Issuer and the payment by the Directors of the Issuer of any unclaimed interest or other sum payable on or in respect of a Bond into a separate account shall not constitute the Issuer a trustee in respect of it.

(d) Cheques or warrants shall be despatched not later than the business day preceding the due date for payment. In these Conditions, "business day" means any day on which banks are open for business in the City of London.

### 15. Taxation

All payments of interest in respect of the Bonds will be made subject to the deduction of any United Kingdom income tax required to be withheld at source, but no deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature ("Taxes") imposed or levied by or on behalf of the United Kingdom or the Island of Jersey or any authority therein or thereof having power to tax shall be made in respect of any other payment in respect of the Bonds (whether of redemption monies or pursuant to Condition 9 or 10 or otherwise (other than payments of interest as provided above)) nor shall any withholding or deduction be made for or on account of any Taxes imposed by or on behalf of the Island of Jersey or any authority therein or thereof having power to tax in respect of any payment of interest on the Bonds, unless in any such case the Issuer or, as the case may be, the Guarantor is required by law to deduct or withhold amounts for, or on account of, such Taxes. If any such deduction or withholding is required to be made by law in respect of any such Taxes, the Issuer or, as the case may be, the Guarantor will pay such additional amounts as shall be necessary in order that the net amounts received by the Bondholders after such deduction or withholding shall equal the amounts which would have been receivable in respect of the Bonds in the absence of such deduction or withholding, except that no such additional amounts shall be payable:—

- (i) to, or to a third party on behalf of, a person who is subject to such Taxes, by reason of his being connected with the Island of Jersey or, as the case may be, the United Kingdom otherwise than merely by the holding of the Bond or the receipt of redemption monies or interest or other amounts payable in respect of the relevant Bond;
- (ii) more than 30 days after the Relevant Date, except to the extent that the holder would have been entitled to such additional amounts on presenting his cheque or warrant for payment on the last day of such period of 30 days; or
- (iii) to, or to a third party on behalf of, a holder where such holder has not made, but in respect of whom such withholding or deduction would not have been required had such holder made, a declaration of non-residence or other similar claim for exemption to the relevant tax authority.

In these Conditions, "Relevant Date" means whichever is the later of (i) the date on which the payment becomes due and (ii) the date on which the relevant cheque or warrant for the amount of the payment then due shall have been duly despatched to the relevant Bondholder.

Reference in these Conditions to amounts payable on redemption of the Bonds (however expressed) or to interest or any other amount payable in respect of the Bonds (whether pursuant to Condition 9 or 10 or otherwise) shall be deemed to include any additional amounts which may be payable under the obligations referred to in this Condition or any obligations undertaken in addition thereto or in substitution pursuant to the Trust Deed.

#### 16. Events of Default

Upon the happening of any of the events listed in paragraphs (i) to (vii) of this Condition and the Trustee giving written notice to the Issuer and the Guarantor, the outstanding Bonds shall become immediately due and repayable at an amount equal to the Issue Price together with accrued interest to the date of repayment.

If the event falls within paragraphs (ii) to (vii) no such notice may be given by the Trustee unless the Trustee certifies to the Issuer and the Guarantor that the happening of such event is in its opinion materially prejudicial to the interests of the Bondholders. Subject thereto, the Trustee may, and if so requested in writing by the holders of not less than one-fifth in principal amount of the outstanding Bonds or if so directed by an Extraordinary Resolution of the Bondholders shall, give such notice as aforesaid.

The said events are that:—

- (i) there is default for more than 15 days in the payment of any redemption monies or interest due on or in respect of the Bonds or any of them or any amount payable pursuant to Condition 9 or 10 or of the redemption monies payable on the redemption of the Preference Shares or any of them; or
- (ii) there is default in the performance or observance by the Issuer or the Guarantor of any obligation or provision under the Bonds, the Trust Deed, the Preference Shares, the Articles of the Issuer (insofar as they relate to the Preference Shares) or the Deed Poll (other than any obligation for the payment of any redemption monies or interest on or in respect of the Bonds) which continues for more than 45 days after written notice thereof shall have been given to the Issuer and the Guarantor by the Trustee (except where the Trustee shall have certified to the Issuer and the Guarantor that such default is, in its opinion, incapable of remedy, when no such notice or continuation shall be required); or
- (iii) a resolution is passed, or a final order of a court in Jersey, or as the case may be, the United Kingdom is made, or an order of a court of competent jurisdiction outside Jersey, or as the case may be, the United Kingdom is made and, where possible, not discharged or stayed within a period of 60 days, that the Issuer, or as the case may be, the Guarantor be wound up or dissolved (otherwise than for the purposes of a reconstruction, amalgamation or merger the terms of which have previously been approved in writing by the Trustee); or
- (iv) an encumbrancer takes possession or an administrative or other receiver or similar officer is appointed of the whole or a substantial part of the assets or undertaking of the Issuer or the Guarantor or an administration or similar order is made in relation to the Issuer or the Guarantor and such taking of possession, appointment or order is not released, discharged or cancelled within 60 days; or
- (v) a distress, execution or seizure before judgment is levied or enforced upon or sued out against a substantial part of the assets or undertaking of the Issuer or the Guarantor and is not discharged, dismissed or stayed within 60 days thereof; or
- (vi) the Issuer or the Guarantor stops payment generally or (otherwise than for the purposes of a reconstruction, amalgamation or merger the terms of which have previously been approved in writing by the Trustee) ceases or threatens to cease to carry on all or substantially all of its business or is unable to pay its debts generally as and when they fall due; or
- (vii) the Issuer or the Guarantor makes an assignment for the benefit of creditors generally or admits in writing its inability to pay its debts generally as they become due or takes corporate action in furtherance of any such action.

#### 17. Undertakings

- (a) While any Bond remains outstanding, the Guarantor will, save with the approval of an Extraordinary Resolution or with the approval of the Trustee where, in its opinion, it is not materially prejudicial to the interests of the Bondholders to give such approval:—
  - (i) perform all of its obligations under the Deed Poll;
  - (ii) not make any amendment to the Deed Poll; and
  - (iii) be the legal and beneficial owner of not less than 25 per cent. of the issued and outstanding ordinary share capital of the Issuer.
 

As used in these Conditions, "ordinary share capital" has the meaning ascribed to it in Section 832 of the Income and Corporation Taxes Act 1988 of Great Britain (or any modification or re-enactment thereof).
- (b) Whilst any Bond remains outstanding, the Issuer will, and the Guarantor will procure that the Issuer will, save with the approval of an Extraordinary Resolution or with the approval of the Trustee where, in its opinion, it is not materially prejudicial to the interests of Bondholders to give such approval:—
  - (i) not make any amendment to the Articles of the Issuer which would vary, abrogate or modify the rights of holders of Preference Shares;
  - (ii) keep available for issue free from pre-emptive rights out of its authorised but unissued capital such number of Unclassified Shares (as defined in the Articles of the Issuer) as would enable all the unexercised Conversion and Exchange Rights and/or Conversion and Redemption Rights to be satisfied in full; and
  - (iii) not issue any other share capital with rights which are more favourable than the rights attaching to the Preference Shares as respects dividends or on a return of capital or otherwise.

#### 18. Liquidation of the Guarantor

If an effective resolution is passed on or before the Maturity Date for the winding-up of the Guarantor, then (unless it be for the purpose of a reconstruction, amalgamation, merger or other similar arrangement previously approved by the Trustee or by an Extraordinary Resolution) the Guarantor will forthwith notify Bondholders that such a resolution has been passed and that the holder of a Bond shall be entitled at any time within three months after the date on which such notice is published to elect by notice in writing delivered to the Guarantor to be treated as if he had, immediately before the date of the passing of such resolution, exercised the Conversion and Exchange Rights in respect of some or all (as specified in such notice) of the Bonds held by him and he shall be entitled to receive, out of the assets which would otherwise be available in the liquidation to the holders of Ordinary Shares, such a sum, if any, as he would have received had he been the holder of the Ordinary Shares to which he would have become entitled by virtue of such exercise.

#### 19. Meetings of Bondholders, modification, substitution, waiver and indemnification

The Trust Deed will contain provisions for convening meetings of Bondholders to consider any matter affecting their interests, including the modification by Extraordinary Resolution (as defined in the Trust Deed) of these Conditions or the provisions of the Trust Deed. The quorum at any such meeting for passing an Extraordinary Resolution will be two or more persons holding or representing a clear majority in principal amount of the Bonds for the time being outstanding, or at any adjourned meeting two or more persons being or representing Bondholders whatever the principal amount of the Bonds so held or represented, except that at any meeting the business of which includes the modification of certain of these Conditions and the provisions of the Trust Deed (including without limitation those relating to status and subordination, Conversion and Exchange Rights, Conversion and Redemption Rights, Required Conversion and Exchange Rights and Guarantor's Exchange Rights and the currency, amount and due date of payment of redemption monies and interest or other amounts in respect of the Bonds) the necessary quorum for passing an Extraordinary Resolution will be two or more persons holding or representing not less than two-thirds, or at any adjourned such meeting not less than one-third, of the principal amount of the Bonds for the time being outstanding. An Extraordinary Resolution passed at any meeting of Bondholders will be binding on all Bondholders, whether or not they are present at the meeting.

The Trustee may agree, without the consent of Bondholders, to any modification (except as aforesaid) of, or the waiver or authorisation of any breach or proposed breach of, any of these Conditions or any of the provisions of the Trust Deed which is not, in the opinion of the Trustee, materially prejudicial to the interests of the Bondholders or to any modification which is of a formal, minor or technical nature or which is made to correct a manifest error.

The Trust Deed contains provisions permitting the Trustee to agree, subject to such amendment of the Trust Deed and such conditions as the Trustee may require which may include the giving of a guarantee, but without the consent of Bondholders, to the substitution of any other company in place of the Issuer, or of any previous substituted company, as principal debtor under the Trust Deed and the Bonds. In the case of any such substitution the Trustee may agree, without such consent, to a change of the law governing the Bonds and/or the Trust Deed provided that such change would not in the opinion of the Trustee be materially prejudicial to the interests of the Bondholders.

