

2010

Consolidated Financial Statements
HSBC Bank Bermuda Limited

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HSBC BANK BERMUDA LIMITED

Independent Auditors' Report

To the Board of Directors and Shareholder of
HSBC Bank Bermuda Limited

We have audited the accompanying consolidated financial statements of HSBC Bank Bermuda Limited and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at 31 December 2010, and the consolidated income statement, and consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, where due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the consolidated financial statement present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2010, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.



Chartered Accountants
Hamilton, Bermuda
17 February 2011

**Consolidated Income Statement
for the year ended 31 December 2010**

	<i>Notes</i>	2010 US\$000	2009 US\$000
Interest income		251,569	255,578
Interest expense		(14,795)	(25,162)
Net interest income	3	236,774	230,416
Fee income		239,483	233,376
Fee expense		(22,035)	(21,679)
Net fee income	3	217,448	211,697
Dealing profits		30,262	34,629
Gains less losses from financial investments	12	5,312	3,102
Dividend income		543	889
Net earned insurance premiums	4	86,629	144,037
Other operating income		6,899	7,774
Total operating income		583,867	632,544
Net insurance claims and underwriting expenses incurred	5	(43,496)	(108,794)
Net operating income before loan impairment charges		540,371	523,750
Loan impairment charges	11	(10,757)	(6,059)
Net operating income		529,614	517,691
Employee compensation and benefits	6,7	(192,752)	(196,255)
General and administrative expenses		(98,814)	(88,228)
Depreciation and impairment of property, plant and equipment	14, 17	(16,879)	(12,332)
Total operating expenses		(308,445)	(296,815)
Operating profit		221,169	220,876
Gains less losses on disposal of property, plant and equipment and subsidiary investments	18	33,305	508
Share of loss in associates	16	(497)	(871)
Profit before tax		253,977	220,513
Tax expense	8	(6,947)	(18,018)
Profit for the year		247,030	202,495
Less: Profit from discontinued operations (net of income tax)	19	(26,701)	(19,685)
Profit for the year from continuing operations		220,329	182,810

The accompanying notes are an integral part of the Consolidated Financial Statements

**Consolidated Statement of Comprehensive Income
for the year ended 31 December 2010**

	<i>Notes</i>	2010 US\$000	2009 US\$000
Profit for the year		247,030	202,495
Other comprehensive (loss) income			
Available-for-sale valuation (losses) gains		(2,489)	161,548
Exchange differences arising from net investments in foreign operations		(26,008)	1,420
Actuarial (losses) gains on defined benefit plans	6	(7,643)	1,214
Other movements		5,945	3,246
Other comprehensive (loss) income for the year		(30,195)	167,428
Total comprehensive income for the year		216,835	369,923

The accompanying notes are an integral part of the Consolidated Financial Statements

**Consolidated Balance Sheet
at 31 December 2010**

	<i>Notes</i>	2010 US\$000	2009 US\$000
ASSETS			
Cash and balances at central banks		29,025	34,280
Items in the course of collection from other banks		522	41
Derivatives	9	7,922	11,105
Loans and advances to banks	10	4,890,172	3,647,066
Loans and advances to customers	11	3,237,846	3,055,878
Financial investments	12	3,055,509	3,273,663
Assets held for sale	19	266,916	15,110
Prepayments and accrued income		50,621	71,647
Deferred tax assets	8	67	234
Other assets	20	17,527	168,554
Interests in associates	16	1,743	2,240
Property, plant and equipment	14	237,619	237,689
Goodwill	15	51,342	239,893
Total assets		<u>11,846,831</u>	<u>10,757,400</u>
LIABILITIES AND EQUITY			
Liabilities			
Deposits by banks		34,519	125,732
Customer accounts		9,707,014	8,220,801
Items in the course of transmission to other banks		10,642	12,717
Derivatives	9	8,196	9,326
Liabilities held for sale	19	34,119	-
Liabilities under insurance contracts	20	-	344,672
Accruals and deferred income		63,495	89,468
Current tax liabilities		16,960	14,983
Deferred tax liabilities	8	-	33,921
Provisions	21	-	4,495
Other liabilities		37,324	49,346
Retirement benefit liabilities	6	51,497	41,878
Total liabilities		<u>9,963,766</u>	<u>8,947,339</u>
Equity			
Called up share capital	30	30,027	30,027
Share premium	30	388,652	388,652
Other reserves		43,982	74,763
Retained earnings		1,420,404	1,316,619
Total equity		<u>1,883,065</u>	<u>1,810,061</u>
Total liabilities and equity		<u>11,846,831</u>	<u>10,757,400</u>

The accompanying notes are an integral part of the Consolidated Financial Statements



John D. Campbell
Chairman



Philip M. Butterfield
Director

**Consolidated Statement of Cash Flows
for the year ended 31 December 2010**

	2010 US\$000	2009 US\$000
Cash flows from operating activities		
Profit (loss) before tax, interest and dividends	16,660	(10,792)
Interest received	242,522	266,711
Interest paid	(17,568)	(29,885)
Adjustments for:		
Non-cash items in profit (loss) before tax, interest and dividends	20,140	(1,741)
Change in loans and advances to customers	(181,968)	(542,363)
Change in net derivatives	2,053	(11,478)
Change in other operating assets	260,038	(30,158)
Change in deposits by banks	(91,213)	40,709
Change in customer accounts	1,486,213	296,627
Change in other operating liabilities	(16,517)	39,192
Net gain from investing activities	(35,241)	(13,462)
Tax paid	(5,266)	(8,784)
Net cash flows from (used in) operating activities	<u>1,679,853</u>	<u>(5,424)</u>
Cash flows from investing activities		
Dividends received	543	889
Purchase of financial investments	(1,167,716)	(786,405)
Proceeds from the sale and maturity of financial investments	820,545	1,008,942
Purchase of property, plant and equipment	(21,268)	(42,959)
Proceeds from the sale of property, plant and equipment	5,759	3,602
Net cash inflow from disposal of subsidiaries	336,226	-
Change in assets held for sale	(251,806)	-
Change to interest in associates	-	(3,000)
Net cash flows (used in) from investing activities	<u>(277,717)</u>	<u>181,069</u>
Cash flows from financing activities		
Dividends paid	(140,300)	(144,000)
Net cash flows used in financing activities	<u>(140,300)</u>	<u>(144,000)</u>
Net increase in cash and cash equivalents	1,261,836	31,645
Cash and cash equivalents at the beginning of the year	3,668,670	3,683,442
Effect of exchange rate changes on cash and cash equivalents	(21,429)	(46,417)
Cash and cash equivalents at the end of the year	<u>4,909,077</u>	<u>3,668,670</u>
Cash and cash equivalents comprise		
Cash and balances at central banks	29,025	34,280
Items in the course of collection from other banks	522	41
Loans and advances to banks	4,890,172	3,647,066
Items in the course of transmission to other banks	(10,642)	(12,717)
Total cash and cash equivalents	<u>4,909,077</u>	<u>3,668,670</u>

The accompanying notes are an integral part of the Consolidated Financial Statements

Consolidated Statement of Changes in Equity
for the year ended 31 December 2010
(In US dollar thousands)

	Called up share capital	Share premium	Other reserves				Retained earnings	Total equity
			Available- for-sale fair value reserve	Foreign exchange reserve	Share based payment reserve	Other reserves		
At 1 January 2009	30,027	388,652	(118,367)	25,235	13,455	121	1,253,604	1,592,727
Comprehensive income, net of income tax								
Profit for the year	-	-	-	-	-	-	202,495	202,495
Available-for-sale valuation gains	-	-	161,548	-	-	-	-	161,548
Exchange differences arising from net investments in foreign operations	-	-	-	1,420	-	-	-	1,420
Actuarial gains on defined benefit plans	-	-	-	-	-	-	1,214	1,214
Other movements	-	-	-	-	-	(60)	3,306	3,246
Total comprehensive income, net of income tax	-	-	161,548	1,420	-	(60)	207,015	369,923
Transactions with the shareholder recorded directly in equity								
Dividends	-	-	-	-	-	-	(144,000)	(144,000)
Share based plan movements	-	-	-	-	(8,589)	-	-	(8,589)
Total transactions with the shareholder recorded directly in equity	-	-	-	-	(8,589)	-	(144,000)	(152,589)
At 31 December 2009	30,027	388,652	43,181	26,655	4,866	61	1,316,619	1,810,061
Comprehensive income, net of income tax								
Profit for the year	-	-	-	-	-	-	247,030	247,030
Available-for-sale valuation losses	-	-	(2,489)	-	-	-	-	(2,489)
Exchange differences arising from net investments in foreign operations	-	-	-	(26,008)	-	-	-	(26,008)
Actuarial losses on defined benefit plans	-	-	-	-	-	-	(7,643)	(7,643)
Other movements	-	-	-	-	-	1,247	4,698	5,945
Total comprehensive income, net of income tax	-	-	(2,489)	(26,008)	-	1,247	244,085	216,835
Transactions with the shareholder recorded directly in equity								
Dividends	-	-	-	-	-	-	(140,300)	(140,300)
Share based plan movements	-	-	-	-	(3,531)	-	-	(3,531)
Total transactions with the shareholder recorded directly in equity	-	-	-	-	(3,531)	-	(140,300)	(143,831)
At 31 December 2010	30,027	388,652	40,692	647	1,335	1,308	1,420,404	1,883,065

The accompanying notes are an integral part of the Consolidated Financial Statements

Notes on the Consolidated Financial Statements

(In US dollar thousands)

31 December 2010

1 Basis of preparation**(a) General**

Effective 3 May 2010, The Bank of Bermuda Limited changed its legal name to HSBC Bank Bermuda Limited. HSBC Bank Bermuda Limited (the 'Bank') was established in 1889 and incorporated in 1891. The address of its registered office is 6 Front Street, Hamilton HM11, Bermuda. The consolidated financial statements of the Bank for the year ended 31 December 2010 comprise the Bank and its subsidiaries (together referred to as the 'group') and the group's interests in associates. The Bank is domiciled in Bermuda and provides retail and corporate banking, investment, trust, custody and fund administration services to international and local clients. The immediate parent company of the Bank is HSBC Asia Holdings BV. The ultimate parent company is HSBC Holdings plc ('HSBC'). Copies of the financial statements of HSBC Holdings plc may be obtained from its registered office at 8 Canada Square, London, England, E14 5HQ, or from the HSBC website, www.hsbc.com.

These consolidated financial statements are authorised for issue by the Board of Directors on 17 February 2011.

The consolidated financial statements are presented in US dollars, which is the presentational currency of the group. The functional currency of the group is primarily Bermuda dollars. Bermuda dollars are translated into US dollars at par. All amounts and figures are rounded to the nearest thousand, except where explicitly stated.

The group has prepared its consolidated financial statements in accordance with International Financial Reporting Standards ('IFRSs'). IFRSs comprise accounting standards issued by the International Accounting Standards Board ('IASB') and its predecessor body, as well as interpretations issued by the International Financial Reporting Interpretations Committee ('IFRIC') and its predecessor body.

Certain reclassifications have been made to the 2009 comparative financial information in order to conform to the current year presentation.

These consolidated financial statements are presented in accordance with IAS 1 'Presentation of Financial Statements'. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of the group's net income, financial position and cash flows for the years ended 31 December 2010 and 31 December 2009 have been made. In accordance with IFRS 8 'Operating Segments', no segment information has been presented as the shares of the group are not publicly traded.

During 2010, the group adopted the revised IFRS 3 'Business Combinations' and amendments to IAS 27 'Consolidated and Separate Financial Statements'. The main changes under the standards are that:

- acquisition-related costs are recognised as an expense in the consolidated income statement in the period in which they are incurred;
- all consideration transferred, including contingent consideration, is recognised and measured at fair value at the acquisition date;
- equity interests held prior to control being obtained are remeasured to fair value at the date of obtaining control, and any gain or loss is recognised in the consolidated income statement;
- an option is available, on a transaction-by-transaction basis, to measure any non-controlling (previously referred to as minority) interests in the entity acquired either at fair value, or at the non-controlling interests' proportionate share of the net identifiable assets of the entity acquired; and
- changes in a parent's ownership interest in a subsidiary that do not result in a change of control are treated as transactions between equity holders and are reported in equity.

In terms of their application to the group, the revised IFRS 3 and the amendments to IAS 27 apply prospectively to acquisitions and transactions taking place on or after 1 January 2010, and have no significant effect on these consolidated financial statements.

During 2010, in the addition to the above, the group adopted a number of standards, interpretations and amendments thereto which had an insignificant effect on the consolidated financial statements.

(b) Basis of consolidation

Entities that are controlled by the Bank are consolidated. Subsidiaries are consolidated from the date the group gains control, until the date that control ceases. The acquisition method of accounting is used when subsidiaries are acquired. The cost of an acquisition is measured at the fair value of the consideration, including contingent consideration, given at the date of exchange. Acquisition-related costs are recognised as an expense in the consolidated income statement in the period in which they are incurred. The acquired identifiable assets, liabilities and contingent liabilities are measured at their fair values at the date of acquisition. Goodwill is measured as the excess of the aggregation of the consideration transferred, the amount of non-controlling interest and the fair value of the acquirer's previously held equity interest, if any, over the net of the amounts of the identifiable assets acquired and the liabilities assumed. The amount of non-controlling interest is measured either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets. In a business combination achieved in stages, the previously held equity interest is remeasured at the acquisition-date fair value with resulting gain or loss recognised in the consolidated income statement or other comprehensive income as appropriate. In the event that the fair value of net assets acquired is in excess of the aggregation of the consideration transferred, the amount of non-controlling interest and the fair value of the previously held equity interest, the difference is recognised immediately in the consolidated income statement.

All intra-group transactions are eliminated on consolidation. The consolidated financial statements of the group include the attributable share of the results of any interests in associates.

(c) Use of estimates and assumptions

The preparation of financial information requires the use of estimates and assumptions about future conditions. The use of available information and the application of judgement are inherent in the formation of estimates; actual results in the future may differ from estimates upon which financial information is prepared. Management believes that the critical accounting policies where judgement is necessarily applied are those which relate to impairment of loans and advances, goodwill impairment, liabilities under insurance contracts issued, the valuation of financial instruments, the impairment of available-for-sale financial assets and deferred tax assets.

Further information about key assumptions concerning the future, and other key sources of estimation uncertainty, are set out in these notes on the consolidated financial statements.

