

KLM ROYAL DUTCH AIRLINES

Form 425

October 01, 2003

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Filed by Air France

This communication is filed pursuant to Rule 425 under The Securities Act of 1933, as amended,  
and deemed filed pursuant to Rule 14d-2 of the Securities Exchange Act of 1934, as amended.

Subject Company: KLM Royal Dutch Airlines

Commission File Number: 001-04059

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## Legal Information

The combination of KLM and Air France will be implemented through an exchange offer made by Air France to all shareholders of KLM. This document is neither an offer to purchase nor a solicitation of an offer to sell shares of KLM. Any offer in the United States will only be made through a prospectus which is part of a registration statement on Form F-4 filed with the U.S. Securities and Exchange Commission (the SEC). KLM shareholders who are U.S. persons or are located in the United States are urged to carefully review the registration statement on Form F-4 and the prospectus included therein, the prospectus, the Schedule TO and other documents relating to the offer that will be filed by Air France with the SEC because these documents contain important information relating to the offer. You are also urged to read the related solicitation/recommendation statement on Schedule 14D-9 that will be filed with the SEC by KLM regarding the offer. You may obtain a free copy of these documents after they are filed with the SEC and other documents filed by Air France and KLM with the SEC at the SEC's web site at [www.sec.gov](http://www.sec.gov). Once such documents are filed with the SEC, you will also be able to inspect and copy the registration statement on Form F-4, as well as any documents incorporated by reference therein, the Schedule TO and the Schedule 14D-9 at the public reference room maintained by the SEC at 450 Fifth Street, NW, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the public reference room. These documents may also be obtained free of charge by contacting Air France, Investor Relations, 45, rue de Paris, 95747 Roissy CDG Cedex, France. (tel: +33 1 41 56 88 60), or KLM, Amsterdamweg 55, 1182 GP Amstelveen, The Netherlands. Attention: Investor Relations (tel: +31 20 64 93099). **YOU SHOULD READ THE PROSPECTUS AND THE SCHEDULE 14D-9 CAREFULLY BEFORE MAKING A DECISION CONCERNING THE OFFER.**

## Forward-Looking Statements

The information herein contains, and the Air France, KLM and their representatives may make, forward-looking statements either orally or in writing, about Air France, KLM and their businesses. These forward-looking statements, which include, but are not limited to, statements concerning the financial condition, results of operations and businesses of Air France and KLM and the benefits expected to result from the contemplated transaction, are based on management's current expectations and estimates.

These forward-looking statements involve known and unknown risks, uncertainties and other factors, many of which are outside of Air France or KLM's control and are difficult to predict, that may cause actual results to differ materially from any future results expressed or implied from the forward-looking statements. These statements are not guarantees of future performance and involve risks and uncertainties including, among others: the risk that the conditions relating to the required minimum tender of shares might not be satisfied; failure by Air France and KLM shareholders to approve the planned corporate reorganizations; inability to obtain, or meet the conditions imposed for, regulatory approvals in a timely manner or at all; the risk that the businesses of Air France and KLM will not be integrated successfully and the the expected synergies and cost savings will not be achieved; unanticipated expenditures; changing relationships with customers, suppliers and strategic partners; and other economic, business, competitive and/or regulatory factors affecting the businesses of Air France and KLM generally. Air France and KLM caution that the foregoing list of important factors is not exhaustive. Additional information regarding the factors and events that could cause differences between forward-looking statements and actual results in the future is contained in KLM's Securities and Exchange Commission filings, including KLM's Annual Report on Form 20-F. Air France and KLM undertake no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

**THE FOLLOWING IS A TRANSLATION OF INFORMATION MADE AVAILABLE  
ON A FRENCH TOLL-FREE TELEPHONE NUMBER ON OCTOBER 1, 2003.**

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**Air France retail shareholders hotline**

**Q&A support document**





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**Strategic rationale of the operation**

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**Strategic rationale**

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1. Why organizational and financial integration and not just a commercial agreement? Couldn't you have reached the same benefits through a commercial alliance with a JV or profit sharing scheme?

There are clearly different ways to approach cooperation between airlines. This ranges from the purely commercial alliance to the full merger. Each has its own advantages and disadvantages. The most important thing is to ensure that the chosen model fits the situation in terms of overlap of the catchment areas, the nature of the competition between the two potential partners, and the desired cooperation strategy.