In connection with the exercise of its powers, trusts, authorities or discretions (including but not limited to those in relation to any proposed modification, waiver, authorisation or substitution as aforesaid) the Trustee shall not have regard to the consequences of such exercise for individual Bondholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory and the Trustee shall not be entitled to require, nor shall any Bondholder be entitled to claim from the Issuer or the Guarantor any indemnification or payment in respect of any tax consequence of any such exercise upon individual Bondholders except to the extent provided for in Condition 15 and/or in any undertakings given in addition thereto or in substitution therefor pursuant to the Trust Deed.

Any such modification, waiver or authorisation shall be binding on all Bondholders and, unless the Trustee agrees otherwise, any such modification or substitution shall be notified to Bondholders as soon as practicable thereafter.

The Trust Deed will contain provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking proceedings against the Issuer and/or the Guarantor, unless indemnified to its satisfaction.

#### 20. Replacement of Bonds

Should any Bond be lost, stolen, destroyed, mutilated or defaced, it may be replaced at the specified office of the Registrar upon payment by the claimant of the expenses incurred in connection therewith and on such terms as to evidence and indemnity as the Issuer may require. Mutilated or defaced Bonds must be surrendered before replacements will be issued.

#### 21. Notification of rights

The Issuer or the Guarantor shall give to the Bondholders notice in writing not less than 28 days nor more than 56 days prior to each Annual Conversion Date informing them of their entitlement to exercise their Conversion and Exchange Rights.

If the Issuer does not by 28 days prior to the Current Maturity Date give a notice pursuant to Condition 12 it shall by not later than such twenty-eighth day give notice to the Bondholders informing them of their entitlement to exercise their Conversion and Exchange Rights.

Any notice given pursuant to Condition 5(b)(ii) or 12 shall contain a statement informing Bondholders of their entitlement to exercise their Conversion and Exchange Rights (and, in the case of Condition 12, their Conversion and Redemption Rights). Any notice given pursuant to Condition 18 shall contain a statement informing Bondholders of their right to make the election therein referred to.

Any such notice as aforesaid shall give the names and addresses of the Registrar.

If the Issuer shall from time to time prescribe a form of Conversion and Exchange Notice or Nationality Declaration different from that set out on the reverse of the Bonds, the Issuer shall forthwith notify Bondholders and such notification shall be accompanied by a copy of the Conversion and Exchange Notice or Nationality Declaration so prescribed.

**22. Notices**

All notices to Bondholders shall be given in writing and shall be valid if posted to the Bondholders at their respective addresses in the Register or in such other manner as may be approved by the Trustee for this purpose. Such notices will be deemed to have been given on the date of such posting.

**23. Registrar**

In acting under the Registrar's Agreement, the Registrar will be acting solely as agent of the Issuer and the Guarantor and will not assume any obligation or duty to, or any relationship of agency or trust for or with, the Bondholders. The Registrar's Agreement will contain provisions indemnifying the Registrar and absolving it from responsibility in connection with certain matters. The name of the initial Registrar is set out at the end of this document. The Issuer may at any time remove the Registrar or appoint a new Registrar, provided that it will at all times maintain a Registrar. Notice of any such removal (other than in the case of insolvency, when it shall take immediate effect) or appointment and of any change in the specified office of the Registrar will be given to Bondholders not less than 30 days prior to such removal, appointment or change taking effect. The Registrar's Agreement, with the consent of the Trustee, may be amended by the Issuer and the Guarantor, without the consent of Bondholders if in the opinion of the Trustee, the amendment is (i) not materially prejudicial to the interests of the Bondholders; or (ii) to correct a manifest error or an error of a formal, minor or technical nature.

**24. Governing law**

The Trust Deed and the Bonds will be governed by English law.

**B. DESCRIPTION OF THE PREFERENCE SHARES**

The terms of the Preference Shares will be contained in the Articles of the Issuer. The Preference Shares will also have the benefit of the Deed Poll. The holders of the Preference Shares ("the Preference Shareholders") will be entitled to the benefit of, will be bound by, and will be deemed to have notice of, all the provisions of the Articles of the Issuer and the Deed Poll.

The Preference Shares will be issued upon conversion of the Bonds as described in "Conditions of the Bonds". Words and expressions defined in "Conditions of the Bonds" have the same meaning in this Description of the Preference Shares, unless the context otherwise requires and references in this Description of the Preference Shares to Conditions, or to particular Conditions, are to "the Conditions of the Bonds" above, or to particular numbered Conditions therein, as the context may require.

The Articles of the Issuer will contain provisions to the following effect:—

**1. Share capital**

- (a) The authorised share capital of the Issuer will be £3,251,000 divided into 1,000 Founders' Shares of £1 each and 325,000,000 Unclassified Shares of 1p each.
- (b) The Directors may, subject as provided in the Articles, issue any of the Unclassified Shares as Preference Shares of 1p each or Nominal Shares of 1p each.

**2. Founders' Shares**

Founders' Shares shall only be issued to or for the benefit of the Guarantor or of a person previously approved in writing by the Guarantor.

**3. Nominal Shares**

Nominal Shares shall only be issued to or for the benefit of the Guarantor for the purposes of providing funds for the redemption of the Preference Shares.

**4. Preference Shares**

Preference Shares shall only be issued on conversion of Bonds pursuant to the Conditions and the terms of the Trust Deed and shall be issued at a price, credited as fully paid, of 100p per Share ("the Paid-up Value") comprising payment in full of the nominal value thereof and the premium on issue thereof of 99p.

**5. Income**

- (a) No dividends shall be paid on the Preference Shares.
- (b) If payment of the redemption monies on the Preference Shares is improperly withheld or refused or default is otherwise made in the payment thereof, default interest at the rate of 9¾ per cent. per annum will accrue (as well after as before any judgment of a competent court) on the amount due for payment up to but excluding the date on which payment in full of the redemption monies in respect thereof is made. The amount of any such default interest accruing in respect of a period shall be calculated on the basis of 365-day year and the number of days elapsed.
- (c) The Preference Shares shall not confer any right of participation in the profits of the Issuer.
- (d) No dividends shall be paid on the Nominal Shares.

**6. Capital**

On a return of capital on liquidation or otherwise, the assets of the Issuer available for distribution shall be applied in the following priority:

- (i) first, in paying to the holder of each Preference Share the Paid-up Value thereof together with a sum equal to any arrears or any accruals of any default interest payable pursuant to Clause 5(b);
- (ii) secondly, in paying to the holder of each Nominal Share the nominal amount paid up thereon;
- (iii) thirdly, in paying to the holder of each Founders' Share an amount equal to the nominal amount paid up thereon plus £1,000,000;

and any surplus of assets then remaining shall be distributed *pari passu* in proportion to the amounts paid up on the Founders' Shares and the Preference Shares among the holders of the Founders' Shares and the Preference Shares.

## 7. Redemption

- (a) Subject to Clause 8 the Issuer shall redeem all the Preference Shares for cash at their Paid-up Value forthwith upon their allotment, save that where Clause 10(a) applies any Preference Share in respect of which the Share Exchange Right has been exercised or is deemed to be exercised shall not be redeemed pursuant to the foregoing but shall be redeemed at any time after the first transfer of the same on any date specified by the holder for the time being in any notice given by the holder to the Issuer requiring such redemption at a date not less than 28 days after the date of such notice.
- (b) On redemption of a Preference Share, the Issuer will cancel the Preference Share and any Preference Shares Certificate relating thereto and such Preference Share may not be re-issued or re-sold but shall be available as an Unclassified Share for issue as a Nominal Share.
- (c) The obligations of the Issuer to redeem Preference Shares as referred to above are subject to applicable law in the Island of Jersey. However, the Guarantor will (as referred to in more detail in "Description of the Deed Poll" below) guarantee on a subordinated basis all amounts payable in respect of Preference Shares on the due date regardless of whether payment thereof by the Issuer is prohibited by law and will also indemnify any Bondholder in respect of any losses which may be suffered or incurred by it arising, directly or indirectly, from the inability or failure of the Issuer to issue Preference Shares pursuant to the Conditions.