(d) Future accounting developments – Standards and Interpretations issued by the IASB*(i) IFRS 9 'Financial Instruments'*

In November 2009, the IASB issued IFRS 9 'Financial Instruments' ('IFRS 9'). This introduced new requirements for the classification and measurement of financial assets. In October 2010, the IASB issued additions to IFRS 9 dealing with financial liabilities. These represent the first instalments in the IASB's planned phased replacement of IAS 39 'Financial Instruments: Recognition and Measurement' ('IAS 39') with a less complex and improved standard for financial instruments.

The standard is effective for annual periods beginning on or after 1 January 2013 with early adoption permitted. IFRS 9 is required to be applied retrospectively. If the standard is adopted prior to 1 January 2012, an entity will be exempt from the requirement to restate prior period comparative information.

The main changes to the requirements of IAS 39 are summarised below:

- All financial assets that are currently in the scope of IAS 39 will be classified as either amortised cost or fair value. The available-for-sale, held-to-maturity and loans and receivables categories will no longer exist.
- Classification is based on an entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. Reclassifications between the two categories are prohibited unless there is a change in the entity's business model.
- A financial asset is measured at amortised cost if two criteria are met: i) the objective of the business model is to hold the financial asset for the collection of the contractual cash flows; and ii) the contractual cash flows of the instrument are solely payments of principal and interest on the principal outstanding. All other financial assets are measured at fair value. Movements in the fair value of financial assets classified at fair value are recognised in profit or loss, except for equity investments where an entity takes the option to designate an equity instrument that is not held for trading at fair value through other comprehensive income. If this option is taken, all subsequent changes in fair value are recognised in other comprehensive income with no recycling of gains or losses to the consolidated income statement. Dividend income would continue to be recognised in the consolidated income statement.
- An entity is only permitted to designate a financial asset otherwise meeting the amortised cost criteria at fair value through profit or loss if doing so significantly reduces or eliminates an accounting mismatch. This designation is made on initial recognition and is irrevocable.

- Financial assets which contain embedded derivatives are to be classified in their entirety either at fair value or amortised cost depending on whether the contracts as a whole meet the relevant criteria under IFRS 9.
- Most of IAS 39's requirements for financial liabilities are retained, including amortised cost accounting for most financial liabilities with bifurcation of embedded derivatives. However, fair value changes attributable to changes in own credit risk for financial liabilities designated under the fair value option other than loan commitments and financial guarantee contracts are to be presented in the consolidated statement of other comprehensive income. These amounts are not subsequently reclassified to the consolidated income statement, but may be transferred within equity.

The next steps in the IASB's project will address the impairment of financial assets measured at amortised cost and hedge accounting. The IASB has indicated that it aims to finalise the replacement of IAS 39 by June 2011. In addition, the IASB is working with the US Financial Accounting Standards Board to reduce inconsistencies between US GAAP and IFRS in accounting for financial instruments. The impact of IFRS 9 may change as a consequence of further developments resulting from the IASB's financial instruments project. As a result, it is impracticable to quantify the impact of IFRS 9 as at the date of publication of these financial statements.

(ii) Revised IAS 24 'Related Party Disclosures'

The IASB issued a revised IAS 24 'Related Party Disclosures' which is effective for annual periods beginning on or after 1 January 2011. The revised standard has an objective of removing complexity in the definition of related party including removing perceived inconsistencies. The new standard may require the collection and disclosure of additional information. The group is currently assessing the effect of this new standard.

2 Significant accounting policies

(a) Interest income and expense

Interest income and expense for all interest-bearing financial instruments is recognised in 'Interest income' and 'Interest expense' in the consolidated income statement using the effective interest rates of the financial assets or financial liabilities to which they relate.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the group estimates cash flows considering all contractual terms of the financial instrument but not future credit losses. The calculation includes all amounts paid or received by the group that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

Interest on impaired financial assets is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(b) Non-interest income

(i) Fee income

Fee income is earned from a diverse range of services provided by the group to its customers. Fee income is accounted for as follows:

- income earned on the execution of a significant act is recognised as revenue when the act is completed (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third-party, such as the arrangement for the acquisition of shares or other securities);
- income earned from the provision of services is recognised as revenue as the services are provided (for example, asset management, portfolio and other management advisory and service fees); and
- income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate (for example, certain loan commitment fees) and is recorded in 'Interest income' (Note 2a).

(ii) Dealing profits

Dealing profits comprise exchange differences on translation of monetary assets and liabilities denominated in foreign currencies and commissions earned on foreign exchange trading transactions. Dealing profits also include gains and losses from changes in the fair value of derivatives that do not qualify for hedge accounting.

(iii) Dividend income

Dividend income is recognised net of withholding taxes when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders have approved the dividend for unlisted equity securities.

(c) Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months maturity from the date of acquisition, and include cash and balances at central banks, loans and advances to banks and items in the course of collection from or in transmission to other banks.

(d) Loans and advances to banks and customers

Loans and advances to banks and customers include loans and advances originated by the group, which are not intended to be sold in the short term and have not been classified either as held for trading or designated at fair value through profit and loss. Loans and advances are recognised when cash is advanced to borrowers. They are initially recorded at fair value plus any net directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment losses.

When the group purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date ("reverse repo" or "stock borrowing"), the arrangement is accounted for as a loan or advance, and the underlying asset is not recognised in the group's consolidated financial statements.

(e) Impairment of loans and advances

Losses for impaired loans are recognised when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Impairment allowances are calculated on individual loans and on groups of loans assessed collectively. Impairment losses are recorded as charges to the consolidated income statement. The carrying amount of impaired loans on the consolidated balance sheet is reduced through the use of impairment allowance accounts. Losses expected from future events are not recognised.

(i) Individually assessed loans and advances

For all loans that are considered individually significant, the group assesses, on a case-by-case basis at each balance sheet date, whether there is any objective evidence that a loan is impaired. The criteria used by the group to determine that there is such objective evidence include:

- known cash flow difficulties experienced by the borrower;
- past due contractual payments of either principal or interest;
- breach of loan covenants or conditions;
- the probability that the borrower will enter bankruptcy or other financial realisation; and
- a significant downgrading in credit rating by an external credit rating agency.

For those loans where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- the group's aggregate exposure to the customer;
- the viability of the customer's business model and capability to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- the amount and timing of expected receipts and recoveries;
- the likely dividend available on liquidation or bankruptcy;
- the extent of other creditors' commitments ranking ahead of, or *pari passu* with, the group and the likelihood of other creditors continuing to support the customer;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other collateral) and likelihood of successful repossession;
- the likely deduction of any costs involved in recovery of amounts outstanding;
- the ability of the borrower to obtain and make payments in the relevant currency if loans are not in local currency; and
- when available, the secondary market price for the debt.

(In US dollar thousands)

31 December 2010

Impairment losses are calculated by discounting the expected future cash flows of a loan at its original effective interest rate, and comparing the resultant present value with the loan's current carrying amount. The impairment allowances on individually significant accounts are reviewed at least semi-annually, and more regularly when circumstances require. This normally encompasses re-assessment of the enforceability of any collateral held and of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

(ii) Collectively assessed loans and advances

Impairment is assessed on a collective basis in two circumstances:

- to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment; and
- for homogeneous groups of loans that are not considered individually significant.

Incurred but not yet identified impairment

Where loans have been individually assessed and no evidence of loss has been identified, these loans are grouped together on the basis of similar credit risk characteristics for the purpose of calculating a collective impairment loss. This loss arises from individual loan impairment at the balance sheet date, which will only be identified in the future.

The collective impairment loss is determined after taking into account:

- historical loss experience in portfolios of similar credit risk characteristics (for example, by industry sector, loan grade or product);
- the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate allowance against the individual loan; and
- management's experienced judgement as to whether current economic and credit conditions are such that the actual level of inherent losses at the balance sheet date is likely to be greater or less than that suggested by historical experience.

The period between a loss occurring and its identification is estimated by local management for each identified portfolio.

Homogeneous groups of loans and advances

For homogeneous groups of loans that are not considered individually significant, allowances are determined on a portfolio basis. Statistical methods are used to determine impairment losses on a collective basis for homogeneous groups of loans that are not considered individually significant, because individual loan assessment is impracticable. Losses in these groups of loans are recorded on an individual basis when individual loans are written off, at which point they are removed from the group.

- The methodology applied is a statistical analysis of historical trends of the probability of default and amount of consequential loss following default. The amount of loss is based on the present value of expected future cash flows. Other historical data and an evaluation of current economic conditions are also considered to calculate the appropriate level of allowance to cover inherent loss.
- Loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

(iii) Write-off of loans and advances

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write off may be earlier.

(iv) Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was initially recognised, the excess is written back by reducing the loan impairment allowance account accordingly. The write-back is recognised in the consolidated income statement.

Notes on the Consolidated Financial Statements (continued)

(In US dollar thousands)

31 December 2010

(v) Assets acquired in exchange for loans

Non-financial assets acquired in exchange for loans in order to achieve an orderly realisation are recorded as assets 'held for sale' and no depreciation is provided in respect of these assets. Assets acquired are recorded at fair value less estimated disposal costs at the date of exchange. Any subsequent decrease in the fair value of the acquired assets is recorded as an impairment loss and included in the consolidated income statement. Any subsequent increase in the fair value of the acquired assets, to the extent this does not exceed the cumulative impairment loss, is recognised in the consolidated income statement.

(vi) Renegotiated loans

Loans subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up to date loans for measurement purposes once the minimum number of payments required under the new arrangements have been received. These renegotiated loans are segregated from other parts of the loan portfolio for the purposes of collective impairment assessment, to reflect their risk profile. Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired or should be considered past due. The carrying amount of loans that have been classified as renegotiated retain this classification until maturity or derecognition.

(f) Financial investments

Debt securities and equity securities intended to be held on a continuing basis are classified as 'available-for-sale' securities. Financial investments are recognised on the trade date when the group enters into contractual arrangements with counterparties to purchase securities, and are normally derecognised when either the securities are sold or the borrowers repay their obligations.

Available-for-sale financial assets are initially measured at fair value plus directly attributable transaction costs. They are subsequently remeasured at fair value, and changes therein are recognised in other comprehensive income in the 'Available-for-sale fair value reserve', until the financial assets are either sold or become impaired. When available-for-sale financial assets are sold, cumulative unrealised gains or losses previously recognised in other comprehensive income are recognised in the consolidated income statement as 'Gains less losses from financial investments'.

Interest income is recognised on available-for-sale debt securities using the effective interest method, calculated over the asset's expected life. Premiums and/or discounts arising on the purchase of fixed maturity investment securities are included in the calculation of their effective interest rates. Dividends are recognised in the consolidated income statement when the right to receive payment has been established.

At each balance sheet date an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If the available-for-sale financial asset is impaired, the difference between the financial asset's acquisition cost (net of any principal repayments and amortisation) and the current fair value, less any previous impairment loss recognised in the consolidated income statement, is removed from other comprehensive income and recognised in the consolidated income statement.

Impairment losses for available-for-sale securities are recognised within 'Gains less losses from financial investments' in the consolidated income statement.

Once an impairment loss has been recognised on an available-for-sale financial asset, the subsequent accounting treatment for changes in the fair value of that asset differs depending on the nature of the available-for-sale financial asset concerned:

- For an available-for-sale debt security, a subsequent decline in the fair value of the instrument is recognised in the consolidated income statement when there is further objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised in other comprehensive income. If the fair value of a debt security increases in a subsequent period, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated income statement, the impairment loss is reversed through the consolidated income statement up to the amount of the impairment loss previously recognised in the consolidated income statement;

- For an available-for-sale equity security, all subsequent increases in the fair value of the instrument are treated as a revaluation and are recognised in other comprehensive income. Impairment losses recognised on the equity security are not reversed through the consolidated income statement. Subsequent decreases in the fair value of the available-for-sale equity security are recognised in the consolidated income statement, to the extent that further cumulative impairment losses have been incurred in relation to the acquisition cost of the equity security.

(g) Determination of fair value

For available-for-sale securities that are quoted in active markets, fair values are determined by reference to the current quoted bid prices. Where independent prices are not available, fair values may be determined using valuation techniques with reference to observable market data. These include comparison to similar instruments where market observable prices exist, discounted cash flow analysis and other valuation techniques commonly used by market participants. Fair values of financial instruments may be determined in whole or in part using valuation techniques based on assumptions that are not supported by prices from current market transactions or observable market data, where current prices or observable market data are not available.

A three level fair value hierarchy, which reflects the significance of observable market inputs, is used when estimating fair values:

- *Level 1 - quoted market price*: financial instruments with quoted prices for identical instruments in active markets.
- *Level 2 - valuation technique using observable inputs*: financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- *Level 3 - valuation technique with significant unobservable inputs*: financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

(h) Securities lending and borrowing

Securities lending and borrowing transactions are generally secured, with collateral taking the form of securities or cash advanced or received. The transfer of the securities to counterparties is not normally reflected on the consolidated balance sheet. Cash collateral advanced or received is recorded as an asset or a liability respectively.

(i) Derivatives and hedge accounting

Derivatives are recognised at fair value on the consolidated balance sheet. All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative.

The method of recognising the resulting fair value gains or losses depends on whether the derivative is held for trading or is designated as a hedging instrument and, if so, the nature of the risk being hedged. All gains and losses from changes in the fair value of derivatives held for trading are recognised in the consolidated income statement.

Where derivatives are designated as hedges, the group classifies them as either: (i) hedges of the change in fair value of recognised assets or liabilities or firm commitments ('fair value hedge'); or (ii) hedges of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction ('cash flow hedge'). Hedge accounting is applied to derivatives designated as hedging instruments in a fair value or cash flow hedge provided certain criteria are met.

(j) Derecognition of financial assets and financial liabilities

Financial assets are derecognised when the contractual right to receive cash flows from the assets has expired; or when the group has transferred its contractual right to receive the cash flows of the financial assets, and either:

- substantially all the risks and rewards of ownership have been transferred; or
- the group has neither retained nor transferred substantially all the risks and rewards, but has not retained control.

Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, is cancelled, or expires.

(k) Offsetting financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount reported in the consolidated balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(In US dollar thousands)

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(l) Subsidiaries and associates

The group classifies investments in entities which it controls as subsidiaries.

Interests in associates, which include entities the group has significant influence over but are not subsidiaries, are recognised using the equity method. Under this method, such investments are initially stated at cost, including attributable goodwill, and adjusted thereafter for the post-acquisition change in the group's share of net assets.

Profits on transactions between the group and its associates are eliminated to the extent of the group's interests in the associates. Losses are also eliminated to the extent of the group's interests in the associates unless the transaction provides evidence of an impairment of the asset transferred.