The alliance of Air France and KLM within the same group provides far more benefits than what could be achieved from a simple commercial partnership (even in the case of a JV with a profit sharing scheme and/or minority cross shareholdings).

In fact it provides the opportunity to achieve the benefits of a commercial agreement (i.e. revenues synergies) while overcoming the drawbacks attached to that formula in the case of Air France and KLM.

Both airlines operate a long-haul network from very close hubs (the distance between the two hubs being less than 400 km). This means that, in certain circumstances, the two hubs are competing for customers. To be fully effective, then, such an alliance can therefore only work better on the basis of an extremely well coordinated strategy and a common bottom line, which advance the alignment of both companies' economic interests.

Moreover, while commercial alliances are a good way to deliver revenue synergies, we believe capitalistic alliances provide the opportunity for both deeper synergies (i.e. cost synergies) and faster phase-in of synergies.

2. Why doesn't KLM join SkyTeam without integrating with Air France?

*same answer as n°1.*

3. Why put in place such one group two airlines concept?

The structure of the deal aims to advance in the consolidation of the industry and promote the benefits of such consolidation in terms of market shares, synergies etc. while at the same time keeping the two airlines distinct in order to capitalize on both brands and temporarily deal with the issue of protecting the air traffic rights.

4. What is the point of taking-over KLM if both companies remain two distinct operating airlines?

After an initial period, Air France and KLM will be headed by a holding company (Air France KLM) which will be responsible for the strategic development of both companies.

The structure of the deal aims to keep two distinct airlines for two main reasons:

From a regulatory point of view, this scheme will allow to secure KLM's traffic rights.

From a strategic point of view, it will enable us to capitalize on both brands (brands are major assets in the airline industry).

5. Why not merge the operating companies as well? Is that an option for the future and if so when could that be achieved?

We ruled out merging the operating companies because we want to preserve the identities of each airline and capitalize on their respective assets, notably their brands. Today we do not envisage this option for the future.

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6. How the two airlines complement each other? In which areas do you view some overlap between the two?

The common approach of the two airlines as well as the effective complementarities of their respective positions and businesses lay the foundation for the success of the enlarged airline group. Both airlines have similar business profile with the same three core businesses: passengers, cargo and maintenance.

In each one of these three core activities, Air France and KLM complement each other very well.

In the passenger business where Air France/KLM will become the 1<sup>st</sup> European airline group and where Air France and KLM have similar hub-based strategies, the complementarities of the Air France and KLM networks are excellent:

out of a total of 101 long-haul destinations Air France and KLM only have 31 in common;

on medium-haul networks, Air France is particularly strong in Southern Europe while KLM is strong in Northern Europe.

The complementarity of Air France's and KLM's partnerships is also excellent, particularly in the US where Air France's partner Delta already has an agreement with KLM's two partners NorthWest and Continental.

A strong presence in cargo where Air France and KLM are the 4<sup>th</sup> and 11<sup>th</sup> largest in the world respectively (*source IATA 2002 excluding integrators such as Fedex and UPS*), but with complementary capabilities and expertise

In the maintenance business, the combination of Air France Industries and KLM E&M will lead to the creation of one of the largest MRO providers with full capabilities for both Airbus and Boeing product lines and scale and capacity to meet the maintenance requirements of major airlines

7. Isn't Air France just taking a main competitor out of the market?

No. KLM will remain a distinct operating airline and will contribute together with Air France to the success of the enlarged group bringing to the group its complementary strengths such as brand, network and non constrained hub.

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Timing

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8. When will the definite agreement be signed?

The definitive agreement is expected to be signed within the next few weeks

9. Is this good timing for Air France? For KLM?

It is good timing for both airlines if they want to take full advantage of being the first movers in the consolidation of the European airline industry at a time when economic conditions are expected to improve and when the enlargement of the European Union is expected to offer additional growth opportunities.

Such a move could also benefit from a favorable evolution of the regulatory framework regarding the traffic rights.

10. Why not wait until Air France is fully privatized?

As part of this transaction, Air France will be privatized by dilution of the stake held by the French State which will decrease from 54% of Air France to 44% of the enlarged group (assuming full acceptance of the offer by KLM common shareholders but before exercise of the warrants) and will subsequently reach 39% if the warrants are fully exercised.