## 8. Share Exchange Rights

- (a) If Conversion and Exchange Rights are exercised pursuant to the Bonds or in the event of a Required Conversion and Exchange, the right ("the Share Exchange Right") to exchange Preference Shares arising on conversion of the Bonds pursuant to the Conditions of the Bonds for fully paid registered Ordinary Shares shall be deemed to have been exercised and the Issuer shall procure that such Preference Shares are exchanged for Ordinary Shares as aforesaid on the relevant Conversion Date in accordance with the following provisions (without any further action being required to be taken by any Bondholder).
- (b) The number of Ordinary Shares to be issued on exercise of a Share Exchange Right shall be determined by dividing the Paid-up Value of the relevant Preference Share by the Exchange Rate in effect as at the relevant Conversion Date. The initial exchange rate shall be: for every 2.43 preference shares so exchanged, one British Airways Ordinary Share, subject to adjustments in the circumstances described below and as set out in the Articles of the Issuer. Fractions of Ordinary Shares will not be issued on exchange and no cash adjustment will be made. However, if Share Exchange Rights in respect of more than one Preference Share shall be exercised at any time by a Bondholder and the Ordinary Shares arising on exchange of the relevant Preference Shares are to be registered in the same name, the number of Ordinary Shares to be issued in respect thereof shall be calculated on the basis of the aggregate Paid-up Value of such Preference Shares. Where Conversion and Exchange Rights are exercised by the Trustee or are deemed to be exercised pursuant to Condition 10 or pursuant to a Required Conversion and Exchange, all the relevant Bonds and Preference Shares shall, for the purpose of the immediately preceding sentence, be deemed to be held by one person. Ordinary Shares arising on exchange will be allotted as of the relevant Conversion Date in the name of the holder of the relevant Preference Share or his nominee save that where Share Exchange Rights are deemed to be exercised pursuant to Condition 10 they shall be allotted in the name of a nominee, selected by the Guarantor, for the relevant Bondholders and where they are exercised by the Trustee they shall be allotted to the Trustee (or as the Trustee may direct) on behalf of the relevant Bondholders.
- (c) The Exchange Rate will be subject to adjustment in any of the following circumstances:—
- any alteration of the nominal value of the Ordinary Shares as a result of consolidation or sub-division;
  - the making of any offer or invitation by way of rights or otherwise (not being an offer to which Condition 5(b)(ii) applies) to the holders of the relevant share capital of the Guarantor (as defined in Section 94 of the Companies Act 1985 of the United Kingdom);
  - the issue of Ordinary Shares credited as fully paid to the holders of Ordinary Shares ("the Ordinary Shareholders") by way of capitalisation of profits or reserves (including any share premium account or capital redemption reserve), except that no adjustment shall be made in the event of an issue of Ordinary Shares by way of capitalisation of profits or reserves at the option of an Ordinary Shareholder in lieu of a cash dividend;
  - the making of any capital distribution by the Guarantor to its Ordinary Shareholders, except where the Exchange Rate falls to be adjusted under (iii) above. For the purposes of this paragraph (iv), "capital distribution" means any dividend or other distribution of capital profits (whether realised or not) or capital reserves, or profits or reserves arising after the date of the issue of the Bonds from a distribution of capital profits (whether realised or not) or capital reserves by a subsidiary, except by means of a capitalisation issue or any repayment of capital or purchase of the Guarantor's own shares (other than a redemption or purchase of redeemable shares in accordance with the terms of issue thereof); for the purpose of this paragraph (iv), insofar as the relevant audited accounts do not distinguish between capital and revenue profits or reserves the Guarantor shall be entitled to rely upon a written estimate by the Auditors of the Guarantor for the time being as to the extent to which any part of any profit or reserve should be regarded as of a capital nature, and in any case where the Guarantor shall purchase its shares, the amount of the capital distribution per Ordinary Share shall be that amount which is the gross amount paid on such purchase divided by the number of Ordinary Shares remaining in issue following such purchase.
- (d) Upon any exercise of Conversion and Exchange Rights pursuant to Condition 5(b)(ii), the Exchange Rate shall be as set out below but in each case adjusted, if appropriate, under the foregoing provisions of this paragraph:—
- | Conversion Date                                  | Exchange Rate |
|--|---------------|
| On or before 14th June, 1990                     | 2.16          |
| Thereafter, but on or before 14th December, 1990 | 2.21          |
| Thereafter, but on or before 14th June, 1991     | 2.25          |
| Thereafter, but on or before 14th December, 1991 | 2.28          |
| Thereafter, but on or before 14th June, 1992     | 2.32          |
| Thereafter, but on or before 14th December, 1992 | 2.36          |
| Thereafter, but on or before 14th June, 1993     | 2.39          |
- (e) If any doubt shall arise as to the appropriate adjustment to the Exchange Rate the certificate of the Auditors of the Guarantor for the time being shall be conclusive and binding on all concerned. No adjustment will be made to the

Exchange Rate where such adjustment would be less than one per cent. of the Exchange Rate then applicable. Any adjustment not required to be made and any amount by which the Exchange Rate has been rounded down will be carried forward and taken into account in any subsequent adjustment. Bondholders will be given notice of all adjustments in accordance with Condition 22 and all adjustments will be made in accordance with the provisions contained in the Articles of the Issuer.

The Exchange Rate shall not be reduced so as to require the allotment of Ordinary Shares at below the par value of the Ordinary Shares.

- (f) Ordinary Shares allotted on exchange will be issued as of the relevant Conversion Date and will be fully paid and rank *pari passu* with the fully paid Ordinary Shares in issue on such Conversion Date.
- (g) On the exercise of Share Exchange Rights pursuant to an exercise of Conversion and Exchange Rights by or on behalf of a Bondholder, such Bondholder must pay all taxes and stamp, issue and registration duties (if any) arising in respect thereof (other than any taxes or capital or stamp duties or stamp duty reserve tax payable in the United Kingdom or the Island of Jersey in respect of the issue of Ordinary Shares on such exercise or on any transfer of the Preference Shares to the Guarantor, which shall be payable by the Guarantor) and such Bondholder must pay all if any taxes arising by reference to any disposal or deemed disposal of a Bond or Preference Share in connection with such exercise. Neither the Issuer nor the Guarantor nor any of their respective agents will impose any charge on exchange of Preference Shares.
- (h) Certificates for Ordinary Shares issued on exchange will be despatched free of charge (but uninsured and at the risk of the holder or the person entitled thereto) within one month after the Conversion Date.

#### 9. Voting and general meetings

- (a) Founders' Shares, Nominal Shares and Preference Shares shall entitle the holders thereof to receive notice of and to attend and vote at every general meeting of the Issuer.
- (b) Whenever the holders of Shares are entitled to vote at a general meeting of the Issuer, on a show of hands every holder thereof who (being an individual) is present in person or (being a corporation) is present by representative shall have one vote and on a poll every holder thereof who is present in person or by proxy shall have one vote in respect of each Share registered in the name of such holder.

#### 10. Transfers

- (a) Any Preference Share in respect of which the Share Exchange Right has been or is deemed to be exercised shall forthwith upon allotment of the same be transferred to the Guarantor in exchange for the issue to the holder thereof of that number of fully paid Ordinary Shares to which he is entitled upon exercise of the Share Exchange Right. Any such transfer shall be effected by the Issuer as agent for the holder thereof and the Issuer shall be authorised by such holder to execute all such documents and do all such things as may be necessary properly to effect the same, without any cost or liability to, or any further action required by, the holder.
- (b) Transfers of Preference Shares shall be effected by any transfer in common or usual form or such other form as may be approved by the Board of the Issuer.

#### 11. Payments

- (a) The provisions set out in Condition 14 shall apply, *mutatis mutandis*, to any payment made or to be made on or with respect to the Preference Shares.
- (b) All payments in respect of the Preference Shares will be made without deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the Island of Jersey or the United Kingdom or any authority thereof or therein having power to tax unless the Issuer is required by law to deduct or withhold amounts for, or on account of, such taxes, duties, assessments or charges. In such event, the Issuer will pay such additional amounts as shall be necessary in order that the net amounts received by the Preference Shareholders after such deduction or withholding shall equal the amounts which would have been receivable in respect of the Preference Shares in the absence of such deduction or withholding, except that no such additional amounts shall be payable:—
  - (i) to, or to a third party on behalf of, a Preference Shareholder who is subject to such taxes, duties, assessments or charges by reason of his being connected with the Island of Jersey or, as the case may be, the United Kingdom otherwise than merely by the holding of such Preference Shares or the receipt of payments in respect of such Preference Shares;
  - (ii) more than 30 days after the Relevant Date, except to the extent that the holder would have been entitled to such additional payments on presenting his cheque or warrant for payment on the last day of such period of 30 days; or
  - (iii) to, or to a third party on behalf of, a Preference Shareholder where such holder has not made, but in respect of whom such withholding or deduction would not have been required had such holder made, a declaration of non-residence or other similar claim for exemption to the relevant tax authority.

Any reference in this Description of the Preference Shares to any amounts or monies payable on or in respect of the redemption of the Preference Shares shall be deemed also to refer to any additional amounts which may be payable under this provision.

#### 12. Variation of rights

- (a) Subject to the provisions of the Companies (Jersey) Laws, 1861 to 1968, all or any of the rights for the time being attached to any class of Shares for the time being issued may from time to time (whether or not the Issuer is being wound up) be varied with the consent in writing of the holders of not less than three-fourths in nominal value of the issued Shares of that class or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of those Shares. All the provisions of the Articles as to general meeting of the Issuer shall *mutatis mutandis* apply to any such separate general meeting, but so that the necessary quorum shall be two persons holding or representing by proxy not less than one-third in nominal value of the issued Shares of the class, that every holder of Shares of the class shall be entitled on a poll to one vote for every Share of the class held by him, that any holder of

Shares of the class present in person or by proxy may demand a poll and that at any adjourned meeting of the holders one holder present in person or by proxy (whatever the number of Shares held by him) shall be a quorum.

- (b) Subject to certain exceptions, the rights conferred upon the holders of the Shares of any class issued with preferred or other rights shall not unless otherwise expressly provided by the terms of issue of the Shares of that class, be deemed to be varied by the creation or issue of further Shares ranking *pari passu* therewith.

### C. DESCRIPTION OF THE DEED POLL

The Deed Poll will contain provisions to the following effect:—

#### 1. Subordinated Guarantee

- (a) The Guarantor will unconditionally and irrevocably undertake to pay (subject as provided below) all redemption monies, default interest and other amounts expressed to be payable in respect of the Preference Shares to the extent that they are not paid by the Issuer on the due date regardless of whether (i) the profits of the Issuer justify the relevant payment of any dividend, (ii) the relevant amounts shall be available for distribution or payment by the Issuer, (iii) payment thereof shall have been declared or approved by or on behalf of the Issuer or the Issuer in general meeting or (iv) the payment thereof by the Issuer shall be prohibited by law. The Guarantor will also unconditionally and irrevocably indemnify Bondholders in respect of any losses which may be suffered or incurred as a result (directly or indirectly) of any inability or failure by the Issuer or the Guarantor duly to comply with their respective obligations with respect to the exercise of Conversion and Exchange Rights or Conversion and Redemption Rights in relation to the Bonds, the issue of Preference Shares or the exchange of Preference Shares for Ordinary Shares pursuant to the exercise of Share Exchange Rights. Such obligations will constitute direct and unsecured obligations of the Guarantor, subordinated in accordance with Clause 1(b).
- (b) If an order is made or an effective resolution is passed for the winding-up of the Guarantor, the Guarantor shall, to the extent required to make payment under its guarantee or indemnity referred to in Clause 1(a) make payment under such guarantee or, as the case may be, such indemnity only of such amounts as would have been payable if the holders of the outstanding Preference Shares or, as the case may be, the outstanding Bonds had, on the day preceding the commencement of the winding-up, become holders of shares in the Guarantor of a class having a right to receive (*pari passu* with the holders of any other class or classes of securities which following the issue of the Bonds may be issued by the Guarantor or any subsidiary of the Guarantor with the benefit of a guarantee of the Guarantor subordinated on a similar basis) in a winding-up of the Guarantor (in priority to the holders of all other classes of shares in the Guarantor, issued or to be issued), (in the case of a payment under such guarantee) an amount equal to the redemption monies, dividends and other amounts expressed to be payable in respect of the Preference Shares to the date of commencement of winding-up or (in the case of a payment under such indemnity) an amount equal to the amount payable pursuant to such indemnity.