(m) Property, plant and equipment

Land and buildings are stated at historical cost except land and buildings held at 1 March 2004, the date of transition to IFRSs. The cost of these land and buildings is the fair value at the transition date. Depreciation is calculated using the straight-line method to write off the cost less residual value of the assets over the estimated useful lives as follows:

Freehold land	not depreciated
Buildings	lesser of 40 years or the remaining useful lives
Leasehold improvements	lesser of life of the lease or the remaining useful lives
Equipment, fixtures and fittings	3 – 7 years

Property, plant and equipment are subject to impairment review if there are events or changes in circumstances indicating that the carrying amounts may not be recoverable.

(n) Goodwill

Goodwill that arises from business combinations is measured as described in Note 1 (b).

Goodwill is tested annually for impairment, is carried at cost less accumulated impairment losses and is subject to impairment review if there are events or changes in circumstances indicating that the carrying amounts may not be recoverable. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold. Goodwill on the acquisition of associates is included in 'Interests in associates'. At the date of disposal of a business, attributable goodwill is included in the group's share of net assets in the calculation of the gain or loss on disposal.

(o) Finance and operating leases

Agreements which transfer to counterparties substantially all the risks and rewards incidental to the ownership of assets, but not necessarily legal title, are classified as finance leases. When the group is a lessee under finance leases, the leased assets are capitalised and included in 'Property, plant and equipment' and the corresponding liability to the lessor is included in 'Other liabilities'. A finance lease and its corresponding liability are recognised initially at the fair value of the asset or, if lower, the present value of the minimum lease payments.

All other leases are classified as operating leases. When acting as lessor, the group includes the assets subject to operating leases in 'Property, plant and equipment' and accounts for them accordingly. Impairment losses are recognised to the extent that residual values are not fully recoverable and the carrying value of the assets are thereby impaired. When the group is the lessee, leased assets are not recognised on the consolidated balance sheet. Rentals payable and receivable under operating leases are accounted for on a straight-line basis over the periods of the leases and are included in 'General and administrative expenses' and 'Other operating income', respectively.

(p) Income tax

Income tax on the profit or loss for the year comprises current tax and deferred tax. Income tax is recognised in the consolidated income statement except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case it is also recognised in the same statement in which the related item appears.

(In US dollar thousands)

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Current tax is the tax expected to be payable on the taxable profit for the year, calculated using tax rates enacted or substantially enacted by the balance sheet date, and any adjustment to tax payable in respect of previous years. Current tax assets and liabilities are offset when the group intends to settle on a net basis and the legal right to offset exists.

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the consolidated balance sheet and the amount attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled. Deferred tax assets and liabilities are offset when they arise in the same tax reporting group, relate to income taxes levied by the same taxation authority and a legal right to offset exists in the group.

(q) Pension and other post-employment benefits

The group operates defined contribution pension plans and defined benefit pension plans, as well as a post-employment healthcare benefits plan.

(i) Defined contribution pension plans

Payments to the defined contribution pension plans are charged as an expense as they fall due. The group has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

(ii) Defined benefit pension plans

The costs recognised for funding defined benefit pension plans are determined using the Projected Unit Credit Method, with annual actuarial valuations performed on each plan. Actuarial differences that arise are recognised directly in retained earnings and presented in the consolidated statement of comprehensive income in the period they arise. Past service costs are recognised immediately to the extent the benefits are vested, and are otherwise recognised on a straight-line basis over the average service period until the benefits vest. The current service costs and any past service costs together with the expected return on plan assets less the unwinding of the discount on the plan liabilities are charged to operating expenses under 'Employee compensation and benefits'. Actuarial gains and losses on defined benefit plans are recognised in other comprehensive income in the period in which they arise.

The net defined benefit pension liability recognised in the consolidated balance sheet represents the present value of the defined benefit obligations adjusted for unrecognised past service costs and reduced by the fair value of plan assets. Any resulting asset from this is limited to unrecognised past service costs plus the present value of available refunds and reductions in future contributions to the plan.

(iii) Post-employment healthcare benefits plan

The costs of providing other post-employment benefits such as post-employment healthcare are accounted for on the same basis as defined benefit pension plans.

(r) Share-based payments

The cost of share-based payment arrangements with employees is measured by reference to the fair value of equity instruments on the date they are granted, and recognised as an expense on a straight-line basis over the vesting period, with a corresponding credit to the 'Share-based payment reserve' in equity. The vesting period is the period during which all the specified vesting conditions of a share-based payment arrangement are to be satisfied. The fair value of equity instruments that are made available immediately, with no vesting period attached to the award, are expensed immediately.

Fair value is determined using appropriate valuation models, taking into account the terms and conditions upon which the equity instruments were granted. Vesting conditions include service conditions and performance conditions; any other features of a share-based payment arrangement are non-vesting conditions. Market performance conditions and non-vesting conditions are taken into account when estimating the fair value of equity instruments at the date of grant, so that an award is treated as vesting irrespective of whether the market performance condition or non-vesting condition is satisfied, provided all other conditions are satisfied.

Vesting conditions, other than market performance conditions, are not taken into account in the initial estimate of the fair value at the grant date. They are taken into account by adjusting the number of equity instruments included in the measurement of the transaction, so that the amount recognised for services received as consideration for the equity instruments granted shall be based on the estimated number of equity instruments that eventually vest. On a cumulative basis, no expense is recognised for equity instruments that do not vest because of a failure to satisfy non-market performance or service conditions.

Where an award has been modified, as a minimum the expense of the original award continues to be recognised as if it had not been modified. Where the effect of a modification is to increase the fair value of an award or increase the number of equity instruments, the incremental fair value of the award or incremental fair value of the extra equity instruments is recognised in addition to the expense of the original grant, measured at the date of modification, over the modified vesting period.

A cancellation that occurs during the vesting period is treated as an acceleration of vesting, and recognised immediately for the amount that would otherwise have been recognised for services over the vesting period.

(s) Foreign currencies

(i) Transactions and balances

Transactions in foreign currencies are recorded in the functional currency at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the balance sheet date. Any resulting exchange differences are included in the consolidated income statement. Non-monetary assets and liabilities that are measured at historical cost in a foreign currency are translated into the functional currency using the rate of exchange at the date of the initial transaction. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined. Any exchange component of a gain or loss on a non-monetary item is recognised directly in other comprehensive income if the gain or loss on the non-monetary item is recognised directly in other comprehensive income. Any exchange component of a gain or loss on a non-monetary item is recognised directly in the consolidated income statement if the gain or loss on the non-monetary item is recognised in the consolidated income statement.

(ii) Group entities

The results and financial positions of all group entities (none of which has the currency of a hyperinflationary economy) that have functional currencies different from the presentation currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated using exchange rates at the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are recognised in the 'Foreign exchange reserve' in other comprehensive income. When a foreign operation is sold, such exchange differences are recognised in the consolidated income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

(t) Customer accounts

Customer accounts are initially measured at fair value plus transaction costs, and subsequently measured at their amortised cost using the effective interest method.

(u) Provisions

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a current legal or constructive obligation as a result of past events, and for which a reliable estimate can be made of the amount of the obligation.

(v) Insurance contracts

Through its insurance subsidiaries (the 'insurer'), the group issues contracts to affiliates that contain insurance risk, financial risk or a combination thereof. An insurance contract is defined as a contract under which the insurer accepts significant insurance risk from another party, by agreeing to compensate that party on the occurrence of a specified uncertain future event. An insurance contract may also transfer financial risk, but is accounted for as an insurance contract if the insurance risk is significant.

Insurance contracts are accounted for as follows:

(i) Premiums

Gross insurance premiums for general insurance business are reported as income over the term of the insurance contract attributable to the risks borne during the accounting period. The unearned premium or the proportion of the business underwritten in the accounting period relating to the period of risk after the balance sheet date is calculated on a daily or monthly pro rata basis.

Reinsurance premiums are accounted for in the same accounting period as the premiums for the direct insurance to which they relate.

(ii) Claims and reinsurance recoveries

Gross insurance claims for general insurance business include paid claims and movements in outstanding claims reserves. The outstanding claims reserves are based on the estimated ultimate cost of all claims that have occurred but not settled at the balance sheet date, whether reported or not, together with related claims handling costs. Reserves for claims incurred but not reported ('IBNR') are adjusted annually based on actuarial valuations, using appropriate statistical techniques.

The benefits to which the group is entitled under its reinsurance contracts held are recognised as reinsurance assets. Amounts recoverable from or due to reinsurers are measured consistently with the reinsured insurance contracts and with the terms of each reinsurance contract. Reinsurance recoveries are accounted for in the same period as the related claim.

(iii) Liabilities under insurance contracts

Outstanding claims liabilities for non-life insurance contracts are based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claim-handling costs and a reduction for the expected value of salvage and other recoveries. Liabilities for claims incurred but not reported are made on an estimated basis, using appropriate statistical techniques.

(w) Fiduciary activities

The group commonly acts as trustee and in other fiduciary capacities resulting in the holding or placing of assets on behalf of individuals, trusts, post-employment benefit plans and other institutions. The assets and liabilities and income and expenditure arising from these assets and liabilities are excluded from the consolidated financial statements, as they are not assets of the group. The group earns a fee for acting in these capacities.

(x) Financial guarantee contracts

Liabilities under financial guarantee contracts which are not classified as insurance contracts are recorded initially at their fair value which is generally the fee received or receivable and is amortised over the life of the contract. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations. Financial guarantee contracts are included in 'Other liabilities'.

(y) Trading assets and liabilities

Treasury bills, debt securities, equity securities, loans, deposits, debt securities in issue, and short positions in securities are classified as held for trading if they have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. These financial assets or financial liabilities are recognised on trade date, when the group enters into contractual arrangements with counterparties to purchase or sell the financial instruments, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the consolidated income statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in the consolidated income statement in 'Dealing profits'.

(In US dollar thousands)

31 December 2010

3 Net interest income and net fee income

(a) Analysis of net interest income is as follows:

	2010	2009
Interest income		
Financial investments	67,655	85,501
Loans and advances to banks	15,095	18,844
Loans and advances to customers	168,819	151,233
	<u>251,569</u>	<u>255,578</u>
Interest expense		
Deposits by banks	(276)	(1,679)
Customer accounts	(14,519)	(23,483)
	<u>(14,795)</u>	<u>(25,162)</u>
Net interest income	<u>236,774</u>	<u>230,416</u>

(b) Analysis of net fee income is as follows:

	2010	2009
Custody and fund administration fees	21,171	38,090
Trust fees	104,564	93,219
Banking fees	39,322	33,111
Management fees	40,409	40,082
Other fees	34,017	28,874
Fee income	<u>239,483</u>	<u>233,376</u>
Fee expense	<u>(22,035)</u>	<u>(21,679)</u>
Net fee income	<u>217,448</u>	<u>211,697</u>

4 Net earned insurance premiums

Analysis of net earned insurance premiums is as follows:

	2010	2009
Gross written insurance premiums	48,846	176,632
Movement in unearned insurance premiums	43,212	(23,401)
Gross earned insurance premiums	<u>92,058</u>	<u>153,231</u>
Gross written insurance premiums ceded to reinsurers	(2,487)	(11,225)
Reinsurers' share of movement in unearned premiums	(2,942)	2,031
Reinsurers' share of gross earned premiums	<u>(5,429)</u>	<u>(9,194)</u>
Net earned insurance premiums	<u>86,629</u>	<u>144,037</u>

All net earned insurance premiums in 2010 and 2009 relate to HSBC Insurance (Bermuda) Limited ('the Captive') which was disposed of effective 1 July 2010 as disclosed in Note 18.

5 Net insurance claims and underwriting expenses incurred

The analysis of net insurance claims and underwriting expenses incurred is as follows:

	2010		
	Gross	Reinsurance	Net
Non-life insurance			
Current period claims reported	(44,422)	-	(44,422)
Previous periods claims reported	20,405	(15)	20,390
Current period claims paid	(8,785)	-	(8,785)
Previous periods claims paid	(7,620)	-	(7,620)
Underwriting expenses	(3,059)	-	(3,059)
Total insurance claims and underwriting expenses incurred	(43,481)	(15)	(43,496)
	2009		
	Gross	Reinsurance	Net
Non-life insurance			
Current period claims reported	(27,560)	84	(27,476)
Previous periods claims reported	(49,299)	(85)	(49,384)
Current period claims paid	(11,565)	-	(11,565)
Previous periods claims paid	(12,074)	-	(12,074)
Underwriting expenses	(8,295)	-	(8,295)
Total insurance claims and underwriting expenses incurred	(108,793)	(1)	(108,794)

All net insurance claims and underwriting expenses incurred in 2010 and 2009 relate to insurance operations which have been disposed of during the year as disclosed in Note 18.

(In US dollar thousands)

31 December 2010

6 Employee compensation and benefits

Post-employment benefit plans

Income statement charge

	2010	2009
Defined contribution pension plans	10,282	10,780
Defined benefit pension plans	549	261
Post-employment healthcare benefits plan	3,973	3,324
Total post-employment benefit income statement charge	<u>14,804</u>	<u>14,365</u>

(a) Defined contribution pension plans

The group provides non-contributory defined contribution pension plans to its employees in Bermuda and in the majority of its locations. Employees are able to make additional voluntary payments to the defined contribution pension plans.

The group's expense for the defined contribution pension plans in 2010 was \$10,282 (2009: \$10,780), of which \$8,005 (2009: \$8,168) relates to the Bermuda-based plan.

(b) Defined benefit pension plans

HSBC has a funded defined benefit pension plan for certain of its employees in Europe, known as the 'Sterling area' plan. This plan is divided into four regional subsets, namely Isle of Man, Guernsey, Jersey and a fourth subset covering international managers ('Plan B').

The group continues to assume responsibility for the entire Plan B which consists of fourteen individuals (2009: fourteen) and of thirty four individuals (2009: thirty four) previously employed by the Bank of Bermuda (Isle of Man) Limited. The net deficit obligation at 31 December 2010 and 31 December 2009 relates only to the components of the plan over which the group maintains current and future legal responsibility.

The group also has an interest in a funded defined benefit plan relating to four individuals (2009: four) in the Cayman Islands, known as the 'Samuel Montagu Jersey Pension Plan'.

Plan B and the Samuel Montagu Jersey Pension Plan are both closed plans not subject to new membership from current employees.