In any case, the French State has publicly stated its intention to substantially reduce its stake, with the timing of a disposal being subject to market conditions. For several years, Air France has been operating as a publicly listed company with the French State as a majority shareholder; the enlarged group, with the French State as a minority shareholder likely to further reduce its stake, will naturally continue to do so.

11. Why didn't Air France wait until KLM had fully implemented its restructuring program?

The deal doesn't call into question the restructuring program of KLM. The sooner Air France and KLM start to cooperate the sooner the synergies are expected to be implemented

12. Is this decision and the timing compelled by KLM's financial situation?

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No. Although KLM, like the whole airline industry, has been suffering from the current crisis, KLM enjoys a strong commercial position (brand, hub, staff, etc.) and still benefits from a comfortable cash position ( 0.9 bn of cash in hand).

Even under these difficult market circumstances, KLM has still been able to attract new financing for its new fleet. Most of KLM's debt is secured debt without any restrictive covenants.

In addition, we believe that KLM's financial position should improve as a result of better market conditions and the implementation of its current restructuring program. Finally, the deal with Air France should bring extra benefits, such as synergies and greater access to financial markets.

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13. What are the main timing risks currently identified?

As of today, we do not expect any specific factor to materially disrupt the planned timing of the operation. The main factors that could impact the timeframe are:

longer than expected examination process by the European Commission

longer than expected preparatory and review process with the SEC

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**Scope of the alliance**

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14. What businesses and other activities are included in the integration? What will be excluded?

The proposed exchange offer applies to all KLM ordinary shares (including New York registry shares). If successful, the share exchange will result, after an initial period, in the totality of both Air France and KLM being consolidated within the Air France-KLM holding company.

15. After integration of KLM, will any of KLM's or Air France's non-core activities be disposed of? In particular, will KLM's leisure activities will be disposed of?

We do not intend at this stage to divest of any activity. Both Air France and KLM are pure players in the air transport sector sharing three core businesses (passenger, cargo and maintenance).

16. Do you expect Alitalia to join the new Air France-KLM structure ?

Air France, KLM and Alitalia have signed a trilateral agreement that covers the conditions under which Alitalia may enter the proposed combination. With regard to the cargo businesses, Air France and KLM intend to agree on an accelerated integration of the Air France, KLM and Alitalia cargo activities, in order to establish a trilateral integrated cargo partnership. Next to the trilateral agreement, KLM and Alitalia intend to sign a bilateral agreement that arranges the commercial cooperation between the two airlines.

17. Beside Alitalia, do you plan to add other parties in the future?

In the short term, Air France and KLM will be busy working on the coordination of their respective networks, their hubs and their other activities while SkyTeam will welcome three new partners (KLM, Northwest and Continental). This will result in the creation of the first European airline group, while putting SkyTeam on an equal footing with Star Alliance as the largest global airline alliance. It already represents a major step forward in the consolidation of the air transport industry.

At this stage, it is too early to tell whether the future addition of new parties will make sense. Should any opportunity arise in the future, it will be carefully studied in the best interests of both Air France and KLM customers, employees and shareholders.

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**Risk factors**

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18. What could jeopardize the transaction?

The deal remains conditional upon several approvals or preliminary requirements, including the following:

approval from relevant European and US competition authorities (including European Commission and Department of Justice),

effectiveness of the SEC registration statement and approval to list on the NYSE

tender by 70% of KLM common shareholders (including treasury shares),

approval of the transaction by the general meeting of Air France shareholders

We are, however, confident that these conditions can be met.

19. Do you foresee any difficulties completing the transaction? And moving forward? Which issues do you see as the most difficult?

We do not foresee any significant difficulties in completing the transaction, which is supported by both management teams, both Boards and both governments.

However, we remain cautious, as the transaction is subject to antitrust authorities and shareholders approval even though we are confident of the positive outcome of these decisions.

Completion of the transaction will obviously depend on whether KLM shareholders tender their KLM shares in exchange for Air France shares and warrants. We believe that the premium offered to KLM shareholders should lead to a successful outcome for the share exchange offer.

Moving forward, initial contacts between the two companies so far confirm that both airlines have much in common and that they share the same business vision while having complementary strengths.