#### 2. Undertakings by the Guarantor

Whilst any Bond remains outstanding, the Guarantor will, save with the consent of an Extraordinary Resolution (as defined in the Trust Deed):—

- (a) ensure that such number of Ordinary Shares as are required at any particular time to enable the Share Exchange Rights and all other rights of conversion into, subscription for and exchange into Ordinary Shares exercisable at that time to be satisfied are kept available for issue free from pre-emptive rights out of its authorised but unissued share capital;
- (b) not make any reduction of share capital, share premium account or capital redemption reserve involving the repayment of money to shareholders (other than to shareholders having the right on a winding-up to a return of capital in priority to the holders of Ordinary Shares) or reduce any uncalled liability in respect thereof unless the same results (or would, but for the fact that the adjustment would be less than one per cent., result) in an adjustment of the Exchange Rate in accordance with the terms of the Preference Shares or the same results from any redemption or purchase by the Guarantor of its own share capital (including Ordinary Shares) or any part thereof;
- (c) not issue or pay up any securities by way of capitalisation of profits or reserves, other than (i) by the issue of fully paid Ordinary Shares to shareholders and other persons entitled thereto; (ii) by the issue of Ordinary Shares paid up in full out of distributable profits or reserves and issued for full consideration in lieu of a cash dividend; or (iii) by the issue of fully paid equity share capital (other than Ordinary Shares) to the holders of such equity share capital and other persons entitled thereto;
- (d) not modify the rights attaching to the Ordinary Shares or issue any other equity share capital (other than Equivalent Preference Shares, as defined in paragraph 4 below) with rights which are more favourable than the rights attaching to the Ordinary Shares, but so that nothing in this provision shall prevent (i) the issue of any equity share capital to employees (including Directors holding executive office) of the Guarantor or any of its subsidiaries or associated companies by the virtue of their office or employment pursuant to any scheme or plan now in existence or which may in the future be approved by the Guarantor in general meetings; (ii) any consolidation or sub-division of the Ordinary Shares or the conversion of any Ordinary Shares into stock or vice versa; (iii) any modification to the rights attached to the Ordinary Shares which is not, in the opinion of a merchant bank in the City of London, selected by the Guarantor, approved by the Trustee (such approval not to be unreasonably withheld or delayed) and acting as an expert, materially prejudicial to the interests of the holders of the Preference Shares;
- (e) procure that no securities (whether issued by the Guarantor or otherwise procured by the Guarantor to be issued) issued without rights to convert into or exchange for Ordinary Shares shall subsequently be granted such rights and that at no time shall there be in issue Ordinary Shares of differing nominal values;
- (f) not take any action which would result in any adjustment of the Exchange Rate if, after giving effect thereto, the Exchange Rate would be decreased to such an extent that Ordinary Shares to be issued on exercise of Share Exchange Rights would fall to be issued below their par value or otherwise could not, under any applicable law then in effect, be legally issued as fully paid;
- (g) if any offer is made to all holders of Ordinary Shares (or all such holders other than the offeror and/or any associates of the offeror (as defined in Section 430 (E)(4) of the Companies Act 1985 of Great Britain)) to acquire the whole or any part of the issued ordinary share capital of the Guarantor, or if any person proposes a scheme with regard to such acquisition, give notice of such offer to the Bondholders at the same time as any notice thereof is sent to its shareholders (or as soon as practicable thereafter) that details concerning such offer may be obtained from the specified office of the Registrar and use its reasonable endeavours to procure that a like offer or scheme is extended to the holders of any Ordinary Shares issued on exercise of Conversion and Exchange Rights or Required Conversion and Exchange Rights during the life of the offer or scheme;

- (h) whilst any Bond remains outstanding, procure that no amendments (other than any amendments of a formal, minor or technical nature or which are made to correct manifest errors) shall be made to the provisions of the Articles of the Issuer relating to the Preference Shares (directly or indirectly) without the approval of the Trustee or the sanction of an Extraordinary Resolution of Bondholders;
- (i) own directly a majority of the Founders' Shares in issue and subscribe such Nominal Shares as are necessary from time to time to provide the Issuer with such amounts as may be necessary to enable the Issuer to redeem the Preference Shares which are from time to time to be redeemed;
- (j) use its best endeavours to ensure that the Ordinary Shares issued upon exchange of any Preference Shares and (if required by The Stock Exchange) the Preference Shares will be admitted to the Official List by the Council of The Stock Exchange and any other stock exchange or securities market on which the Ordinary Shares and, if applicable, the Preference Shares may then be listed or dealt in; and
- (k) procure the fulfilment of all the Issuer's obligations with respect to the Share Exchange Rights, and upon the first exercise (or deemed exercise) of any Share Exchange Right will issue to the holders of any Founders' Shares not then owned by the Guarantor one fully paid Ordinary Share in exchange for each such Founders' Share then tendered and transferred to the Guarantor.

In this Clause, "equity share capital" has the meaning ascribed to it in Section 744 of the Companies Act 1985 of Great Britain (or any modification or re-enactment thereof).

### 3. Payments

- (a) The provisions set out in Condition 14 shall apply, *mutatis mutandis*, to any payment made or to be made pursuant to the provisions of the Deed Poll.
- (b) All payments pursuant to the Deed Poll will be made without deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the United Kingdom or any authority thereof or therein having power to tax unless the Guarantor is required by law to deduct or withhold amounts for, or on account of, such taxes, duties, assessments or charges. In such event, the Guarantor will pay such additional amounts as shall be necessary in order that the net amounts received by the Preference Shareholders or, as the case may be, the Bondholders after such deduction or withholding shall equal the amounts which would have been receivable in the absence of such deductions or withholding, except that no such additional amounts shall be payable in respect of any amounts payable on or with respect to a Preference Share:—
  - (i) to, or to a third party on behalf of, a Preference Shareholder who is subject to such taxes, duties, assessments or charges by reason of his being connected with the United Kingdom otherwise than merely by the holding of such Preference Shares or the receipt of payments in respect of such Preference Shares;
  - (ii) more than 30 days after the Relevant Date, except to the extent that the holder would have been entitled to such additional amounts on presenting his cheque or warrant for payment on the last day of such period of 30 days; or
  - (iii) to, or to a third party on behalf of, a Preference Shareholder where such holder has not made, but in respect of whom such withholding or deduction would not have been required had such holder made, a declaration of non-residence or other similar claim for exemption to the relevant tax authority.

Any reference in this Description of the Deed Poll to any amounts or monies payable pursuant to the Deed Poll shall be deemed also to refer to any additional amounts which may be payable under this provision.

### 4. Further Issues

The Guarantor may from time to time create and issue preference shares ("Equivalent Preference Shares") which would, if Guarantor Preference Shares had been in issue at the relevant time, rank as regards participation in the profits and assets of the Guarantor *pari passu* with but not in priority to the Guarantor Preference Shares except that:—

- (a) the rate of dividend (which may be cumulative or non-cumulative) may differ;
- (b) the Equivalent Preference Shares may rank for dividend as from such date as may be provided by the terms of issue thereof and the dates for payment of dividend may differ;
- (c) a premium may be payable on a return of capital or there may be no such premium; and
- (d) the Equivalent Preference Shares may be redeemable and/or convertible into Ordinary Shares on such terms and conditions as may be prescribed by the terms of the issue thereof and/or the Articles of the Guarantor for the time being or may not be so redeemable and/or so convertible.

### 5. Meetings of Preference Shareholders; Modification of rights

The Deed Poll contains provisions similar to those of the Trust Deed for convening meetings of Bondholders to consider any matter affecting their interests thereunder, including the modification or abrogation of any right arising under the Deed Poll.

The Deed Poll may be amended by the Guarantor without the consent of the Bondholders if, in the reasonable opinion of a merchant bank in the City of London, selected by the Guarantor, the amendment is (i) not materially prejudicial to the interests of the Bondholders (in which event, notice of the change will be given to Bondholders) or (ii) to correct a manifest error or an error of a formal, minor or technical nature. In forming such opinion, such merchant bank shall not be bound to take into account the individual tax circumstances or residence of any Bondholder.

### 6. Governing Law

The Deed Poll will be governed by English law.

## APPENDIX 5

### ADDITIONAL INFORMATION

#### 1. Responsibility

The Directors of the Company, whose names appear below, accept responsibility for the information contained in this document. The only responsibility accepted by the Directors in respect of information relating to UAL has been to ensure that it has been correctly and fairly reproduced or presented from published information. Subject as aforesaid, to the best of the knowledge and belief of the Directors (who have taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

#### 2. Directors of British Airways

The Directors of British Airways and their responsibilities are as follows:—

Lord King of Wartnaby (*Chairman*)  
Sir Colin Marshall (*Deputy Chairman and Chief Executive*)  
D. M. Stevens (*Chief Financial Officer*)  
M. R. Angus (*Deputy Chairman*)  
A. M. Davies  
J. W. Jessop  
Sir Francis Kennedy  
H. U. A. Lambert  
Hon. Charles Price II

all of Speedbird House, Heathrow Airport (London), Hounslow TW6 2JA.

#### 3. Share capital of British Airways

(a) (i) As at the date of this document, the authorised share capital of the Company is £267,000,000 comprising 1,068,900,000 Ordinary shares of 25p each, of which 720,484,536 have been issued fully paid and 347,516,973 remain authorised but unissued. Of this number, 131,775,863 have been reserved to provide for conversion and exchange of the Bonds and the Preference shares.

(ii) As at the date of this document, options to subscribe for Ordinary shares are outstanding under the Company's share option schemes as follows:—

	Numbers of shares	Subscription prices per share (p)	Dates first normally exercisable
Savings related share option scheme	42,757,139	135-161	1992
US employee share purchase plan	795,400	202	1992
Executive share option scheme	13,659,680	150-210	1990
US executive share option plan	492,490	150-225	1990

Save as disclosed, no share or loan capital of any member of the Group is under option or is agreed conditionally to be put under option.