Actuarial valuation of the assets and liabilities of the group's defined benefit pension plans are carried out annually to determine its financial position and to ensure that benefit obligations are adequately funded. The group's pension expense for the defined benefit pension plans in 2010 was \$549 (2009: expense of \$261).

The weighted average principal actuarial financial assumptions used to calculate the defined benefit plans at 31 December are:

	Rate of increase for pensions in payment and deferred pension	Inflation assumption	Discount Rate	Rate of pay increase
	%	%	%	%
2010	3.4	4.1	5.4	4.8
2009	3.5	4.1	5.6	5.1

The net obligation amount recognised in the consolidated balance sheet in respect of the Sterling area plan is as follows:

	2010	2009
Equities	7,554	6,577
Bonds	7,593	7,915
Property and other	766	469
Fair value of plan assets	<u>15,913</u>	<u>14,961</u>
Present value of funded obligations	<u>(15,535)</u>	<u>(15,702)</u>
Net surplus (deficit) obligation	<u>378</u>	<u>(741)</u>

(In US dollar thousands)

31 December 2010

The weighted average expected rate of return on assets for 2010 was 6.1% (2009: 6.0%). The basis used to determine the percentage expected rate of return on assets was market conditions at the date of the actuarial valuation. The changes in the present value of the defined benefit obligation in respect of the group's pension plan are presented below.

	2010	2009
At 1 January	15,702	12,571
Current service cost	165	184
Interest cost	815	850
Actuarial losses	275	968
Benefits paid	(566)	(565)
Exchange and other movements	(856)	1,694
At 31 December	<u>15,535</u>	<u>15,702</u>

The changes in the fair value of the group's pension plan assets are presented below.

	2010	2009
At 1 January	14,961	11,392
Expected return	832	773
Contributions by the group	1,078	116
Actuarial gains	430	1,669
Benefits paid	(566)	(565)
Exchange and other movements	(822)	1,576
At 31 December	<u>15,913</u>	<u>14,961</u>

The actual return on plan assets for the year ended 31 December 2010 was a gain of \$1,262 (2009: gain of \$2,442).

The total net expense recognised in the consolidated income statement in 'Employee compensation and benefits' in respect of the pension plans comprises:

	2010	2009
Current service cost	(165)	(184)
Interest cost	(815)	(850)
Expected return on plan assets	832	773
Other movements	(401)	-
Total net expense	<u>(549)</u>	<u>(261)</u>

An actuarial gain of \$189 (2009: gain of \$583) was included in the consolidated statement of comprehensive income for the defined benefit pension plans. The cumulative amount of actuarial losses recognised in the consolidated statement of comprehensive income is \$2,384 (2009: \$2,573).

(c) Post-employment healthcare benefits plan

The group provides a non-contributory unfunded post-employment healthcare benefits plan for certain Bermuda-based retired employees. To qualify, employees must have a minimum of 15 years of successive service at the date of retirement. Independent, qualified actuaries carry out an actuarial assessment of the liabilities of the plan on an annual basis using the RP-2000 Fully Generational Mortality Improvement Projection table. The liabilities are evaluated by discounting the expected future claims to a net present value.

The latest actuarial assessment was carried out in October 2010 in accordance with IAS 19 'Employee Benefits'. At 31 December 2010, the estimated present value of the post-employment healthcare benefit obligation was \$51,875 (2009: \$41,137). The main financial assumptions used to estimate the obligation at 31 December 2010 are current and ultimate healthcare claims trend rate of 9.00% and 4.75% per annum respectively (2009: 8.00% and 4.75%) and a discount rate of 5.66% (2009: 6.00%) per annum.

Notes on the Consolidated Financial Statements (continued)

(In US dollar thousands)

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The changes in the present value of the post-employment healthcare benefit obligations are as follows:

	2010	2009
At 1 January	41,137	39,677
Current service cost	1,720	1,441
Interest cost	2,378	2,008
Contributions by employees	1,075	1,121
Actuarial losses (gains)	7,832	(631)
Benefits paid	(2,142)	(2,354)
Plan amendments	(125)	(125)
At 31 December	<u>51,875</u>	<u>41,137</u>

The total net expense recognised in the consolidated income statement within 'Employee compensation and benefits' in respect of the post-employment healthcare benefits plan is comprised of:

	2010	2009
Current service cost	(1,720)	(1,441)
Interest cost	(2,378)	(2,008)
Plan amendments	125	125
Total net expense	<u>(3,973)</u>	<u>(3,324)</u>

Total net actuarial results recognised in the consolidated statement of comprehensive income in 2010 in respect of the post-employment healthcare benefits plan are a loss of \$7,832 (2009: gain of \$631). The total cumulative net actuarial loss to date, which has been recognised in the consolidated statement of comprehensive income, is \$503 (2009: \$7,329).

The net deficits and the experience adjustments on plan liabilities expressed as an amount and as a percentage of the net deficit for the current and previous annual period are as follows:

	2010	2009
Net obligation	51,875	41,137
Experience adjustments on plan liabilities expressed as an amount	(7,832)	631
Experience adjustments on plan liabilities expressed as a percentage	(15.1%)	1.5%

The actuarial assumptions of the healthcare cost trend rates may have a significant effect on the amounts recognised. A one-percentage point change in assumed healthcare cost trend rates would have the following effects on amounts recognised in 2010:

	1% increase	1% decrease
Effect on the aggregate of the current service cost and interest cost	1,041	(778)
Effect on present value of the benefit obligation	10,680	(8,247)

7 Share-based payments

During 2010, \$6,503 was charged to the consolidated income statement in respect of share-based payment transactions settled in equity (2009: \$7,164). This expense, which was computed from the fair values of the share-based payments on transaction dates, arose under employee share awards made in accordance with the group's reward structures. All share plans are based on ordinary \$0.50 par value shares in the ultimate parent company HSBC Holdings plc. All exercise prices and fair values of shares and options presented below are exact amounts (not rounded or shown to the nearest thousand).

In April 2009, HSBC Holdings plc completed a rights issue. The terms of the share plans have been adjusted accordingly to maintain the value of the awards and these adjustments are set out in the tables below. The adjustments were based on the theoretical ex-rights price, which was considered to be the most appropriate methodology to reflect the rights issue.

(In US dollar thousands)

31 December 2010

Calculation of fair values

Fair values of share options/awards, measured at the date of grant of the option/award, are calculated using a Black-Scholes model. When modelling options/awards with vesting dependent on HSBC's Total Shareholder Return ('TSR') over a period, the TSR performance targets are incorporated into the model using Monte Carlo simulation. The expected life of options depends on the behaviour of option holders, which is incorporated into the option model on the basis of historical observable data. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitations of the model used.

The significant weighted average assumptions used to estimate the fair value of the options granted were as follows:

	1-year Savings-related share option plan	3-year Savings-related share option plan	5-year Savings-related share option plan
2010			
Risk-free interest rate ¹ (%).....	0.7	1.9	2.9
Expected life ² (years)	1	3	5
Expected volatility ³ (%).....	30	30	30
Share price at grant date (\$).....	10.60	10.60	10.60
2009			
Risk-free interest rate ¹ (%).....	0.7	2.1	2.1
Expected life ² (years)	1	3	5
Expected volatility ³ (%).....	50	35	30
Share price at grant date (\$).....	6.88	6.88	6.88

¹ The risk-free rate was determined using a similar yield curve to the UK gilts yield curve.

² Expected life is not a single input parameter but a function of various behavioural assumptions.

³ Expected volatility is estimated by considering both historic average HSBC Holdings plc share price volatility and implied volatility for traded options over HSBC Holdings plc shares of similar maturity to those of the employee options.

Expected dividends are incorporated into the valuation model for share options and awards, where applicable. The expected US dollar denominated dividend yield was determined to be 4.5 per cent, in line with consensus analyst forecast.

The HSBC share plan

The HSBC share plan was adopted by HSBC Holdings plc in 2005. Under this plan, performance share awards, restricted share awards and share option awards may be made. The aim of the HSBC share plan is to align the interests of executives with the creation of shareholder value and recognise individual performance and potential. Awards are also made under this plan for recruitment and retention purposes.

Performance share awards

Performance shares are awarded to executive directors and other senior executives after taking into account individual performance in the previous year. For awards made prior to 2008, each award is divided into two equal parts for testing attainment against pre-determined benchmarks. One half of the award is subject to a TSR measure, based on HSBC's ranking against a comparator group of 28 major banks; the other half is subject to an earnings per share target. For each element of the award, shares are released to the employee on a sliding scale from 30 to 100 per cent of the award, depending on the scale of achievement against the benchmarks, providing that the minimum criteria for each performance measure has been met.

In determining whether HSBC Holdings plc has achieved sustained improvement the Remuneration Committee will take account of all relevant factors, in particular, comparisons against the TSR comparator group in areas such as revenue growth and mix, cost efficiency, credit performance, cash return on cash invested, dividend performance and TSR.

(In US dollar thousands)

31 December 2010

	2010	2009
	Number of awards (000s)	Number of awards (000s)
Outstanding at 1 January	-	104
Adjustment for rights issue	-	15
Granted in the year ¹	-	2
Exercised in the year	-	(24)
Forfeited in the year	-	(97)
Outstanding at 31 December	<u>-</u>	<u>-</u>

¹ Additions during the year include reinvested scrip dividends.

The weighted average fair value of shares awarded by the group for performance share awards in 2010 was \$NIL (2009: \$12.95).

Restricted share awards

Restricted shares are awarded to employees on the basis of their performance, potential and retention requirements, to aid retention or as a part-deferral of annual bonuses. Shares are awarded without corporate performance conditions and generally vest between one and three years from the date of award, providing the employees have remained continually employed by the group for this period.

	2010	2009
	Number of awards (000s)	Number of awards (000s)
Outstanding at 1 January	2,097	1,031
Adjustment for rights issue	-	289
Granted in the year ¹	260	1,309
Transferred (out)/in from group companies	(69)	51
Exercised in the year	(450)	(354)
Forfeited in the year	(17)	(229)
Outstanding at 31 December	<u>1,821</u>	<u>2,097</u>

¹ Additions during the year include reinvested scrip dividends.

The weighted average fair value of shares awarded by HSBC for restricted share awards in 2010 was \$12.78 (2009: \$6.35).

Savings-related share option plans

Savings-related share option plans invite eligible employees to enter into savings contracts to save up to four hundred (2009: three hundred and fifty) dollars per month, with the option to use the savings to acquire shares. The aim of the plans is to align the interests of all employees with the creation of shareholder value. The options are exercisable within three months following the first anniversary of the commencement of a one-year savings contract or within six months following either the third or fifth anniversaries of the commencement of three-year or five-year savings contracts, respectively. The exercise price is set at a 20 percent discount to the average market value immediately preceding the date of invitation.

(In US dollar thousands)

31 December 2010

	2010		2009	
	Number of options (000s)	Weighted average exercise price	Number of options (000s)	Weighted average exercise price
Outstanding at 1 January ¹	1,196	6.63	662	11.44
Adjustment for rights issue	-	-	81	11.44
Granted in the year ²	211	7.24	983	5.04
Transferred in from group companies	7	8.05	36	11.30
Exercised in the year	(201)	5.20	(43)	9.66
Forfeited in the year	(229)	9.57	(523)	10.54
Outstanding at 31 December	984	6.33	1,196	6.63

¹ Opening weighted average exercise price adjusted for rights issue.

² Additions during the year include reinvested scrip dividends.

The weighted average fair value of options granted during the year was \$2.55 (2009: \$2.08). The weighted average share price at the date the share options were exercised was \$10.55 (2009: \$10.64). The exercise price range and weighted average remaining contractual life for options outstanding at the balance sheet date were as follows:

	2010	2009
Exercise price range from lowest to highest price (\$)	4.83 - 9.44	4.87 - 13.88
Weighted average remaining contractual life (years)	1.8	2.5
Number of options exercisable at year end (in thousands)	458	21
Weighted average exercise price of options exercisable at year end (\$)	8.99	8.80

HSBC Holdings plc group share option plan

The HSBC Holdings plc group share option plan was a long-term incentive plan under which certain HSBC employees between 2000 and 2005 were awarded share options. The aim of the plan was to align the interests of those higher performing employees with the creation of shareholder value. This was achieved by setting certain TSR targets which would normally have to be attained in order for the awards to vest. Options were granted at market value and are normally exercisable between the third and tenth anniversaries of the date of grant, subject to vesting conditions. The options granted after May 2005 are made under the HSBC share plan.

	2010		2009	
	Number of options (000s)	Weighted average exercise price	Number of options (000s)	Weighted average exercise price
Outstanding at 1 January ¹	118	11.09	60	11.26
Adjustment for rights issue	-	-	16	11.26
Transferred in from group companies	(1)	3.63	51	10.78
Exercised in the year	(1)	4.58	-	-
Forfeited in the year	(37)	9.22	(9)	10.78
Outstanding at 31 December	79	12.11	118	11.09

¹ Opening weighted average exercise price adjusted for rights issue.

The number of options, weighted average exercise price, and weighted average remaining contractual life of options outstanding at the balance sheet date, analysed by exercise price range, were as follows:

	2010	2009
Exercise price range from lowest to highest price (\$)	7.82 - 9.98	9.68 - 12.21
Weighted average remaining contractual life (years)	1.12	3.27
Number of options exercisable at year end (in thousands)	79	118

(In US dollar thousands)

31 December 2010

8 Tax expense

Under current Bermuda law the group is not required to pay any corporate taxes in Bermuda on either income or capital gains. The group has received an undertaking from the Minister of Finance in Bermuda that in the event of such taxes being imposed, the group will be exempt from corporate taxation until the year 2016. The group's income tax expense relates to income from operations and is attributable to the income tax expense of certain overseas subsidiaries. Overseas subsidiary undertakings and overseas branches provided for taxation at the appropriate rates in the countries in which they operate.