We are therefore extremely confident that both airlines will fruitfully cooperate on the implementation of revenue and cost synergies while organizing the development of both Air France and KLM in a coherent and harmonious manner. The corporate governance system in place will assist this coordinated implementation and harmonious development.

20. What are the chances that the transaction will be rejected by regulatory bodies/ anti-trust authorities?

We are confident of the approval of the transaction by regulatory bodies and anti-trust authorities. We believe the transaction is in line with the foreseeable evolution of the European air transport sector advocated by the European Commission.

Our businesses operate in a highly competitive market, and competitive issues are likely to arise on a limited number of routes.

21. What are the chances of a counter-bid for KLM's shares?

Given the current regulation of traffic rights and the necessary cooperation between the two parties in this kind of transaction, it is hard to imagine a hostile take-over from a third party.

22. Do you expect any difficulties, as far as these plans are concerned, coming from the Italian government?

Absolutely not. We expect the Italian government to support the deal, as we have secured Alitalia's consent. We have kept them informed of our intentions, and we have preserved the Alitalia/Air France alliance already in place in order to share the benefits of this transaction with Alitalia.

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**Key terms and conditions of the transaction**

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**Terms of the transaction**

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23. What is the exchange parity?

KLM shareholders will receive 11 Air France shares and 10 warrants for 10 KLM ordinary shares.

Based on the closing price of Air France stock on 29 September 2003 this values each KLM ordinary share at 16.74 and represents a premium of 40% to the closing share price of KLM on 29 September and a premium of 77% to the 3 months average share price of KLM.

The transaction values the entire common share capital of KLM at approximately 784 million (including the theoretical value of the warrants).

24. How will the warrants be offered to KLM shareholders?

The warrants will be offered to KLM shareholders on the following terms:

- n 10 Air France warrants for 10 KLM Shares
- n 3 warrants give the right to subscribe or acquire 2 Air France (future Air France-KLM) shares at a price of 20
- n The maturity of the warrants will be 3<sup>1/2</sup> years post closing of the transaction
- n The exercise period will start after the 18<sup>th</sup> month following the closing of the transaction

The warrants will be listed on Euronext Paris, Euronext Amsterdam and the New York Stock Exchange.

25. How will the other classes of shares (KLM preference and priority shares) be acquired?

Upon the successful closing of the exchange offer, the Dutch State has agreed to sell to Air France its holding of 975 priority shares in KLM. The total costs for priority shares is not significant to Air France.

The Stichting Luchtvaartbelangen Nederland and Rabobank, owners of the 7 million outstanding Cumulative Preference C shares in KLM (representing 11.7% of KLM's voting rights outstanding) have agreed to sell those shares to Air France conditional to the successful closing of the exchange offer. The total cost of the Cumulative Preference C Shares for Air France will be 14 million.

The Dutch State which currently owns 8.8 millions Cumulative Preference Shares A in KLM (representing 14.7% of total voting rights outstanding), will decrease its stake in a similar proportion to the French State in Air France-KLM over time. The total cost of the Cumulative Preference A shares for Air France will be 20 million.

26. What is the minimum tender for the exchange offer?

The minimum level of acceptances is 70%.

27. Where will the Air France shares to be exchanged for KLM shares come from?

KLM shareholders will receive newly issued Air France shares.

28. When will the Air France capital increase take place?

Air France's reserved capital increase will take place after the closing of the exchange offer, provided the minimum tender has been reached.

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29. Where will the shares attributed to the exercise of warrants come from?

Shares attributed to the exercise of warrants will either be newly issued Air France shares or treasury shares owned by Air France.

30. What is the timetable for the actual share exchange offer? Why wait for the 1<sup>st</sup> quarter 2004 before launching it?

Before the offer can be launched, several conditions will need to be satisfied or waived. Approval from the European and US competition authorities is one of them. Air France also needs to register the shares to be offered in the exchange offer with the SEC and list them on the NYSE.

It is expected that these conditions will have sufficiently advanced to permit the launch of the offer early next year.

Expected timetable:

October 2003:	Envisaged signing of the transaction agreement and regulatory filings with competition authorities
First half of March 2004:	Offer scheduled to be launched
Second half of March 2004:	EGM of Air France and KLM shareholders
Second half of April 2004:	Closing of the offer

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Conditions

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31. What are the main pre-conditions for Air France share exchange offer?