- (b) Application has been made to the Council of The Stock Exchange for the Bonds to be admitted to the Official List. It is expected that listing will become effective and dealings in the Bonds are expected to commence, nil paid, on 2nd October, 1989. No application will be made for the Bonds to be listed on any other stock exchange. Dealings in the new British Airways shares issued on conversion and exchange are expected to commence, fully paid, on the first business day after the relevant Conversion Date. Neither the Bonds nor the new British Airways shares have been or are available to the public in whole or in part except on the terms of the rights issue.
- (c) The provisions of Section 89(1) of the Companies Act 1985 (which, to the extent not disapplied pursuant to Section 95 of that Act, confer on shareholders rights of pre-emption in respect of the allotment of equity securities (within the meaning of Section 94 of that Act) which are, or are to be, paid up in cash) will apply to the new British Airways shares.
- (d) The Directors are at present generally and unconditionally authorised to allot relevant securities (as defined in Section 80(2) of the Companies Act 1985) up to a maximum nominal amount of £60,000,000 at any time up to the date of the next Annual General Meeting or 17th October, 1990, whichever is the earlier.
- (e) By a special resolution passed at the Annual General Meeting held on 17th July, 1989 the pre-emption rights contained in Section 89(1) of the Companies Act 1985 were disapplied and the Directors were empowered to allot equity securities (as defined in Section 94 of that Act) for cash in connection with a rights issue up to a maximum nominal amount of £60 million; and otherwise than on a rights issue up to a maximum nominal amount of £9 million, in each case at any time up to the date of the next Annual General Meeting or 17th October, 1990, whichever is the earlier.
- (f) The provisional allotment letters representing the right to the Bonds will be temporary documents of title and will be renounceable until 3.00 pm on the last date for acceptance and payment, expected to be 21 days after the date of posting of the provisional allotment letters. Thereafter the Bonds will be in registered form transferable by instrument in writing in the usual common form or in such other form as the issuer shall from time to time approve. Certificates in respect of the Bonds will be issued within 42 days after payment.

(g) The Articles of Association of British Airways contain the following provisions relating to the Ordinary shares for which the Preference shares will be exchangeable:—

- (i) **Transfer of shares and registration declaration:** The British Airways shares are in registered form, Shares are transferable by an instrument of transfer in the usual form or in any other form which the Directors may approve. The Directors may, in their absolute discretion and without assigning any reason therefor, decline to register any transfer of any share which is not a fully paid share. Save as referred to in (iii) below and subject to the furnishing of a registration declaration as described below, there is no restriction on the registration of a duly stamped transfer of fully paid shares provided the transfer (a) is lodged at the transfer office or such other place as the Directors may appoint, accompanied by the relevant share certificate and such other evidence of ownership as the Directors may require; (b) is only in respect of one class of share; and (c) is in favour of not more than four transferees. If any of the above conditions are not complied with, the Directors have a discretion whether or not to register the transfer in question.

Except in respect of any shares issued under a capitalisation issue, the Directors shall not register any person other than a Stock Exchange Nominee or a Depository (defined in the Articles to mean a custodian or other person appointed under contractual arrangements with the Company (or a nominee for such custodian or other person) for the purpose of issuing depository receipts in respect of shares of the Company) as a shareholder unless he has furnished a signed declaration stating (a) the name and nationality of any person who has an Interest (as defined in (iii) below) in any such share and (if such declaration or the Directors so require) the nature and extent of such Interest or (b) such other information as the Directors may determine. The Directors may require any such person to provide such evidence or information as to the matters referred to in the declaration as they think fit.

- (ii) **Disclosure of interests:** The Directors may by a Disclosure Notice require any member or other person appearing to be or to have been interested in Ordinary shares to disclose such information as the Directors shall require relating to the ownership of or Interests in the shares in question. If any member or person appearing to have an Interest in any shares fails to give to the Company, within 28 days of the service on him of a Disclosure Notice, the information required, the registered holder of those shares shall not be entitled to attend or vote at any general meeting of the Company or any meeting of holders of any class of shares of the Company.

- (iii) **Restrictions on ownership of shares:** For the purpose of ensuring that, so long as any operating rights or status as an airline of the Company or any subsidiary are conditional on the Company being to any degree owned or controlled by United Kingdom nationals, it is so owned and controlled, the following provisions apply:—

- (a) The following terms are defined, broadly, as follows:—

“Interest” means any interest which would (subject as provided below) be taken into account, or which any person would be taken as having, in determining for the purposes of Part VI of the Companies Act 1985, whether a person has a notifiable interest and including an interest referred to in Section 209(1)(a), (b), (c) and (j) of that Act but not an interest which a person would be deemed to have in shares in which his spouse or any infant child or stepchild (or, in Scotland, pupil or minor) of his is interested by virtue of that relationship or which he holds as a bare or custodian trustee under the laws of England or a simple trustee under the laws of Scotland;

“Intervening Act” means the refusal, withholding, suspension or revocation of any right enabling an air service to be operated which is granted to, or applied for or enjoyed by, the Company or any subsidiary or the imposition of any conditions or limitations upon any such operating right which materially inhibit the exercise thereof, in either case by any state, authority or person in reliance upon any provision or by reason of any matter or circumstance relating to the nationality of persons owning or controlling the Company;

“Relevant Person” means: (a) any individual who is not a British citizen as defined by the British Nationality Act 1981; (b) any body corporate other than a body corporate which is incorporated under the laws of any part of, and which has its principal place of business and central management and control in, the United Kingdom; (c) a government or governmental department, agency or body, other than of the United Kingdom or any part thereof; (d) any municipal, local or statutory or other authority or any undertaking or body formed or established in any country other than the United Kingdom; and (e) any person who both falls within any of the foregoing paragraphs of this definition and would be taken to be interested in any shares pursuant to the provisions of Section 203 of the Companies Act 1985 if a body corporate were interested in those shares;

“Relevant Share” means any share in which a Relevant Person has an Interest or which is declared by the Directors to be a Relevant Share pursuant to (b) below, other than one particulars of which are removed from the separate register pursuant to (b) below and other than one held by (1) a trustee of an employees' share scheme of the Company or any subsidiary; (2) a trustee of a pension scheme approved by the Inland Revenue for the Company or any other business or undertaking carried on wholly or mainly in the United Kingdom; or (3) a charity which is registered or exempt under the Charities Act 1960;

- (b) The Directors shall maintain a separate register in which shall be entered particulars of any share in which a Relevant Person has been acknowledged to hold an Interest or in which the Directors consider there may be an Interest of a Relevant Person and have not been otherwise satisfied within 21 days of notice to the registered holder or to any other person who appears to them to be interested in that share, other than any share which they determine is not, or should not be treated as, a Relevant Share. Registered holders of shares which have not been acknowledged to be Relevant Shares will be obliged to notify the Directors if they become aware of Interests of Relevant Persons in shares held by them. The Directors are entitled to assume that all or any shares held by a Depository are Relevant Shares unless the contrary is established to their satisfaction;
- (c) The provisions of (d) to (k) below shall apply if the Secretary of State, on the application of the Directors, determines that it is necessary to take steps in order to protect any operating right of the Company or any subsidiary or the status of the Company or such subsidiary as a United Kingdom airline because (1) an Intervening Act has taken place or is contemplated, threatened or intended; or (2) the aggregate number of shares in the separate register or the ownership or control of the Company is otherwise such that an Intervening Act may occur;

- (d) After such a determination the Chairman or the Directors shall take such of the following steps as seem to him or them necessary or desirable to overcome, prevent or avoid an Intervening Act:—
- (1) the Chairman (or any other Director duly acting in place of the Chairman) may remove any Director from office;
  - (2) the Directors may seek to identify those shares which gave rise to the determination or would have given rise to a determination; or
  - (3) the Directors may specify a maximum aggregate number of Relevant Shares provided that the maximum shall never be less than 25 per cent.;
- (e) Shares identified pursuant to (d)(2), and shares in excess of the maximum specified in (d)(3), may be treated as Affected Shares. The Directors shall give a notice to the registered holder of any share which they determine to deal with as an Affected Share and to any other person who appears to the Directors to be interested in that share stating which of the following provisions shall apply to such share. The holder and any such other person may make representations to the Directors as to why any share should not be treated as an Affected Share;
- (f) A registered holder of an Affected Share on whom a notice so specifying has been served and not withdrawn shall not be entitled to attend or vote in respect of such share at any general or class meeting of the Company but the votes attached to such share shall vest in the chairman of any such meeting;
- (g) The persons on whom a notice so specifying has been served shall within 21 days thereafter dispose of either the Affected Share or Interests therein such that it ceases to be an Affected Share and if, after 21 days, the Directors are not satisfied that a suitable disposal has been made, the Directors may arrange for the sale of the Affected Share on behalf of the registered holder so that it is no longer capable of being treated as an Affected Share at the best price reasonably obtainable at the relevant time, based upon advice obtained by them for the purpose. The net proceeds of sale shall be held in trust by the Company for and paid (together with interest at such rate as the Directors deem appropriate) to the former registered holder on surrender of the certificate for such Affected Share;
- (h) In deciding which shares are to be dealt with as Affected Shares the Directors shall be entitled to have regard to which Interests in their opinion have caused the determination by the Secretary of State but, subject thereto, shall have regard to the chronological order in which particulars of Relevant Shares have been entered in the separate register, except where in their opinion to do so would be inequitable, in which case the Directors shall apply such other criteria as they may consider appropriate;
- (i) The transfer of any share shall be subject to the approval of the Directors if, in the opinion of the Directors, such share would upon transfer become or be capable of becoming or being treated as an Affected Share and the Directors may refuse to register the transfer of any such share;
- (j) At any time when the Directors have specified a maximum for the number of Relevant Shares or determined to deal with shares as Affected Shares they will publish in the United Kingdom, the United States and Canada notice of the determination of the Secretary of State, of any such maximum specified and of the provisions which can apply to Affected Shares and the name of any person who will answer enquiries relating to Affected Shares. At other times the Directors shall from time to time publish information as to the number of shares particulars of which have been entered in the separate register. The Directors will not be required to make the separate register available for inspection but will provide information to bona fide enquirers as to the number of Relevant Shares from time to time on such register;
- (k) If at any time when a determination has been made and not withdrawn anyone enquires of the Directors whether the number of Relevant Shares exceeds any maximum specified or whether any shares which he proposes to buy or in which he proposes to acquire an Interest would, in the opinion of the Directors, be capable on acquisition of becoming Affected Shares, the Directors shall, on sufficient information being given to them, notify the enquirer whether in their opinion the shares would in such circumstances be capable of becoming Affected Shares. Such notification shall not, however, be binding on the Directors or the Company;
- (l) If the Secretary of State, after consulting the Directors, resolves that grounds for the making of a determination have ceased to exist, he shall withdraw the determination and, on withdrawal, the above provisions shall cease to apply and the Directors shall give notice to any holder of an Affected Share on whom a notice under (v) above has been served and shall remove any maximum specified and shall publicise a notice of such withdrawal in a newspaper in the United Kingdom, the United States and Canada.