	2010	2009
Current tax		
Current overseas tax charge	41,379	29,384
Deferred tax		
Origination and reversal of temporary differences	(34,432)	(11,366)
Tax expense	<u>6,947</u>	<u>18,018</u>
	2010	2009
Analysis of overall tax charge		
Taxation at Bermuda corporation tax rate of 0%	-	-
Impact of overseas profits in principal locations taxed at different rates	22,360	18,425
Non taxable items	(15,871)	(1,492)
Prior period adjustments	472	(244)
Other items	(14)	1,329
Deferred tax	34,432	11,366
Overall tax charge	<u>41,379</u>	<u>29,384</u>
Deferred tax		
At 1 January	(33,687)	(44,961)
Charge to profit for the year	34,432	11,366
Movement arising from subsidiary reclassified as held for sale	(405)	-
Exchange differences and other movements	(273)	(92)
Overall tax charge	<u>67</u>	<u>(33,687)</u>
Deferred tax liabilities	-	(33,921)
Deferred tax assets	67	234
Net deferred tax assets (liabilities) at 31 December	<u>67</u>	<u>(33,687)</u>
Comprising:		
- Short-term timing differences	-	(33,875)
- Accelerated capital allowances	11	72
- Other items	56	116
Net deferred tax assets (liabilities) at 31 December	<u>67</u>	<u>(33,687)</u>

9 Derivatives

Derivatives are financial instruments that derive their value from the price of an underlying item such as equities, bonds, interest rates, foreign exchange rates, credit spreads, commodities and equity or other indices. Derivatives enable users to increase, reduce or alter exposure to credit or market risks. The group makes markets in derivatives for its customers and uses derivatives to manage its exposure to credit and market risks (Note 27).

Derivatives are carried at fair value and shown in the consolidated balance sheet gross. Asset values represent the cost to the group of replacing all transactions with a fair value in the group's favour assuming that the entire group's relevant counterparties default at the same time, and that transactions can be replaced instantaneously. Liability values represent the cost to the group's counterparties of replacing all their transactions with the group with a fair value in their favour if the group were to default. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Derivative assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right of offset exists and the cash flows are intended to be settled on a net basis. Changes in the values of derivatives are recognised in 'Dealing profits' unless they qualify as hedges for accounting purposes.

(a) Use of derivatives

The group uses derivatives for two primary purposes: to create risk management solutions for clients and to manage and hedge the group's own risks. For accounting purposes, derivative instruments are classified as held either for trading or hedging. Derivatives that are held as hedging instruments are formally designated as hedges as defined in IAS 39. All other derivative instruments are classified as held for trading. The held for trading classification includes two types of derivative instruments: those used in sales and trading activities, and those instruments that are used for risk management purposes but which for various reasons do not meet the qualifying criteria for hedge accounting.

The group's derivative activities give rise to significant open positions in portfolios of derivatives. These positions are managed constantly to ensure that they remain within acceptable risk levels, with offsetting deals being entered into to achieve this where necessary. When entering into derivative transactions, the group employs the same credit risk management procedures to assess and approve potential credit exposures as are used for traditional lending.

With respect to exchange rate derivative contracts, the notional or contractual amounts of these instruments indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

(b) Trading derivatives

The derivative transactions of the group relate to foreign exchange sales and trading activities. Sales activities include the structuring and marketing of derivative products to customers to enable them to take, transfer, modify or reduce current or expected risks.

As mentioned above, other derivatives classified as held for trading may include non-qualifying hedging derivatives, ineffective hedging derivatives and the components of hedging derivatives that are excluded from assessing hedge effectiveness. Non-qualifying hedging derivatives are entered into for risk management purposes but do not meet the criteria for hedge accounting.

Gains and losses from changes in the fair value of derivatives that do not qualify for hedge accounting are reported in 'Dealing profits'.

The total of all outstanding contract amounts of derivatives held for trading purposes at 31 December 2010, which are exclusively exchange rate products, amounts to \$966,922 (2009: \$1,415,177).

(In US dollar thousands)

31 December 2010

The following table summarises the fair values of exchange rate derivatives, comprised of foreign exchange forward and spot contracts, held for trading purposes:

	2010		2009	
	Assets	Liabilities	Assets	Liabilities
Forward contracts	7,896	8,193	11,015	9,169
Spot contracts	26	3	90	157
Derivatives	<u>7,922</u>	<u>8,196</u>	<u>11,105</u>	<u>9,326</u>

A three level fair value hierarchy, which reflects the availability of observable market inputs, is used when estimating fair values. All derivatives are considered Level 2 as they are based upon observable market inputs. There was no netting of derivative assets and liabilities at 31 December 2010 or 31 December 2009. Total exposure to HSBC Group counterparties at 31 December 2010 amounted to \$7,064 (2009: \$3,592) and cash collateral was \$NIL (2009: \$NIL). Where the group receives collateral from customers related to outstanding foreign exchange rate derivative contracts, these comprise cash and cash equivalents, securities and mortgage interests over property. Credit concentrations with large counterparties are controlled through counterparty limits. Credit exposures, incorporating derivative exposures, to single names are capped and monitored by senior management as detailed in Note 27.

10 Loans and advances to banks

	2010		2009	
	Amortised cost	Fair value	Amortised cost	Fair value
Maturity analysis:				
One year or less	<u>4,890,172</u>	<u>4,890,172</u>	<u>3,647,066</u>	<u>3,647,066</u>

There are no impairment losses included in loans and advances to banks (2009: \$NIL) and there are no netting agreements or collateral held in respect of loans and advances to banks (2009: \$NIL).

	2010	2009
Credit rating analysis of loans and advances to banks		
AAA	512,537	178,819
AA	183,852	1,112,019
AA-	1,725,089	1,157,864
A+	1,412,052	1,013,824
A	675,835	25,000
A-	50,000	50,000
BBB+	10,000	-
BBB	137,500	-
BBB-	75,000	-
Not rated	-	15,139
Cash and cash equivalents	<u>108,307</u>	<u>94,401</u>
	<u>4,890,172</u>	<u>3,647,066</u>

Collateral is held for the group's securities lending activity, for which the bank normally accepts collateral in the form of cash, US government or federal agency securities, letters of credit or OECD debt instruments approved by the group.

(In US dollar thousands)

31 December 2010

11 Loans and advances to customers

The group has the following concentration of loans and advances to customers in Bermuda and Cayman.

Where customers have both a borrowing and a deposit relationship with the group, loans and deposits are presented gross:

	2010	2009
Residential mortgages	1,707,755	1,578,549
Other personal	519,568	545,269
Total loans to individuals	2,227,323	2,123,818
Commercial, industrial and international trade	102,725	149,297
Commercial real estate	529,269	359,191
Government	20,802	116,565
Other commercial	298,131	212,366
Total commercial	950,927	837,419
Non-bank financial institutions	77,668	106,438
Allowance for losses on loans and advances	(18,072)	(11,797)
At 31 December	3,237,846	3,055,878

Gross loans with variable rates are \$2,798,258 (2009: \$2,784,174) and fixed rates are \$457,660 (2009: \$283,501).

The following table provides an analysis of remaining contractual maturities and measurement bases of loans and advances to customers:

	2010		2009	
	Amortised cost	Fair value	Amortised cost	Fair value
Maturity analysis:				
One year or less	474,912	474,909	524,025	524,019
More than one year	2,762,934	2,685,372	2,531,853	2,445,872
	3,237,846	3,160,281	3,055,878	2,969,891

The loan fair values disclosed above are based on weighted average estimated remaining maturities and are determined using a valuation technique supported by observable market rates. Additional information about the interest rate risk exposure pertaining to loans and advances to customers is presented in Note 25.

The following tables provide further analyses of customer loans and related allowances and collateral types at 31 December:

	2010			2009		
	Gross	Allowance	Net	Gross	Allowance	Net
Loans and advances to customers:						
Not past due or impaired	2,879,914	(4,265)	2,875,649	2,831,819	(4,487)	2,827,332
Past due less than 30 days	176,415	(256)	176,159	88,533	(140)	88,393
Past due between 30 and 60 days	36,393	(50)	36,343	62,788	(104)	62,684
Past due between 60 and 90 days	20,205	(29)	20,176	21,841	(34)	21,807
Impaired	142,991	(13,472)	129,519	62,694	(7,032)	55,662
Total	3,255,918	(18,072)	3,237,846	3,067,675	(11,797)	3,055,878

(In US dollar thousands)

31 December 2010

	2010			2009		
	Specifically provided	Collectively provided	Total allowance	Specifically provided	Collectively provided	Total allowance
Allowances for loans and advances to customers:						
Not past due or impaired	-	(4,265)	(4,265)	-	(4,487)	(4,487)
Past due less than 30 days	-	(256)	(256)	-	(140)	(140)
Past due between 30 and 60 days	-	(50)	(50)	-	(104)	(104)
Past due between 60 and 90 days	-	(29)	(29)	-	(34)	(34)
Impaired	(11,880)	(1,592)	(13,472)	(5,429)	(1,603)	(7,032)
Total	(11,880)	(6,192)	(18,072)	(5,429)	(6,368)	(11,797)

	2010			2009		
	Mortgage interest	Assets other than mortgage interest	Unsecured	Mortgage interest	Assets other than mortgage interest	Unsecured
Gross loans and advances to customers by type of collateral:						
Not past due or impaired	2,321,097	89,681	469,136	2,214,757	103,883	513,181
Past due less than 30 days	130,085	649	45,681	80,331	357	7,844
Past due between 30 and 60 days	31,179	567	4,647	53,287	128	9,372
Past due between 60 and 90 days	17,520	473	2,212	19,673	21	2,148
Impaired	126,777	670	15,544	56,019	931	5,743
Total	2,626,658	92,040	537,220	2,424,067	105,320	538,288

The group holds collateral against loans and advances to customers in the form of mortgage interests over property, other charges over real and financial assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and updated in circumstances where a loan is showing signs of potential impairment or is individually assessed as impaired.

The table below shows an estimate of the fair value of collateral held against loans and advances to customers.

Estimate of fair value of collateral (unaudited)	2010	2009
Not past due or impaired	2,389,829	2,243,647
Past due but not impaired	180,126	151,142
Impaired	129,342	54,798
Total	2,699,297	2,449,587

The group adheres to HSBC policy direction and monitors credit concentration risk in accordance with local regulatory requirements. Additional analysis of credit concentration is provided above.

The group regularly reviews loans and advances to customers and allocates a risk rating against each loan or advance based on performance criteria. The breakdown of loans and advances to customers by risk category at 31 December 2010 is 91.0% (2009: 97.5%) performing, 4.6% (2009: 0.5%) substandard and 4.4% (2009: 2.0%) non-performing. Renegotiated loans that would otherwise have been past due or impaired totalled \$156,507 at 31 December 2010 (2009: \$NIL).

At 31 December 2010, the group does not hold any financial or non-financial assets obtained by taking possession of collateral held as security (2009: \$NIL).

(In US dollar thousands)

31 December 2010

The following table provides an analysis of the movements in allowance for impairment losses on loans and advances to customers during the year:

	Individually assessed loans	Collectively assessed loans	Total
Opening balance at 1 January 2009	3,440	4,576	8,016
Uncollectible amounts written off during the year	-	(2,846)	(2,846)
Recoveries	-	568	568
Impairment charges during the year	1,989	4,070	6,059
Balance at 31 December 2009	5,429	6,368	11,797
Uncollectible amounts written off during the year	(232)	(5,115)	(5,347)
Recoveries	-	865	865
Impairment charges during the year	6,683	4,074	10,757
Balance at 31 December 2010	11,880	6,192	18,072

12 Financial investments

The following tables provide an analysis of the group's financial investments, all classified as available-for-sale securities with the exception of \$31,093 (2009: \$NIL) trading assets related to structured certificates of deposit.

	2010		2009	
	Amortised cost	Fair value	Amortised cost	Fair value
Debt securities – fixed rate	1,716,461	1,744,612	1,271,510	1,307,728
Debt securities – floating rate	1,287,884	1,275,116	1,943,257	1,922,416
Equity securities	11,007	35,781	15,715	43,519
Total financial investments	3,015,352	3,055,509	3,230,482	3,273,663

Maturities analysis of debt securities

	2010	2009
One year or less	1,100,412	605,844
More than one year	1,919,316	2,624,300
	3,019,728	3,230,144

Credit rating analysis of debt securities

	2010	2009
AAA	1,451,601	879,003
AA+	163,831	100,810
AA	420,409	563,142
AA-	245,198	912,155
A+	424,172	472,742
A	250,089	188,603
A-	45,023	106,345
BBB+	13,173	7,344
BBB	6,232	-
	3,019,728	3,230,144

Total gains or losses included in profit and loss for the period are presented in the consolidated income statement in 'Gains less losses from financial investments'. Where debt securities are rated by Standard & Poor's ("S&P"), this rating is used. If the debt security is not rated by S&P, the Fitch rating is used. All securities guaranteed by the U.S. Government are assigned the U.S. Government's sovereign rating.

(In US dollar thousands)

31 December 2010

Financial investments by country and sector

Country	2010					
	Sovereign	Bank	Corporate	Asset backed	Equities	Total
Australia	77,323	89,088	-	-	-	166,411
Belgium	-	-	-	-	31	31
Bermuda	15,402	-	-	-	2,473	17,875
Canada	162,097	24,088	-	-	-	186,185
Cayman Islands	-	-	-	-	20,773	20,773
Denmark	-	26,387	-	-	-	26,387
Finland	-	76,297	-	-	-	76,297
France	178,702	141,625	-	-	-	320,327
Germany	-	163,173	-	-	-	163,173
Great Britain	299,003	560,233	-	-	12,000	871,236
Hong Kong	-	-	-	-	9	9
Ireland	-	39,336	-	-	-	39,336
Netherlands	-	61,431	-	-	-	61,431
Norway	25,914	-	-	-	-	25,914
Sweden	20,632	50,158	-	-	-	70,790
United States	35,971	653,158	92,287	227,423	495	1,009,334
	815,044	1,884,974	92,287	227,423	35,781	3,055,509

Financial investments by country and sector

Country	2009					
	Sovereign	Bank	Corporate	Asset backed	Equities	Total
Australia	-	70,476	-	-	-	70,476
Austria	-	24,725	-	-	-	24,725
Belgium	-	-	-	-	34	34
Bermuda	-	-	-	-	1,710	1,710
Canada	-	52,892	-	-	-	52,892
Cayman Islands	-	-	-	-	17,894	17,894
Denmark	-	26,690	-	-	-	26,690
Finland	-	76,493	-	-	-	76,493
France	-	327,096	-	-	-	327,096
Germany	-	166,927	-	-	-	166,927
Great Britain	-	802,709	15,841	-	19,064	837,614
Hong Kong	-	-	-	-	4,376	4,376
Ireland	-	80,595	-	-	-	80,595
Italy	-	19,808	-	-	-	19,808
Luxembourg	-	121,045	-	-	-	121,045
Netherlands	-	97,594	3,005	-	-	100,599
Norway	-	24,953	-	-	-	24,953
Singapore	8,952	-	-	-	-	8,952
Spain	-	82,352	-	-	-	82,352
Sweden	47,765	10,014	-	-	-	57,779
United States	53,642	714,923	114,809	286,838	441	1,170,653
	110,359	2,699,292	133,655	286,838	43,519	3,273,663

Debt securities amounting to \$46,719 (2009: \$49,845) are pledged to third parties in security lending agreements. The group is carrying all financial investments at fair value. During the year the group received proceeds of \$820,545 (2009: \$1,008,942) from the sale or maturity of financial investments and realised a net gain of \$5,312 (2009: \$13,462). In March 2009, an impairment loss of \$10,360 was recognised on HSBC Holdings plc shares in the available-for-sale portfolio for the purpose of long term incentive plans (see Note 7 for plan details). The group monitors interest rate sensitivity under varying interest rate scenarios as summarised in Note 27.