The offer will be subject to, amongst others, the following conditions being satisfied:

At least 70% of the common shares of KLM being tendered;

Approval from antitrust and other governmental authorities, and no governmental orders restricting the consummation of the transaction;

Consultation with the Works Council of KLM;

Approval by the Air France s shareholders meeting of the capital increase in relation with the share exchange offer;

Formal approval from French, Dutch and US stock exchange and other regulatory authorities for listing and offer documentation.

32. Does Air France and/or KLM need approval from their respective shareholders?

Air France shareholders will be asked to approve the Air France capital increase at the Extraordinary General Meeting that is expected to take place in March 2004.

KLM shareholders will have to approve the changes in KLM s articles of association regarding the governance structure. An Extraordinary General Meeting is expected to take place in March 2004.

33. Does Air France need approval from the French government?

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The proposed transaction is subject to the approval of the exchange ratio and the exchange procedure by the French Commission des Participations et Transferts (CPT) and by the French Minister of Economy.

Furthermore, as a majority shareholder, the French State will have to vote for the proposed Air France capital increase.

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**Shares & listing**

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34. How many common shares will be listed?

Before the exercise of warrants, 271.3 million common shares are expected to be listed (of which 219.8 million shares held by former Air France shareholders and 51.5 million held by former KLM shareholders).

An additional 31.2 million common shares could be created following the exercise of the warrants (exercise period will start after the 18<sup>th</sup> month following the closing of the transaction)

35. Where will the new shares be listed?

The new shares will be listed on the Paris, Amsterdam and New York stock exchanges (in the form of American Depositary Shares).

36. How many warrants will be issued?

Assuming 100% acceptance of the share exchange offer, 46.8 million Air France warrants will be issued. If all the issued Air France warrants are exercised 31.2 million new Air France-KLM shares will be issued which would lead to an increase of the share capital of Air France-KLM of 624 million euros.

37. Where will the warrants be listed? When?

The warrants will be listed on the Paris, Amsterdam and New York stock exchanges at the closing of the exchange offer.

38. How much of KLM's capital is already committed to the exchange of shares?

None of the common shares, but there is an understanding with KLM in respect of its treasury shares.

39. Why does Air France need to list on the NYSE? When will this happen?

KLM New York registry shares will be exchanged against Air France ADS (American Depositary Shares) at an exchange ratio of 11 Air France ADSs + 10 Air France warrants for 10 KLM New York Registry shares.

40. What is an ADS?

An ADS is a dollar-denominated negotiable security that represents ownership of shares in a non-U.S. company. ADSs are evidenced by ADRs (American Depositary Receipts).

41. Which level of ADSs will Air France choose to list on NYSE?

Air France's ADS program will be level 3.

Unlike a level 1 ADS facility, which can only be traded over-the-counter, level 3 ADSs are traded on an organized market (NYSE, NASDAQ, Amex). Level 3 programs also require a greater degree of SEC reporting: issuers must reconcile their accounting to U.S. GAAP and meet the listing requirements of a particular U.S. exchange.



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Shareholding structure

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42. What is the current capital structure of KLM?

KLM shareholders' capital includes common shares and shares with specific rights:

- n 46.8 million common shares are listed on the Amsterdam and New York (in the form of New York registry shares) stock exchanges
  
- n *non-listed* shares with specific rights
  - 1,275 priority shares held by the State of the Netherlands and five Dutch institutions
  - 8.8 millions cumulative preference shares A held by the State of the Netherlands
  - 7 million cumulative preference shares C held by a Dutch foundation

In addition, the Dutch State has an option allowing it to obtain 50.1% of KLM's voting rights if KLM's traffic rights are challenged because of the nationality of KLM shareholders.

43. What will the new shareholding structure be at the end of the offer?

Assuming 100 percent acceptance of the offer and before exercise of the warrants:

Current KLM common shareholders would own 19% of the enlarged group.  
The shareholding of the French state in Air France would mechanically be diluted from 54% to 44%.  
The other Air France shareholders would own 37% of the enlarged group.