For the purpose of preventing, until 31st January, 1992, any person (other than the Custodian Bank under the Instalment Agreement entered into in connection with the offer for sale, a Depositary, a trustee of an employees' share scheme of the Company or any subsidiary, a Stock Exchange Nominee, the chairman of a meeting or underwriters in respect of contingent obligations to take up shares pursuant to an underwriting or sub-underwriting agreement) from retaining an Interest in shares which carry 15 per cent. or more of the votes attaching to the issued share capital of the Company the following provisions apply until 31st January, 1992:—

- (a) Any person who has an Interest (as defined above but including any interest which a person would be taken as having by reason of Section 203(1) of the Companies Act 1985) in shares which carry 5 per cent. or more of the votes attaching to the issued share capital of the Company is required to notify the Company of that Interest;
- (b) If any person has, or appears to the Directors to have or, if the Directors are unable to ascertain whether such a person has an Interest in the shares and so resolve, is deemed to have, an Interest in shares which carry 15 per cent. or more of the total votes attaching to the issued shares of the Company, the Directors shall serve a written notice on the registered holder of the shares concerned and on any other person who appears to the Directors to be interested in those shares. Such notice shall set out the restrictions referred to below and shall call for the interest concerned to be reduced to less than 15 per cent. by a disposal of shares or Interests therein within 21 days of the service of the notice (or such longer period as the Directors consider reasonable). The holder and any such other person may make representations to the Directors to the effect that no person having an Interest in shares which carry 15 per cent. or more of the votes attaching to the issued share capital of the Company is interested in such shares. No transfer of the shares comprised in the Interest may be made except for the purpose of reducing such Interest to less than 15 per cent.

- (d) After such a determination the Chairman or the Directors shall take such of the following steps as seem to him or them necessary or desirable to overcome, prevent or avoid an Intervening Act:—
  - (1) the Chairman (or any other Director duly acting in place of the Chairman) may remove any Director from office;
  - (2) the Directors may seek to identify those shares which gave rise to the determination or would have given rise to a determination; or
  - (3) the Directors may specify a maximum aggregate number of Relevant Shares provided that the maximum shall never be less than 25 per cent.;
- (e) Shares identified pursuant to (d)(2), and shares in excess of the maximum specified in (d)(3), may be treated as Affected Shares. The Directors shall give a notice to the registered holder of any share which they determine to deal with as an Affected Share and to any other person who appears to the Directors to be interested in that share stating which of the following provisions shall apply to such share. The holder and any such other person may make representations to the Directors as to why any share should not be treated as an Affected Share;
- (f) A registered holder of an Affected Share on whom a notice so specifying has been served and not withdrawn shall not be entitled to attend or vote in respect of such share at any general or class meeting of the Company but the votes attached to such share shall vest in the chairman of any such meeting;
- (g) The persons on whom a notice so specifying has been served shall within 21 days thereafter dispose of either the Affected Share or Interests therein such that it ceases to be an Affected Share and if, after 21 days, the Directors are not satisfied that a suitable disposal has been made, the Directors may arrange for the sale of the Affected Share on behalf of the registered holder so that it is no longer capable of being treated as an Affected Share at the best price reasonably obtainable at the relevant time, based upon advice obtained by them for the purpose. The net proceeds of sale shall be held on trust by the Company for and paid (together with interest at such rate as the Directors deem appropriate) to the former registered holder on surrender of the certificate for such Affected Share;
- (h) In deciding which shares are to be dealt with as Affected Shares the Directors shall be entitled to have regard to which Interests in their opinion have caused the determination by the Secretary of State but, subject thereto, shall have regard to the chronological order in which particulars of Relevant Shares have been entered in the separate register, except where in their opinion to do so would be inequitable, in which case the Directors shall apply such other criteria as they may consider appropriate;
- (i) The transfer of any share shall be subject to the approval of the Directors if, in the opinion of the Directors, such share would upon transfer become or be capable of becoming or being treated as an Affected Share and the Directors may refuse to register the transfer of any such share;
- (j) At any time when the Directors have specified a maximum for the number of Relevant Shares or determined to deal with shares as Affected Shares they will publish in the United Kingdom, the United States and Canada notice of the determination of the Secretary of State, of any such maximum specified and of the provisions which can apply to Affected Shares and the name of any person who will answer enquiries relating to Affected Shares. At other times the Directors shall from time to time publish information as to the number of shares particulars of which have been entered in the separate register. The Directors will not be required to make the separate register available for inspection but will provide information to bona fide enquirers as to the number of Relevant Shares from time to time on such register;
- (k) If at any time when a determination has been made and not withdrawn anyone enquires of the Directors whether the number of Relevant Shares exceeds any maximum specified or whether any shares which he proposes to buy or in which he proposes to acquire an Interest would, in the opinion of the Directors, be capable on acquisition of becoming Affected Shares, the Directors shall, on sufficient information being given to them, notify the enquirer whether in their opinion the shares would in such circumstances be capable of becoming Affected Shares. Such notification shall not, however, be binding on the Directors or the Company;
- (l) If the Secretary of State, after consulting the Directors, resolves that grounds for the making of a determination have ceased to exist, he shall withdraw the determination and, on withdrawal, the above provisions shall cease to apply and the Directors shall give notice to any holder of an Affected Share on whom a notice under (v) above has been served and shall remove any maximum specified and shall publicise a notice of such withdrawal in a newspaper in the United Kingdom, the United States and Canada.

For the purpose of preventing, until 31st January, 1992, any person (other than the Custodian Bank under the Instalment Agreement entered into in connection with the offer for sale, a Depositary, a trustee of an employees' share scheme of the Company or any subsidiary, a Stock Exchange Nominee, the chairman of a meeting or underwriters in respect of contingent obligations to take up shares pursuant to an underwriting or sub-underwriting agreement) from retaining an Interest in shares which carry 15 per cent. or more of the votes attaching to the issued share capital of the Company the following provisions apply until 31st January, 1992:—

- (a) Any person who has an Interest (as defined above but including any interest which a person would be taken as having by reason of Section 203(1) of the Companies Act 1985) in shares which carry 5 per cent. or more of the votes attaching to the issued share capital of the Company is required to notify the Company of that Interest;
- (b) If any person has, or appears to the Directors to have or, if the Directors are unable to ascertain whether such a person has an Interest in the shares and so resolve, is deemed to have, an Interest in shares which carry 15 per cent. or more of the total votes attaching to the issued shares of the Company, the Directors shall serve a written notice on the registered holder of the shares concerned and on any other person who appears to the Directors to be interested in those shares. Such notice shall set out the restrictions referred to below and shall call for the interest concerned to be reduced to less than 15 per cent. by a disposal of shares or Interests therein within 21 days of the service of the notice (or such longer period as the Directors consider reasonable). The holder and any such other person may make representations to the Directors to the effect that no person having an Interest in shares which carry 15 per cent. or more of the votes attaching to the issued share capital of the Company is interested in such shares. No transfer of the shares comprised in the Interest may be made except for the purpose of reducing such Interest to less than 15 per cent.

- (c) If such a notice is served and is not complied with in all respects to the satisfaction of the Directors and has not been withdrawn, the Directors shall arrange for the sale of shares on behalf of the registered holder at the best price reasonably obtainable at the relevant time, based upon advice obtained by them for the purpose. The net proceeds of sale shall be held on trust by the Company for and paid (together with interest at such rate as the Directors deem appropriate) to the former registered holder on surrender of the certificate for the shares concerned;
- (d) A registered holder on whom a notice referred to in (b) has been served is not entitled in respect of the share or shares comprised in the Interest, until such notice has been withdrawn or complied with to the satisfaction of the Directors, to attend or vote at any general or class meeting of the Company and the votes attaching to such shares shall vest in the chairman of any such meeting;

Any resolution or determination of, or decision or exercise of any discretion or power by, the Chairman or the Directors in relation to the provisions of this paragraph (iii) shall be conclusive and binding on all persons concerned and shall not be open to challenge and they shall not be obliged to give reasons therefor. The Directors shall not be obliged to serve any notice required under the provisions of this paragraph (iii) on any person if they do not know his identity or address. The absence of service in such circumstances or any accidental error in or failure to give any notice required shall not prevent the implementation of or invalidate any procedure referred to hereunder.

- (iv) Dividends and other distributions and return of capital: The Company may by ordinary resolution declare final dividends and the Directors may declare interim dividends but no final dividend shall be declared in excess of the amount recommended by the Directors and no dividend shall be payable otherwise than out of profits available for the purpose under applicable legislation. Except in so far as the rights attaching to, or the terms of issue of, any shares otherwise provide (no such shares currently being in issue), all dividends shall be apportioned and paid pro rata according to the amounts paid up thereon. On any distribution by way of capitalisation, the amount to be distributed will be appropriated pro rata amongst the holders of Ordinary shares according to the amounts paid up on their shares respectively. On a return of capital, whether on a winding-up or otherwise, the Ordinary shares will rank *pari passu* in all respects.