13 Fair values of financial investments carried at fair value

A three level fair value hierarchy, which reflects the significance of observable market inputs, is used when estimating fair values and is summarised in the chart below:

Fair value hierarchy summary by sector	2010			
	Level 1	Level 2	Level 3	Total
Sovereign	-	815,044	-	815,044
Bank	-	1,884,974	-	1,884,974
Corporate	-	92,287	-	92,287
Asset backed	-	227,423	-	227,423
Equities	3,539	-	32,242	35,781
	<u>3,539</u>	<u>3,019,728</u>	<u>32,242</u>	<u>3,055,509</u>

Fair value hierarchy summary by sector	2009			
	Level 1	Level 2	Level 3	Total
Sovereign	-	110,359	-	110,359
Bank	-	2,699,292	-	2,699,292
Corporate	-	133,655	-	133,655
Asset backed	-	286,838	-	286,838
Equities	11,239	-	32,280	43,519
	<u>11,239</u>	<u>3,230,144</u>	<u>32,280</u>	<u>3,273,663</u>

The following table shows a reconciliation of equities from the beginning balance to the ending balance for fair value measurements in Level 3 of the fair value hierarchy:

	2010	2009
At 1 January	32,280	45,540
Purchases	51,442	1,454
Sales	(52,324)	(1,599)
Total gains or losses:		
in profit or loss	(1,652)	(13,836)
in other comprehensive income	2,496	955
Other movements	-	(234)
At 31 December	<u>32,242</u>	<u>32,280</u>

14 Property, plant and equipment

	Land and buildings	Equipment, fixtures and fittings	Total
Cost			
Cost at 1 January 2010	225,171	76,102	301,273
Additions at cost	8,290	12,978	21,268
Disposals and write-offs	(5,695)	(1,646)	(7,341)
Reclassified as assets held for sale	(675)	(3,001)	(3,676)
Other movements	1,279	(880)	399
Cost at 31 December 2010	228,370	83,553	311,923
Accumulated depreciation			
Accumulated depreciation at 1 January 2010	26,677	36,907	63,584
Depreciation charge for the year	5,938	8,712	14,650
Disposals and write-offs	(469)	(953)	(1,422)
Reclassified as assets held for sale	(162)	(2,399)	(2,561)
Other movements	472	(419)	53
Accumulated depreciation at 31 December 2010	32,456	41,848	74,304
Net book value at 31 December 2010	195,914	41,705	237,619
2009			
	Land and buildings	Equipment, fixtures and fittings	Total
Cost			
Cost at 1 January 2009	218,942	61,193	280,135
Additions at cost	25,369	17,590	42,959
Disposals and write-offs	(2,625)	(1,020)	(3,645)
Reclassified as assets held for sale	(16,515)	(1,677)	(18,192)
Other movements	-	16	16
Cost at 31 December 2009	225,171	76,102	301,273
Accumulated depreciation			
Accumulated depreciation at 1 January 2009	24,053	29,741	53,794
Depreciation charge for the year	5,460	6,872	12,332
Disposals and write-offs	(541)	(10)	(551)
Reclassified as assets held for sale	(2,295)	(787)	(3,082)
Other movements	-	1,091	1,091
Accumulated depreciation at 31 December 2009	26,677	36,907	63,584
Net book value at 31 December 2009	198,494	39,195	237,689

Included in land and buildings are assets held on a finance lease with a net book value of \$NIL (2009: \$4,760). During the year the group completed its construction of a new office building located in Hamilton, Bermuda. At 31 December 2009, construction costs incurred in respect of this building amounted to \$69,482 (*unaudited*).

15 Goodwill

	2010	2009
Cost		
At 1 January	239,893	239,893
Disposals	(19,507)	-
Assets held for sale (Note 19)	(169,044)	-
At 31 December	<u>51,342</u>	<u>239,893</u>

Note 18 and 19 present information about subsidiary undertakings disposed of and the discontinued operations of a subsidiary during the year ended 31 December 2010. There were no additions or disposals to goodwill during the year ended 31 December 2009.

Goodwill is reviewed for impairment annually and was determined not to be impaired at 31 December 2010 or 31 December 2009.

16 Group entities
(a) Principal subsidiary undertakings

	Country of incorporation or registration	Bank's interest in equity capital (%)
Bermuda International Securities Limited	Bermuda	100
Bermuda Trust Company Limited	Bermuda	100
HSBC Global Asset Management (Bermuda) Limited	Bermuda	100
HSBC Institutional Trust Services (Bermuda) Limited	Bermuda	100
HSBC Insurance Holdings (Bermuda) Limited	Bermuda	100
HSBC Securities Services (Bermuda) Limited	Bermuda	100
HSBC International Trustee Limited	British Virgin Islands	100
HSBC Bank (Cayman) Limited	Cayman	100

All of the above entities prepare their financial statements up to 31 December. Please refer to Note 18 for details of acquisitions and disposals during 2010.

(b) Principal associates
Movement in investments in associates

	2010	2009
At 1 January	2,240	111
Additions	-	3,000
Share of loss	(497)	(871)
At 31 December	<u>1,743</u>	<u>2,240</u>

Summarised aggregate financial information on associates at 31 December

	2010	2009
Assets	4,829	6,291
Liabilities	1,272	1,680
Operating income	7,159	6,883
Loss for the year	(994)	(1,547)

The additions in 2009 relate to an additional investment to support operations in an existing associate, ProServe Bermuda Limited, and resulted in the level of ownership remaining unchanged. Associates are accounted for using the equity method.

17 Impairment of assets other than financial instruments

During 2010, the group obtained an independent market valuation for each major building owned and compared the carrying cost to the appraisal and the assets value in use where appropriate. As a result, an impairment loss on two buildings, classified as 'assets held for sale', was recognised in the amount of \$2,229. The impairment has been included in the consolidated income statement as part of 'Depreciation and impairment of property, plant and equipment'.

As at 31 December 2009, there was no impairment of 'assets other than financial instruments'.

18 Investments

(a) Acquisitions

The group did not purchase any subsidiary undertakings in 2010 or 2009.

(b) Disposals

During the year ended 31 December 2010, the group made the following disposal to an HSBC affiliated entity for total cash proceeds of \$400,000. The attributable gain has been included in the 'Gains less losses on disposal of property, plant and equipment and subsidiary investments' in the group's consolidated income statement as follows:

Location	Subsidiary / Business	Cash and cash equivalents in subsidiaries	Net asset value	Attributable gain
Bermuda	HSBC Insurance (Bermuda) Limited ('the Captive')	63,774	377,890	30,670

During the year ended 31 December 2010, the group also liquidated its subsidiary in the Isle of Man.

The group did not dispose of any subsidiary undertakings in 2009.

19 Assets held for sale

	Property, plant and equipment	Discontinued operations of subsidiary	Total
Assets			
At 1 January 2010	15,110	-	15,110
Transfers in	513	-	513
Disposals	(513)	-	(513)
Reduction in value through impairment (Note 17)	(2,229)	-	(2,229)
Subsidiary assets reclassified as held for sale	-	254,035	254,035
Assets held for sale 31 December 2010	12,881	254,035	266,916
Liabilities			
At 1 January 2010	-	-	-
Subsidiary liabilities reclassified as held for sale	-	34,119	34,119
Liabilities held for sale at 31 December 2010	-	34,119	34,119

Notes on the Consolidated Financial Statements (continued)

(In US dollar thousands)

31 December 2010

(a) Assets held for sale – Property, plant and equipment

At 31 December 2010, assets held for sale is comprised of an office building and a mixed use property in the process of being sold by the group. The assets were recorded at the lower of net book value and fair value less costs to sell, which amounted to \$12,881 (2009: \$15,110).

(b) Assets and liabilities held for sale – Discontinued operations of subsidiary

Subject to regulatory approvals, during 2011 the group will dispose of HSBC International Trustee Limited to an HSBC affiliated entity for total cash proceeds of \$222,000 which is the estimated fair value of the business at sale date. The 'Consolidated income statement for the year ended 31 December 2010' has been presented to show the discontinued operations separately from continuing operations and the assets and liabilities of the discontinued operations have been separately included in assets and liabilities held for sale, respectively, in the 'Consolidated balance sheet at 31 December 2010'. The results and impact of the discontinued operations of the subsidiary are summarised below:

	2010	2009
Results from discontinued operations		
Net operating income	87,516	83,782
Total operating expenses	<u>(56,281)</u>	<u>(58,883)</u>
Profit before tax	31,235	24,899
Tax expense	<u>(4,534)</u>	<u>(5,214)</u>
Profit from discontinued operations (net of income tax)	<u>26,701</u>	<u>19,685</u>
Cash flows (used in) from discontinued operations		
Net cash flows from operations	22,243	35,532
Net cash flows used in investing operations	(171)	(2,365)
Net cash flows used in financing activities	<u>(32,000)</u>	<u>(10,000)</u>
Net cash flows for the year	<u>(9,928)</u>	<u>23,167</u>
Net assets of discontinued operations of subsidiary		
Cash and cash equivalents	43,663	
Financial investments	12,065	
Prepayments and accrued income	17,989	
Other assets	10,672	
Property, plant and equipment	602	
Goodwill	<u>169,044</u>	
Assets held for sale	<u>254,035</u>	
Accruals and deferred income	25,727	
Provisions and other liabilities	<u>8,392</u>	
Liabilities held for sale	<u>34,119</u>	
Net assets and liabilities	<u>219,916</u>	

(In US dollar thousands)

31 December 2010

20 Liabilities under insurance contracts

The analysis of the movement of liabilities under insurance contracts for the year ended 31 December 2010 and 31 December 2009 is as follows:

	Non-life insurance			
	Unearned premium	Outstanding claims	IBNR losses	Total
Gross liabilities				
At 1 January 2010	127,729	66,239	150,704	344,672
Premiums/claims in respect of new business	3,222	-	-	3,222
Other premiums/claims in respect of current year	45,624	976	42,119	88,719
Policy terminations	(55)	-	-	(55)
Premiums recognised	(92,003)	-	-	(92,003)
Movements due to claims development in respect of prior year claims	-	8,257	(28,662)	(20,405)
At 30 June 2010	84,517	75,472	164,161	324,150
Disposal of subsidiary	(84,517)	(75,472)	(164,161)	(324,150)
At 31 December 2010	-	-	-	-
Reinsurance assets				
At 1 January 2010	7,293	83	-	7,376
Premiums/claims in respect of current year	128	-	-	128
Premiums/claims in respect of prior year	(3,070)	404	-	(2,666)
At 30 June 2010	4,351	487	-	4,838
Disposal of subsidiary	(4,351)	(487)	-	(4,838)
At 31 December 2010	-	-	-	-
Net liabilities under insurance contracts at 30 June 2010	80,166	74,985	164,161	319,312
Disposal of subsidiary	(80,166)	(74,985)	(164,161)	(319,312)
Net liabilities under insurance contracts	-	-	-	-
	Non-life insurance			
	Unearned premium	Outstanding claims	IBNR losses	Total
Gross liabilities				
At 1 January 2009	104,329	45,554	94,527	244,410
Premiums/claims in respect of new business	8,469	405	-	8,874
Other premiums/claims in respect of current year	168,163	6,629	19,916	194,708
Policy terminations	(661)	612	-	(49)
Premiums recognised	(152,571)	-	-	(152,571)
Movements due to claims development in respect of prior year claims	-	13,039	36,261	49,300
At 31 December 2009	127,729	66,239	150,704	344,672
Reinsurance assets				
At 1 January 2009	5,262	84	-	5,346
Premiums/claims in respect of current year	4,528	83	-	4,611
Premiums/claims in respect of prior year	(2,497)	(84)	-	(2,581)
At 31 December 2009	7,293	83	-	7,376
Net liabilities under insurance contracts	120,436	66,156	150,704	337,296

Reinsurance assets are included within 'Other assets' in the consolidated balance sheet.

(In US dollar thousands)

31 December 2010

Effective 1 July 2010, HSBC Insurance (Bermuda) Limited ('the Captive') was sold to an HSBC affiliated entity (see Note 18). The Captive provided professional indemnity and directors' and officers' liability insurance coverage on an annual renewal basis to affiliated HSBC Group companies. All claims, potential losses and liabilities under insurance contracts have been transferred with the Captive.

21 Provisions

	2010	2009
At 1 January	4,495	18,462
Increases in provisions	3,522	1,451
Provisions recovered	(721)	(5,684)
Provisions utilised	(6,070)	(9,734)
Transfer to assets held for sale	(1,226)	-
At 31 December	-	4,495

'Provisions' for 2010 and 2009 are comprised entirely of legal provisions related to ongoing legal proceedings.

22 Contingent liabilities, contractual commitments and guarantees

The table below discloses the nominal principal amounts of third party off-balance sheet transactions. Contingent liabilities and commitments are credit-related instruments, which include letters of credit, guarantees and commitments to extend credit. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. Since a significant portion of guarantees and commitments are expected to expire without being drawn upon, the total of the contractual amounts is not representative of future liquidity requirements.

	2010	2009
Guarantees and contingent liabilities		
Guarantees in the form of irrevocable letters of credit	245,426	178,794
Other guarantees	2,526	8,179
Other contingent liabilities	3,655	4,765
	<u>251,607</u>	<u>191,738</u>
Commitments		
Documentary credits and short-term trade-related transactions	3,235	1,847
Undrawn revolving underwriting facilities	316,494	297,811
Undrawn formal standby facilities, credit lines and other commitments to lend		
– one year or less	239,064	275,980
– more than one year	372,469	126,322
	<u>931,262</u>	<u>701,960</u>
Guarantees in favour of third parties		
Guarantee type		
Financial guarantees	2,500	8,179
Standby letters of credit which are financial guarantees	245,452	178,794
Performance bonds	2,887	1,630
Standby letters of credit related to particular transactions	348	217
Other items	3,655	4,765
	<u>254,842</u>	<u>193,585</u>

At 31 December 2010 approximately 67% (2009: 84%) of the above guarantees have an original contractual term of less than one year. Guarantees with a term of more than one year are subject to the group's annual credit review process.