44. What does integration mean for existing Air France shareholders? KLM shareholders?

Former Air France and KLM shareholders will be joint shareholders of the Air France-KLM holding company.

When KLM shareholders offer their shares in the tender offer, they will become shareholder of the enlarged Air France, which after an initial period will become Air France-KLM.

If the transaction is successful, Air France shareholders will automatically become shareholders of the enlarged Air France group, which after an initial period will become the holding company Air France-KLM.

Assuming full acceptance by KLM common shareholders, former Air France shareholders will have a 81% stake in Air France-KLM and former KLM shareholders will have a 19% stake in the new entity. As such, both may benefit from the synergies generated by the integration of the two companies within a single group.

45. What does this transaction mean for KLM's priority shareholders (including the State of The Netherlands)?

As part of the transaction, an agreement with the Dutch State regarding its 14.7% voting rights in KLM has been concluded stating that it would decrease its stake in KLM in a similar proportion as the French State in Air France-KLM over time and would sell it to Air France-KLM for a total amount of 20m.

The acquisition of KLM's other classes of shares has been secured by Air France for a maximum cost of 14m and will be effective as of the closing of the exchange offer.

46. Will Air France obtain 100% of KLM's shares? Voting rights?

During a three-year transition period, Air France will own 100% of KLM's economic rights and 49% of KLM voting rights.

The remaining 51% KLM voting rights will be shared by two Dutch Foundations and the Dutch State to allow for the protection of traffic rights.

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47. Will the French State own any shares in KLM?

No, not directly. But by being a shareholder of Air France, the French State will become a shareholder of the enlarged group, which obviously includes KLM. The French State has, however, indicated publicly its intention to reduce its stake.

48. Will the Dutch State own any shares in Air France?

No, the State of the Netherlands will not hold any shares in Air France.

49. Will the Dutch government own any shares in KLM?

The Dutch State which currently owns 8.8 millions Cumulative Preference Shares A in KLM (representing 14.7% of total voting rights outstanding), will decrease its stake in a similar proportion to the French State in Air France-KLM over time.

The Dutch State will keep, for a three year period, an option allowing it to obtain 50.1% of KLM's voting rights if KLM's traffic rights are challenged because of the nationality of KLM shareholders.

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**Air France privatization**

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50. Why has the French Government not decided to privatize Air France through an offering of its shares?

As part of this transaction, it is expected that Air France will be privatized by dilution of the stake held by the French State. The French State's shareholding will decrease from 54% of Air France to 44% of the enlarged group (assuming all KLM common shares are tendered in the exchange offer but before exercise of the warrants) and would subsequently reach 39% after full exercise of the warrants.

The French State has publicly stated its intention to reduce its stake in Air France to a much lower level. The timing of any disposal will be subject to the decision of French government, depending on market conditions.

51. When is the French State planning to sell its remaining shares? Has a deadline been set with regard to KLM?

The French State has stated that it remains strongly committed to reducing its stake further. The timing of any disposal will be subject to the decision of French government, but in any event Air France should be effectively privatized upon completion of (and as a result of) the KLM share exchange offer.

No deadline has been set. Any disposal by the French State will continue to be subject to market conditions.

52. What will happen if Air France is not fully privatized in the end?

The privatization of Air France was decided by the French government in July 2002. Since that announcement, all the necessary legislative requirements have been met. We have no reason to believe that the French State will not fulfill its commitment provided that market conditions permit it.

53. Did KLM impose the condition that the French State reduce its stake in Air France to 20% or sell it completely?

The French State has publicly indicated its commitment to reduce its stake to 20% or less.

54. Can the French Government sell all or part of its stake between now and the completion of the share exchange offer?

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The French State remains strongly committed to reducing its stake further. As previously stated by the French government, the timing of any disposal will be subject to market conditions.

In any case, the French State has indicated that it does not intend its decision to hinder the Air France / KLM deal.

55. What will the Air France/KLM transaction cost the French Government? Or will the French State get any cash as part of the transaction?

The transaction will not cost the French Government anything but neither will it receive any cash. The only impact for the French State will be the dilution of its stake in Air France from 54% to 44% of the enlarged group (including KLM) (assuming full tender by KLM shareholders but before exercise of the warrants), as a result of the capital increase. The French State's stake will subsequently reach 39% if the warrants are fully exercised.

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