The Directors may, in their discretion, fix any date as the record date for any dividend or distribution. Any dividend unclaimed after a period of twelve years from the date of declaration thereof will be forfeited and revert to the Company. No dividends or other monies payable on or in respect of a share shall (except as specified in the Articles) bear interest against the Company.

- (v) Voting: Subject to disfranchisement in the event of non-payment of calls or non-compliance with a Disclosure Notice or pursuant to the provisions summarised in (iii) above and subject to any special terms as to voting attached to any shares (of which there are none at present), every member present in person (including any corporation present by a duly authorised representative) at a general meeting of the Company shall upon a show of hands have one vote and on a poll every member present as aforesaid or by proxy shall have one vote for every share held by him.

#### 4. Indebtedness

At the close of business on 31st August, 1989 the British Airways Group had outstanding the following borrowings and capital obligations under finance leases:—

Bank and other loans repayable:	
Within one year	£m 7
After more than one year	659
	<hr/> 666
Capital obligations under finance leases payable:	
Within one year	33
After more than one year	207
	<hr/> 240
Total	<hr/> <hr/> 906

All borrowings and capital obligations under finance leases which are denominated in foreign currency have been translated into sterling at the rates of exchange prevailing at the close of business on 31st August, 1989 or, where the loan repayment instalments have been covered forward, at the applicable forward contract rate.

Until 1st April, 1984, British Airways was able to enter into arrangements for borrowings and finance lease obligations with the benefit of guarantees provided by HM Treasury. At 31st August, 1989 loans and capital obligations under finance leases amounting to £14 million were guaranteed by HM Treasury and these guarantees will remain in force for the life of these loans and finance leases. If any such guarantee is called, the undertaking and all the property and revenues of British Airways would be charged with the repayment of any monies paid thereunder with priority from the date on which British Airways committed to or incurred the liability. At 31st August, 1989 there was no other security in respect of any of the British Airways Group's outstanding indebtedness.

At 31st August, 1989, the British Airways Group had contingent liabilities in respect of obligations of the Company and guarantees given by or on behalf of subsidiaries and related companies amounting to £104 million.

Cash balances and short-term deposits amounted to £160 million at 31st August, 1989.

Save as aforesaid and apart from intra-Group indebtedness and guarantees, neither the Company nor any of its subsidiaries had, at 31st August, 1989, any loan capital outstanding or created but unissued, term loans or other borrowings or indebtedness in the nature of borrowing, including bank overdrafts and liabilities under acceptances (other than normal trade bills) or acceptance credits, hire-purchase commitments, mortgages or charges, commitments under finance leases, guarantees or other material contingent liabilities.

British Airways is a party to certain operating leases which, at its option, may be converted into finance leases. None of these leases has been so converted and hence obligations thereunder have not been included in the above statement.

### 5. Working capital

The Directors consider that, having regard to available bank facilities and the proceeds of the rights issue described in this document, the British Airways Group will, following its participation in the Acquisition of UAL, have sufficient working capital for its present requirements.

### 6. Litigation

There are a number of identified legal and other claims which emanate from international airline operations and other activities of the British Airways Group for which the Directors have made what they believe is appropriate provision. In addition, experience with litigation and regulation in the United States and elsewhere has led the Directors to conclude that it is prudent to carry forward the provision of £25 million made in prior years. Neither British Airways nor any of its subsidiaries is engaged in or is aware of any litigation, claims or arbitration proceedings pending or threatened against them which, having regard to provisions already made, are likely to have, or which have had during the previous 12 months, a significant effect on the British Airways Group's financial position.

### 7. Directors' and other interests

- (a) As at 19th September, 1989 Morgan Guaranty Trust Company of New York, the Depository of the Company's ADR facility, has a non-beneficial interest in approximately 20.3 per cent. of the Company's existing issued share capital. The Directors are not aware of any other person who may be interested directly or indirectly in 5 per cent. or more of the issued share capital of the Company.
- (b) The interests, all of which are beneficial, of the Directors and their connected persons (as defined in Section 346 of the Companies Act 1985) in the share capital of the Company as shown in the register of Directors' interests required to be kept under the Companies Act 1985 are as follows:—

	Ordinary shares subject to no restrictions	Ordinary shares subject to restrictions *	Options Executive share option scheme	Options SAYE share option scheme
Lord King	29,684	316	750,695	4,596
Sir Colin Marshall	25,120	316	607,520	4,596
D. M. Stevens	5,000	246	200,000	
M. R. Angus	3,000			
A. M. Davies	5,000			
J. W. Jessop		3,500		
Sir Francis Kennedy	3,200			
H. U. A. Lambert	1,000			
Hon. Charles Price II	10,000			
	<u>82,004</u>	<u>4,378</u>	<u>1,558,215</u>	<u>9,192</u>

\* The British Airways Ordinary shares subject to restrictions are held in trust and may not be dealt in for a minimum period of two years following subscription.

The Ordinary shares in which the Hon. Charles Price II is interested are represented by American Depository Receipts.

The options under the Executive Share Option Scheme are at a price of 150p per share in relation to 266,666 options held by Lord King, at a price of 178p per share in relation to 224,719 options held by Sir Colin Marshall, at a price of 200p per share in relation to 200,000 options held by D. M. Stevens, at a price of 206p per share in respect of 194,174 options held by Lord King and 97,087 options held by Sir Colin Marshall, at a price of 207p per share in respect of 289,855 options held by Lord King and at a price of 210p per share in relation to 285,714 options held by Sir Colin Marshall. The options under the SAYE share option scheme are at a price of 161p per share. Options are normally exercisable during periods ranging from 1990 to 1999. No Director has an interest in shares in any subsidiary of the Company.

- (c) No Director has any interest in any transaction which is or was unusual in its nature or conditions or significant to the business of the British Airways Group and which was effected by the Company since 31st March, 1988 or which was effected prior to that date and remains in any respect outstanding or unperformed.
- (d) The aggregate remuneration (including pension contributions) of the Directors of the Company in the financial year ended 31st March, 1989 amounted to £1.84 million. In the financial year ending 31st March, 1990 the aggregate remuneration (including pension contributions) of the Directors of the Company is estimated to be £1.99 million.
- (e) The total emoluments of the Directors will not be varied as a consequence of the proposed investment in Airline Acquisition Corp.

### 8. Directors' service agreements

The service agreements of Lord King, Sir Colin Marshall and D. M. Stevens were on public display at the last Annual General Meeting of the Company on 17th July, 1989. There are no existing or proposed service agreements between any of the Directors of British Airways and British Airways or any other member of the British Airways Group which have not previously been on display and there have been no changes in any of the service contracts between British Airways and the Directors since they were made available for inspection as aforesaid.

### 9. Material contracts

The only contracts, not being contracts entered into in the ordinary course of business, which have been entered into by the British Airways Group during the two years preceding the date of this document, and which are, or may be, material are as follows:—

- (a) An agreement dated 29th April, 1988 between the Covia Partnership (1), Covia Corporation (2), Cypher Corporation (3), United Air Lines, Inc. (4), Distribution Systems Inc. (a wholly owned subsidiary of British Airways) (5), Roscor A.G. (6), Travel Industry Systems BV (7) and USAM Corp. (8), pursuant to which Distribution Systems Inc. purchased an 11.3 per cent. interest in the Covia Partnership, a Delaware general partnership established to operate the Apollo computer reservation system, from Covia Corporation (a wholly owned subsidiary of UAL) for \$113,130,000.

- (b) Letter agreement dated 14th September, 1989 from British Airways to Airline Acquisition Corp. pursuant to which British Airways agreed, subject (*inter alia*) to the approval of the shareholders of British Airways, to subscribe \$750 million for preferred stock in Airline Acquisition Corp. on the terms described in the letter agreement and in this document. Subscription for the preferred stock will be made simultaneously with the closing of the tender offer made by Airline Acquisition Corp. for UAL.
- (c) an agreement dated 26th September, 1989 between the the Issuer (1), the Company (2), and Lazard Brothers, SG Warburg Securities and UBS Phillips & Drew Securities Limited ("the Underwriters") (3) whereby the Underwriters (severally as to one-third each) have conditionally agreed to underwrite the issue of the 320,215,349 Bonds at 100p per Bond in consideration of the payment to the Underwriters of a commission of 2 per cent. of the aggregate subscription price of the Bonds out of which the Underwriters will pay all sub-underwriting commissions in respect of the underwriting, a fee to the brokers to the rights issue of ¼ per cent. of such value and their own legal expenses. All other expenses of the rights issue are to be paid by the Issuer. The agreement includes warranties and indemnities given by the Issuer and the Company in favour of the Underwriters.

#### 10. UK Taxation

- (a) The Company is not and has not since incorporation been a close company as defined in the Income and Corporation Taxes Act 1988.
- (b) Under current legislation, no tax will be withheld by the Company when it pays a dividend. However, when paying a dividend the Company is obliged to account to the Inland Revenue for advance corporation tax ("ACT"). The rate of ACT is fixed by reference to the basic rate of income tax and at present equals 25 per cent. of the aggregate of the dividend and of the related ACT.

A holder of ordinary shares who is resident (for tax purposes) in the United Kingdom and who receives a dividend from the Company will be entitled to a tax credit of an amount equal to the related ACT. A company so resident will be able to treat any dividend received and the related tax credit as franked investment income. An individual so resident will be taxable upon the total of the dividend received and the tax credit, but the tax credit will discharge his liability to basic rate income tax and, if the tax credit exceeds his liability to tax on the dividend, he will be able to claim the excess.

Subject to certain exceptions for Commonwealth citizens, citizens of the Republic of Ireland, residents of the Isle of Man or the Channel Islands and certain others, the right of a holder of Ordinary shares who is not resident in the United Kingdom to claim any part of the tax credit will depend upon the existence and terms of any double tax convention between the United Kingdom and the country in which he is resident. A holder who is not resident in the United Kingdom should consult his own tax advisers concerning his tax liabilities on dividends received, whether he is entitled to reclaim any part of the tax credit and, if so, the procedure for doing so.

A shareholder resident outside the United Kingdom may also be subject to foreign taxation on dividend income under local law. Any person who is in doubt as to his taxation position should consult an appropriate professional adviser.