When the group has given a guarantee on behalf of a customer, it will have the right to recover from that customer any amounts paid under the guarantee. At 31 December 2010, the group holds collateral amounting to \$133,587 (2009: \$161,567), which could be used to recover amounts paid under the above guarantees.

Notes on the Consolidated Financial Statements (continued)

(In US dollar thousands)

31 December 2010

23 Lease commitments

At 31 December 2010, the group was obligated under a number of non-cancellable operating leases for properties, plant and equipment, for which the future minimum lease payments extend over a number of years as follows:

	2010		2009	
	Land and buildings	Equipment	Land and buildings	Equipment
Annual commitments under non-cancellable operating leases expiring:				
Not later than one year	1,920	168	2,235	359
Later than one year and not later than five years	6,455	105	6,627	102
Later than five years	13,759	-	13,638	-
	<u>22,134</u>	<u>273</u>	<u>22,500</u>	<u>461</u>

During the year \$3,187 (2009: \$3,646) was recognised within 'General and administrative expenses' in respect of lease agreements.

24 Maturity analysis of financial assets and financial liabilities

The following is an analysis of financial assets and financial liabilities by remaining contractual maturities at the date of the consolidated balance sheet:

31 December 2010	On demand	Due within one year	Due between one and five years		Due after five years	Undated	Total	Fair Value
			one and five years	five years				
Financial assets								
Cash and balances at central banks	29,025	-	-	-	-	-	29,025	29,025
Items in the course of collection from other banks	522	-	-	-	-	-	522	522
Derivatives	-	7,400	515	7	-	-	7,922	7,922
Loans and advances to banks	666,505	4,116,167	107,500	-	-	-	4,890,172	4,890,172
Loans and advances to customers	175,438	299,474	726,714	2,036,220	-	-	3,237,846	3,160,281
Financial investments	-	1,100,412	1,541,873	377,444	35,780	-	3,055,509	3,055,509
Total at 31 December 2010	871,490	5,523,453	2,376,602	2,413,671	35,780	-	11,220,996	11,143,431
Financial liabilities								
Deposits by banks	34,519	-	-	-	-	-	34,519	34,519
Customer accounts	7,240,682	2,416,039	49,955	338	-	-	9,707,014	9,709,833
Items in course of transmission to other banks	10,642	-	-	-	-	-	10,642	10,642
Derivatives	-	7,685	505	6	-	-	8,196	8,196
Total at 31 December 2010	7,285,843	2,423,724	50,460	344	-	-	9,760,371	9,763,190

(In US dollar thousands)

31 December 2010

31 December 2009	On demand	Due within one year	Due between one and five years	Due after five years	Undated	Total	Fair Value
Financial assets							
Cash and balances at central banks	34,280	-	-	-	-	34,280	34,280
Items in the course of collection from other banks	41	-	-	-	-	41	41
Derivatives	-	10,928	177	-	-	11,105	11,105
Loans and advances to banks	663,473	2,983,593	-	-	-	3,647,066	3,647,066
Loans and advances to customers	326,116	197,909	806,825	1,725,028	-	3,055,878	2,969,891
Financial investments	-	605,844	2,211,078	413,222	43,519	3,273,663	3,273,663
Total at 31 December 2009	1,023,910	3,798,274	3,018,080	2,138,250	43,519	10,022,033	9,936,046
Financial liabilities							
Deposits by banks	36,672	89,060	-	-	-	125,732	125,732
Customer accounts	6,331,030	1,841,528	47,988	255	-	8,220,801	8,224,505
Items in course of transmission to other banks	12,717	-	-	-	-	12,717	12,717
Derivatives	-	9,156	170	-	-	9,326	9,326
Total at 31 December 2009	6,380,419	1,939,744	48,158	255	-	8,368,576	8,372,280

Financial instruments included within 'Prepayments and accrued income', 'Other assets', 'Retirement benefit liabilities', 'Liabilities under insurance contracts', 'Accruals and deferred income', 'Provisions' and 'Other liabilities' have not been included in the analysis above as they do not have contractual maturities. Fair values for 'Loans and advances to customers' and 'Customer accounts' are based on weighted average estimated remaining maturities determined using a valuation technique supported by observable market rates.

(In US dollar thousands)

31 December 2010

25 Interest rate analysis of financial instruments

The table below discloses the mismatch of the dates on which interest on financial assets and financial liabilities are next reset to market rate on a contractual basis, or if earlier, the dates on which the instruments mature. Contractual terms may not be representative of the behaviour of financial assets and liabilities and the group therefore manages interest rate risk based on the behavioural characteristics of the relevant financial assets and liabilities.

31 December 2010	Due within three months	Due between three and six months	Due between six months and one year	Due between one and five years	Due after five years	Non- interest bearing	Total	Range of weighted average effective interest rates
Financial assets								
Cash and balances at central banks	-	-	-	-	-	29,025	29,025	
Items in the course of collection from other banks	-	-	-	-	-	522	522	
Derivatives	-	-	-	-	-	7,922	7,922	
Loans and advances to banks	4,692,672	102,500	95,000	-	-	-	4,890,172	0.36-0.59%
Loans and advances to customers	2,589,617	648,229	-	-	-	-	3,237,846	4.86-5.46%
Financial investments	1,342,656	232,379	277,092	1,136,509	31,093	35,780	3,055,509	1.98-2.17%
Total at 31 December 2010	8,624,945	983,108	372,092	1,136,509	31,093	73,249	11,220,996	
Financial liabilities								
Deposits by banks	34,519	-	-	-	-	-	34,519	0.21-0.53%
Customer accounts	9,125,179	323,575	207,967	49,955	338	-	9,707,014	0.52-0.73%
Items in course of transmission to other banks	-	-	-	-	-	10,642	10,642	
Derivatives	-	-	-	-	-	8,196	8,196	
Total at 31 December 2010	9,159,698	323,575	207,967	49,955	338	18,838	9,760,371	
Interest rate sensitivity gap	(534,753)	659,533	164,125	1,086,554	30,755	54,411	1,460,625	
Cumulative interest rate sensitivity gap	(534,753)	124,780	288,905	1,375,459	1,406,214			

(In US dollar thousands)

31 December 2010

31 December 2009	Due within three months	Due between three and six months	Due between six months and one year	Due between one and five years	Due after five years	Non-interest bearing	Total	Range of weighted average effective interest rates
Financial assets								
Cash and balances at central banks	-	-	-	-	-	34,280	34,280	
Items in the course of collection from other banks	-	-	-	-	-	41	41	
Derivatives	-	-	-	-	-	11,105	11,105	
Loans and advances to banks	3,608,454	27,520	11,092	-	-	-	3,647,066	0.37-0.91%
Loans and advances to customers	2,508,448	270,229	82,009	195,192	-	-	3,055,878	5.20-5.98%
Financial investments	1,889,065	117,905	171,401	1,047,607	4,166	43,519	3,273,663	2.20-4.39%
Total at 31 December 2009	8,005,967	415,654	264,502	1,242,799	4,166	88,945	10,022,033	
Financial liabilities								
Deposits by banks	125,732	-	-	-	-	-	125,732	0.31-1.51%
Customer accounts	7,600,146	366,464	202,766	51,190	235	-	8,220,801	0.67-1.73%
Items in course of transmission to other banks	-	-	-	-	-	12,717	12,717	
Derivatives	-	-	-	-	-	9,326	9,326	
Total at 31 December 2009	7,725,878	366,464	202,766	51,190	235	22,043	8,368,576	
Interest rate sensitivity gap	280,089	49,190	61,736	1,191,609	3,931	66,902	1,653,457	
Cumulative interest rate sensitivity gap	280,089	329,279	391,015	1,582,624	1,586,555			

Financial instruments included within 'Prepayments and accrued income', 'Other assets', 'Retirement benefit liabilities', 'Liabilities under insurance contracts', 'Accruals and deferred income', 'Provisions for liabilities and charges' and 'Other liabilities' have not been included in the analysis above and are all considered non-interest bearing.

(In US dollar thousands)

31 December 2010

26 Foreign currency exposures

(a) Balance sheet denominated in foreign currency

The group recognises that changes in foreign exchange rates can result in changes to profit and loss and other comprehensive income. In order to effectively mitigate this risk, the group matches assets and liabilities by currency to the greatest extent possible.

	2010	2009
Assets		
US and Bermuda dollars	8,781,292	8,312,969
Pound sterling	999,768	981,258
Euro	1,065,071	801,047
Japanese yen	241,831	199,931
Canadian dollars	232,740	165,347
Other currencies	526,129	296,848
Total assets	<u>11,846,831</u>	<u>10,757,400</u>
Liabilities and equity		
US and Bermuda dollars	8,819,215	8,305,023
Pound sterling	999,449	982,368
Euro	1,064,337	801,000
Japanese yen	241,713	200,055
Canadian dollars	232,527	164,155
Other currencies	489,590	304,799
Total liabilities and equity	<u>11,846,831</u>	<u>10,757,400</u>

At 31 December 2010, assets and liabilities in all currencies other than US and Bermuda dollars are matched to within 1% (2009: 3%) of each currency total and to within 0.3% (2009: 0.1%) of total assets. The group therefore considers that the overall risk of changes in foreign exchange rates to profit and loss and equity is not significant.

(b) Structural currency exposures

The group's structural foreign currency exposure is represented by the net asset value of its foreign currency equity and subordinated debt investments in subsidiary undertakings and associates. Gains or losses on structural foreign currency exposures are recognised in other comprehensive income. The group's management of structural foreign currency exposures is discussed in the 'Market risk management' section in Note 27.

27 Risk management

All of the group's activities involve measurement, evaluation, acceptance and management of some degree of risk, or combination of risks. The most important types of risk categories that the group are exposed to are market risk (including interest rate, equity price, foreign exchange and credit spread risk), liquidity risk, operational risks in various forms, insurance risk, credit risk (including cross-border risk), reputational risk and sustainability (environmental and social) risks. This note presents information about the group's exposure to each of the material risks, the group's risk governance framework, objectives, policies and processes for measuring and managing risk, and the group's management of capital.

(i) Risk governance

The risk management framework established by the group seeks to foster the continuous monitoring of the risk environment and an integrated evaluation of risks and their interdependencies.

Primary responsibility for managing risk at the group's operating entity levels lies with the relevant Chief Executive Officer, as custodian of the relevant balance sheets. In turn, the Chief Risk Officer and the group's internal controls division ('IC') have functional responsibility for the primary financial risk types, namely: credit, market, operational and security / fraud risks. The IC co-ordinates the development of the risk appetite, economic capital and stress-testing frameworks, in consultation with the finance and the asset and liability management divisions.

(ii) Risk management framework

The group's risk management policies, encapsulated in the HSBC Group Standards Manual is cascaded in a hierarchy of policy manuals throughout the group and are designed to support the formulation of risk appetite, guide employees and establish procedures for monitoring and controlling risks, with timely and reliable reporting to senior management. Personal accountability reinforced by the group's governance structure and instilled by training, helps to foster throughout the group a disciplined and constructive culture of risk management and control.

(a) Market risk management

Market risk is the risk that changes in interest rates, credit spreads, foreign exchange rates or equity and commodity prices will affect the group's income or the value of its holdings of financial instruments. Market risk arises on financial instruments which are valued at current market prices (mark-to-market basis) and those valued at cost plus accrued interest (accruals basis). The main valuation sources are securities prices, foreign exchange rates, interest rate yield curves and volatilities.

Trading risks arise from customer-related business and positions are valued on a mark-to-market basis.

Equity price risk is subject to regular monitoring by the group but is not currently significant in relation to the overall results and financial position.

The group manages market risk through risk limits assigned by HSBC. Traded Markets Development and Risk ('TMR'), a division within HSBC, develops risk management policies and measurement techniques and reviews limit utilisation on a daily basis. HSBC global risk limits are approved by TMR. Limits are set by product and risk type, using a combination of risk measurement techniques, including position limits, sensitivity limits, as well as value at risk limits at a portfolio level.

The group's interest rate risks relate exclusively to structural interest rate exposures managed under the limits described above. Structural interest rate risk arises primarily on accrual book positions and from the differing repricing characteristics of commercial and retail banking assets and liabilities.

The group assesses the structural interest rate risks which arise in the businesses and transfers these risks to the group's balance sheet management team. When the behavioural characteristics of a product differ from its contractual characteristics, the behavioural characteristics are assessed to determine the appropriate underlying interest rate risk. The Asset and Liability Committee ('ALCO') regularly monitors all such behavioural assumptions and interest rate risk positions to ensure they comply with established interest rate risk limits. In the course of managing interest rate risk, quantitative techniques and simulation models are used where appropriate to identify the potential net interest income and market value effects of these interest rate positions under different scenarios. The primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on net interest income whilst balancing the effect on the current net operating income stream and unrealised mark-to-market positions.

The table in Note 25 discloses the mismatching of the dates on which interest rates on assets and interest rates on liabilities are next reset to market rate on a contractual basis, or, if earlier, the dates on which the instruments mature. Contractual terms may not be representative of the behaviour of assets and liabilities and the group therefore manages its interest rate risk on the behavioural characteristics of its assets and liabilities.

A principal part of the group's management of market risk is to monitor the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling). The group aims to mitigate the effect of prospective interest rate movements, which could reduce future net interest income, while balancing the cost of such hedging activities on the current net operating income stream.

The models measure the effect on net interest income due to parallel and ramp movements of plus or minus 100 basis points in all yield curves. The sensitivities are illustrative only and are based on simplified assumptions as set out below. The figures represent the effect of the pro-forma movements in net interest income based on the projected yield curve scenarios and the group's current interest rate risk profile.

Change in 2011 projected net interest income arising from 100 basis points movement in yield curves (unaudited)	At 31 December 2010 increase (decrease)	At 31 December 2009 increase (decrease)
+100 basis points parallel	29,533	22,746
+100 basis points ramp	16,321	10,997
-100 basis points parallel	(20,029)	(31,152)
-100 basis points ramp	(13,683)	(24,979)

The scenarios are calculated by first establishing a base case projection for the following financial year using the current consolidated balance sheet. The base case assumes no change in volumes or margins across all currencies. The parallel scenario is calculated by impacting all interest margins by 100 basis points immediately while the ramp scenario simulates a margin impact of 25 basis points every 3 months. The prospective annual differences in net interest income, between the base case and the parallel and ramp cases respectively, are set out in the table above. The model is further simplified in the assumption that all currency yield curves rise and fall at the same time and does not incorporate any management response to changes in prospective interest rates. In particular, the model does not incorporate the proactive management of the interest rate risk profile undertaken by the group's ALCO and global markets division in order to minimise losses and optimise net income. In the falling interest rate scenarios for 2010, the low absolute interest rate levels in shorter maturities provide a natural 0% interest rate floor in the model.