- (c) Any dealing for consideration with a provisional allotment letter representing Bonds will generally be subject to stamp duty reserve tax at 0.5 per cent. on the consideration and any transfer on a sale of any Bonds will be subject to *ad valorem* stamp duty of 0.5 per cent.

#### 11. Information concerning British Airways Capital Limited

- (a) The Issuer is a subsidiary of British Airways and was incorporated in Jersey under Jersey law (registration number 45321) on 25th September, 1989 with limited liability. Under Clause 3 of its Memorandum of Association its corporate purposes include the lending of monies and the issue of shares, as well as the borrowing of monies and the issue of debt securities.

The Issuer has not engaged in any activities other than those incidental to its formation and the authorisation of the issue of the Bonds and the Preference Shares.

The registered office of the Issuer is located at 39/41 Broad Street, St. Helier, Jersey Channel Islands.

- (b) The Directors of the Issuer are D. M. Stevens, R. J. Ayling, R. D. A. Galbraith and D. Ford, each of Speedbird House, Heathrow Airport (London), Hounslow TW6 2JA.

The Secretary of the Issuer is Barclaytrust International Limited of 39/41 Broad Street, St. Helier, Jersey, Channel Islands.

- (c) The Issuer has an authorised share capital of £3,261,000 which will be divided into 1,000 Founders' Shares having a par value of £1 each and 325,000,000 Unclassified Shares having a par value of 1p each. All of the Founders' Shares will be issued, fully paid, and will be beneficially owned as to 890 by British Airways and as to 110 by Barclays Bank PLC. The Issuer is also issuing the Bonds. The Unclassified Shares may be issued either as Exchangeable Redeemable Preference Shares having a par value of 1p each on conversion of Bonds or may be issued as Nominal Shares having a par value of 1p each for the purpose of providing funds for the redemption of such Preference Shares.

The capitalisation of the Issuer immediately following the issue of the Bonds will be as follows:—

Issued share capital - Founders' Shares £1,000

Other than the Bonds, the Issuer has no borrowings, or indebtedness in the nature of borrowings, or contingent liabilities.

#### 12. General

- (a) British Airways is the parent company of the British Airways Group.
- (b) The auditors of British Airways are Ernst & Young of Becket House, 1 Lambeth Palace Road, London SE1 7EU. Ernst & Young have audited British Airways' annual accounts for the five financial years ended 31st March, 1989.
- (c) Lazard Brothers & Co., Limited, Morgan Stanley & Co. Incorporated and R. Watson & Sons have each given and have not withdrawn their respective written consents to the issue of this document with the inclusion of the references to them (and, in the case of R. Watson & Sons, to the references to their report) and to their names in the form and context in which they appear.

- (d) The rights issue has been underwritten by Lazard Brothers & Co., Limited of 21 Moorfields, London EC2P 2HT, SG Warburg Securities of 1 Finsbury Avenue, London EC2M 2PA and UBS Phillips & Drew Securities Limited, 100 Liverpool Street, London EC2M 2RH.
- (e) The financial information in respect of the British Airways Group contained in Appendix 3 of this document does not constitute full accounts in respect of the financial period ended 31st March, 1989. Full accounts of the Company for that financial period have been delivered to the Registrar of Companies and the auditors have made an unqualified report thereon within the meaning of Section 271 of the Companies Act 1985.
- (f) The Registrars of the Company are Lloyds Bank Plc, Registrar's Department, Goring-by-Sea, Worthing, West Sussex BN12 6DA. The receiving bankers for the rights issue are Barclays Bank PLC, New Issues, PO Box 123, Fleetway House, 25 Farringdon Street, London EC4A 4HD. The Registrars to the issue are Barclays Bank PLC, Registration, PO Box 34, Octagon House, Gadbrook Park, Northwich, Cheshire CW9 7RD.
- (g) Save as disclosed in this document there has been no significant change in the financial or trading position of the British Airways Group since 31st March, 1989, the date to which British Airways' latest audited consolidated financial statements were made up.

### 13. Overseas shareholders

#### (a) United States and Canada

The provisional allotment letters, the Bonds and the new British Airways shares have not been, and will not be, registered under the United States Securities Act of 1933, as amended, or under the securities legislation of any province or territory of Canada and accordingly, none of the provisional allotment letters, the Bonds or the new British Airways shares may be offered, sold, delivered, renounced, transferred, assigned, exchanged or otherwise disposed of, directly or indirectly, as part of their distribution, in the United States or Canada or to or for the account or benefit of any North American person. Bonds will not be provisionally allotted, nor will provisional allotment letters be despatched to any shareholders with registered addresses in the United States or Canada. The rights of such persons will be sold in the market, nil paid, by the close of business on 2nd October, 1989 and any net proceeds (after deduction of expenses) will be distributed to the persons entitled thereto, save that no payment will be made of any individual amount of less than £2.50. Such amounts will be retained by the Issuer.

To give effect to the foregoing restrictions, in order to take up rights to the Bonds or register renunciation each prospective holder of Bonds will be required to make a declaration, utilising the definitions of "United States" and "North American person" set forth in this document, to the following effect:—

"(1) I am not/None of us is a North American person; and

(2) I am not/None of us is acquiring any of the Bonds for the account or benefit of a North American person or with a view to their offer, sale, delivery, renunciation, transfer, assignment, exchange or other disposition, directly or indirectly, in the United States or Canada or to or for the account or benefit of a North American person or to any other person whom I/we have reason to believe is purchasing with a view to such offer, resale or delivery."

If this declaration is not made any Bonds to which the prospective holder would have become entitled will be sold in the market on 23rd October, 1989 and the cash proceeds (if a premium over the subscription price and the expenses of sale can be obtained) remitted, save that no payment will be made of an individual amount of less than £2.50. Such amounts will be retained by the Issuer.

The underwriters have represented that they are not North American persons and are not acquiring the provisional allotment letters or the Bonds for the account of North American persons and have agreed that they will not offer, sell or deliver, directly or indirectly, such provisional allotment letters or Bonds in the United States or Canada or to or for the account of North American persons. In addition, the underwriters have agreed that prior to the date 90 days after the date of distribution of the provisional allotment letters and the Bonds is completed (as determined by Lazard Brothers) they will not, as principal or agent, offer, sell or deliver, directly or indirectly, in the United States or Canada or to or for the account of any North American person, any provisional allotment letters or Bonds no matter how acquired.

#### (b) South Africa

In order to comply with South African law, provisional allotment letters to be sent to shareholders with registered addresses in South Africa will not be renounceable. Such persons may require the approval of the South African Exchange Control authorities if they wish to take up their rights. All payments must be in pounds sterling.

#### (c) Republic of Ireland

The attention of shareholders resident in the Republic of Ireland is drawn to the Irish Exchange Control regulations applicable to holders of United Kingdom securities. If such shareholders wish to take up their allotments they should consult an Approved Agent in the Republic of Ireland (i.e. a bank, stockbroker or solicitor) to ensure that they obtain the necessary permission to enable them to take up their allotments. All payments must be in pounds sterling.

#### (d) Other overseas territories

Persons resident in other overseas territories should consult their professional advisers as to whether they require any governmental or other consents or need to observe any other formalities to enable them to take up the Bonds provisionally allotted to them. All payments must be in pounds sterling.

In cases where overseas shareholders are not allotted Bonds or are unable to take up the Bonds provisionally allotted to them, such Bonds will (if a net premium can be obtained over the subscription price and expenses of sale) be sold in the market for the benefit of such persons as described under "Procedure in respect of rights not taken up".

**14. Documents available for inspection**

Copies of the following documents will be available for inspection at the offices of Linklaters & Paines, Barrington House, 59-67 Gresham Street, London EC2V 7JA during normal business hours on any weekday (excluding Saturdays and public holidays) until 13th October, 1989 and at the Extraordinary General Meeting:—

- (a) the Memorandum and Articles of Association of the Company and the Issuer;
- (b) the published audited consolidated accounts of the British Airways Group for each of the two financial years ended 31st March, 1989;
- (c) the annual reports and Forms 10-K of UAL filed with the United States Securities and Exchange Commission for the two fiscal years ended 31st December, 1988 and UAL's quarterly report on Form 10-Q for the quarter ended 30th June, 1989;
- (d) the rules of the share option schemes referred to in paragraph 7 above;
- (e) the service agreements referred to in paragraph 8 above;
- (f) the contracts referred to in paragraph 9 above;
- (g) the written consents and the report referred to in paragraph 12(c) above; and
- (h) the Trust Deed, the Deed Poll and the Registrar's Agreement (in each case as defined in Appendix 4).

27th September, 1989 ✓

# BRITISH AIRWAYS Plc

## NOTICE OF EXTRAORDINARY GENERAL MEETING

Notice is hereby given that an Extraordinary General Meeting of the Company will be held at The New Connaught Rooms, 61/65 Great Queen Street, London WC2 on Friday, 13th October, 1989 at 9.00 am to consider and if thought fit to pass the resolution set out below as an Ordinary Resolution:—

### ORDINARY RESOLUTION

THAT the proposed participation by the Company in the Acquisition of UAL and arrangements relating thereto on the terms described in the letter from the Chairman of the Company to the Company's shareholders dated 27th September, 1989 or on such other terms as the Directors may consider appropriate is hereby approved.

By order of the Board  
R. J. Ayling  
Secretary

27th September, 1989

Registered Office:  
Speedbird House  
Heathrow Airport (London)  
Hounslow TW6 2JA

#### Notes:

- (i) Every person entitled to attend and vote at the Extraordinary General Meeting convened by the above notice is entitled to appoint a proxy or proxies to attend and, on a poll, to vote on his behalf. A proxy need not be a member of the Company.
- (ii) To be valid, a form of proxy and any power of attorney or other authority under which it is signed must be lodged with the Registrars of the Company, Lloyds Bank Plc, Registrar's Department, Goring-by-Sea, Worthing, West Sussex BN12 4ZZ, not less than 48 hours before the time appointed for the holding of the meeting.
- (iii) Completing and returning a form of proxy will not prevent a member from attending in person and voting at the meeting should he so wish.