The group's foreign exchange exposure comprises trading exposures and structural foreign currency translation exposure. Structural currency risk exists for the group in holding subsidiary company investments whose functional currencies are not the US dollar or Bermuda dollar.

(b) Liquidity risk management

The group manages its liquidity risk by:

- Modelling scenarios based on behavioural characteristics of individual classes of financial instruments;
- Monitoring balance sheet liquidity ratios against internal and regulatory requirements;
- Monitoring of depositor concentration both in terms of the overall funding mix and to avoid undue reliance on large individual depositors; and
- Maintaining liquidity and funding contingency plans.

These actions ensure the group adheres to HSBC liquidity policies and maintains sufficient liquidity to meet day-to-day needs and local regulatory requirements.

Core deposits (current accounts and savings deposits payable on demand or at short notice) form a significant part of the group's overall funding. Considerable importance is attached to this core deposit base which, over the years, has been stable and predictable. Additional information regarding liquidity risk is found in Note 24.

(c) Operational risk management

Operational risk is the risk of loss arising through fraud, unauthorised activities, error, omission, inefficiency, systems failure or from external events. It is inherent to every business organisation and covers a wide spectrum of issues.

The group manages this risk through a controls-based environment in which processes are documented, authorisation is independent and transactions are reconciled and monitored. This is supported by internal control reviews as well as an independent programme of periodic reviews undertaken by internal audit, and by monitoring external operational risk events, which ensure that the group adheres to best practice and actively learns from the publicised operational failures within the financial services industry.

The group has adopted the HSBC operational risk management process with annual compliance certification. The HSBC standards explain how the group manages operational risk by identifying, assessing, monitoring, controlling and mitigating the risk, rectifying operational risk events, and implementing any additional procedures required for compliance with local regulatory requirements. The processes undertaken to manage operational risk are determined by reference to the scale and nature of each business operation. The HSBC standard covers the following:

- Operational risk management responsibility is assigned at a senior management level within the business operation;
- Information systems are used to record the identification and assessment of operational risks and generate appropriate, regular management reporting;
- Operational risks are identified by risk assessments covering operational risks facing each business and risks inherent in processes, activities and products. Risk assessment incorporates a regular review of risks identified to monitor significant changes;
- Operational risk loss data is collected and reported to senior management. This report covers aggregate operational risk losses and details of incidents above a materiality threshold; and
- Risk mitigation, including insurance, is considered where this is cost-effective.

HSBC is in the process of implementing the “Advanced Measurement Approach” to operational risk, entailing the complete integration of the “Use Test”, which confirms that operational risk assessment is used within business decision making processes, the roll out of a global approach to classification and reporting of risk events and the preparation of key risk indicators by jurisdiction. Included in the process will be the assessment of controls implemented to mitigate operational risk.

Local management is responsible for implementation of the HSBC standards on operational risk, throughout their operations and where deficiencies are evident, these are required to be rectified within a reasonable timeframe.

(d) Insurance risk management

Insurance risk is the risk of incurring financial loss through an insured event, such as fraud, error or omission, fire, theft and natural disaster. The frequency and severity of losses are affected by several factors. The most significant are the effectiveness of HSBC's operational risk management and the individual insurance policy deductible. HSBC manages its operational risk through a controls-based environment, as explained more fully in (c) ‘Operational risk management’ above. All HSBC companies are required to share in HSBC's insurance risk assumed by HSBC Insurance (Bermuda) Limited (‘the Captive’), by retaining appropriate deductibles. The Captive was owned by the group for 2009 and effective 1 July 2010, it was disposed of to an HSBC affiliated entity (see Note 18).

The objective of the Captive is to enhance financial risk management in the HSBC Group through increased risk retention by transfer of insurance risk to the Captive where economically beneficial to do so. This provides the benefits of pricing stability, reduced counterparty risk, greater claims certainty, capture of insurance profits and improved insurance for the HSBC Group. The Captive retains a portion of the HSBC Group insurance risk and writes coverage for HSBC on a direct and indirect basis on a number of lines including, but not limited to, criminal, professional indemnity and directors' and officers' liability lines, personal accident, property and employers' liability.

The Board of Directors of the Captive is responsible for determining the Captive's underwriting strategy, and has appointed an underwriting committee to ensure the strategy is appropriately implemented and monitored. Specific responsibilities of the underwriting committee include:

- Risk selection;
- Acceptance of limits of liability / sums insured;
- Imposition of appropriate deductibles;
- Arms length premium pricing; and
- Claims investigation.

(In US dollar thousands)

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In addition to the work of the underwriting committee, insurance risk is also managed by performing an annual risk scenario analysis and stress test on the insurance risk underwritten by the Captive. Independent, qualified actuaries perform an annual actuarial valuation and assessment of insurance liabilities to ensure these accurately and adequately correspond to the projected future liquidity and cash flow requirements of the risks assumed.

(e) Credit risk management

Credit risk is the risk that a customer or counterparty of the group will be unable or unwilling to meet a commitment into which it has entered with a member of the group. It arises from lending, trade finance, treasury and other activities. The group has in place standards, policies and procedures for the control and monitoring of all such risks. Additional credit-related information is presented in Note 9 'Derivatives', Note 10 'Loans and advances to banks', Note 11 'Loans and advances to customers' and Note 12 'Financial investments'.

HSBC is responsible for the formulation of high-level credit policies. It also reviews the application of HSBC's universal credit risk rating system. HSBC's credit risk limits to counterparties in the financial and government sectors are managed centrally to optimise the use of credit availability and to avoid excessive risk concentration. Cross-border risk is controlled through the imposition of country limits, which are determined by taking into account economic and political factors, and local business knowledge, with sub-limits by maturity and type of business. Transactions with counterparties in higher risk countries are considered on a case-by-case basis.

Within the overall framework of the HSBC policy, the group has an established risk management process encompassing credit approvals, the control of exposures (including those to borrowers in financial difficulty), credit policy direction to business units and the monitoring and reporting of exposures both on an individual and a portfolio basis. The group's management is responsible for the quality of its credit portfolios and follows a credit process involving delegated approval authorities and credit procedures, the objective of which is to build and maintain risk assets of high quality. Regular reviews are undertaken to assess and evaluate levels of risk concentration, including those to individual industry sectors and products. Special attention is paid to the management of problematic loans. Where deemed appropriate, specialist units are established to provide intensive management and control to maximise recoveries of assets, which show early signs of potential impairment.

(f) Capital management*(i) Regulatory capital*

The group's lead regulator, Bermuda Monetary Authority (the "Authority"), sets and monitors capital requirements for the group as a whole under the Banks and Deposit Companies Act 1999. Individual banking operations of the group are directly supervised by their local regulators.

With effect from 1 January 2009, the group is required to comply with the provisions of the Basel II framework in respect of regulatory capital. Basel II is structured around three 'pillars': Pillar 1, 'minimum capital requirements', 'Pillar 2, 'supervisory assessment process' and Pillar 3, 'market discipline'. The "Revised Framework for Regulatory Capital Assessment" is the means by which Basel II is implemented in Bermuda. Although the basis for calculating capital changed, Tier 1 capital and total capital shown in the table below, 'Composition of regulatory capital', is not affected.

The Authority has granted approval to exclude insurance operations from the consolidated regulatory capital position and capital requirements under Basel II. The group's insurance operations are regulated by the Authority under The Insurance Act 1978, as amended under the Insurance Amendment Act 2006.

The group's total banking regulatory capital is analysed into two tiers:

- Tier 1; which includes ordinary share capital, share premium and retained earnings after deduction of goodwill and other intangible assets; and
- Tier 2; which consist of collective impairment allowances.

Various limits are applied to elements of the capital base. Total Tier 2 capital is limited to 100% of the Tier 1 capital. There are also restrictions on the level of collective impairment allowances that may be included in Tier 2 capital. Other deductions from capital include the carrying amounts of investments in subsidiaries that are not included in the regulatory consolidation, investments in the capital of banks and certain other regulatory items.

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The group's policy is to maintain a strong capital base so as to maintain creditor and market confidence and to sustain future development of the business. The group and its individual regulated operations have complied with all external imposed capital requirements throughout the period. There have been no material changes in the group's management of capital during the year.

The group's consolidated regulatory capital position under Basel II at 31 December was as follows:

Composition of regulatory capital

	<i>Notes</i>	2010	2009
Tier 1 capital			
Called up share capital	<i>30</i>	30,027	30,027
Share premium		388,652	388,652
Retained earnings		1,425,277	1,276,019
Less goodwill and other intangibles assets		<u>(220,386)</u>	<u>(221,052)</u>
Total Tier 1 capital		<u>1,623,570</u>	<u>1,473,646</u>
Tier 2 capital			
Collective impairment allowances	<i>11</i>	6,192	6,368
Deductions: Investments in insurance subsidiary and associates		(1,743)	(327,657)
Deductions: Investments in capital of other banks		(4,093)	(7,929)
Deductions: Off-balance sheet items of a capital nature		<u>-</u>	<u>(101,687)</u>
Total regulatory capital		<u><u>1,623,926</u></u>	<u><u>1,042,741</u></u>

The group has been granted approval by the Authority to adopt the standardised approach to credit and operational risk management. For credit risk, the standardised approach requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties. It groups other counterparties into broad categories and applies standardised risk weightings to these categories. Basel II also introduces an additional capital requirement for operational risk. The capital required for operational risk is calculated by applying a percentage to each of the eight defined revenue categories. The group continued to be exempt from market risk reporting requirements under Basel II from the Authority.

The second Pillar of Basel II involves both the group and the Authority to assess and agree the appropriate capital necessary to mitigate the impact of risks not fully captured by the credit risk measures ('Pillar 1'). The annual supervisory assessment process (SAP), undertaken by the Authority, aims to assess the group's risk profile and self assessment as documented in the Capital Assessment and Risk Profile (CARP). The completion of the SAP formed the basis for the final agreements on new statutory minimum capital requirements for the group going forward. The group has complied with all minimum capital requirements prescribed by the Authority in 2010 and 2009.

Pillar 3 of Basel II, implemented by the Authority in the second half of 2009, aims to encourage market discipline by the requirement of disclosures, quantitative and qualitative, to allow market participants to assess certain specified information on the scope of application of Basel II, capital, particular risk exposures, risk assessment processes, and hence the capital adequacy of the group. The most recent disclosure of the group, 'Capital and Risk Management Interim Pillar 3 Disclosures as at 30 June 2010' is published in the group's internet website in the 'About us' section.

(ii) *Capital allocation*

Although maximisation of return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the group to particular operations or activities, it is not the sole basis used for decision-making. Account is also taken of synergies, and the fit of the activity within the group's longer-term strategic objectives.

28 Litigation

In the ordinary course of business, the Bank and its subsidiaries are routinely defendants in, or parties to, a number of pending and threatened legal actions and proceedings. Management believes, based on information currently available to it and subject to the provisions taken, that the actions and proceedings and losses, if any, resulting from the final outcome thereof will not be material in the aggregate to the group's financial position or results of operations.

Bernard L. Madoff Investment Securities LLC

In December 2008, Bernard L. Madoff ('Madoff') was arrested for running a Ponzi scheme and a trustee was appointed for the liquidation of his firm, Bernard L. Madoff Investment Securities LLC ('Madoff Securities'), an SEC-registered broker-dealer and investment adviser. Since his appointment, the trustee has been recovering assets and processing claims of Madoff Securities customers. Madoff subsequently pleaded guilty to various charges and is serving a 150-year prison sentence. He has acknowledged, in essence, that while purporting to invest his customers' money in securities and, upon request, return their profits and principal, he in fact never invested in securities and used other customers' money to fulfill requests for the return of profits and principal. The relevant US authorities are continuing their investigations into his fraud, and have brought charges against others.

Various non-US HSBC companies provided custodial, administration and similar services to a number of funds incorporated outside the US whose assets were invested with Madoff Securities.

Based on information provided by Madoff Securities as at 30 November 2008, the purported aggregate value of these funds was \$8.4 billion, an amount that includes fictitious profits reported by Madoff. Based on information available to HSBC to date, we estimate that the funds' actual transfers to Madoff Securities minus their actual withdrawals from Madoff Securities during the time that HSBC serviced the funds totalled approximately \$4.3 billion.

Plaintiffs (including funds, fund investors, and the Madoff Securities trustee) have commenced Madoff-related proceedings against numerous defendants in a multitude of jurisdictions. Various HSBC companies have been named as defendants in suits in the US, Ireland, Luxembourg, and other jurisdictions. The suits (which include US class actions) allege that the HSBC defendants knew or should have known of Madoff's fraud and breached various duties to the funds and fund investors.

In December 2010, the Madoff Securities trustee commenced suits against various HSBC companies in the US bankruptcy court and in the English High Court. The US action (which also names certain funds, investment managers, and other entities and individuals) seeks \$9 billion in damages and additional recoveries from HSBC and the various co-defendants. It seeks damages against HSBC for allegedly aiding and abetting Madoff's fraud and breach of fiduciary duty. It also seeks, pursuant to US bankruptcy law, recovery of unspecified amounts received by HSBC from funds invested with Madoff, including amounts that HSBC received when it redeemed units HSBC held in various funds that invested with Madoff. HSBC acquired those fund units in connection with various financing transactions HSBC had entered into with various clients. The trustee's US bankruptcy law claims also seek recovery of fees earned by HSBC for providing custodial, administration and similar services to funds. The trustee's English action seeks recovery of unspecified transfers of money from Madoff Securities to or through HSBC, on the ground that the HSBC defendants actually or constructively knew of Madoff's fraud.

Between October 2009 and July 2010, Fairfield Sentry Limited and Fairfield Sigma Limited ('Fairfield'), funds whose assets were directly or indirectly invested with Madoff Securities, commenced multiple suits in the British Virgin Islands and the US against numerous fund shareholders, including various HSBC companies that acted as nominees for clients of HSBC's private banking business and other clients who invested in the Fairfield funds. The Fairfield actions seek restitution of amounts paid to the defendants in connection with share redemptions, on the ground that such payments were made by mistake, based on inflated values resulting from Madoff's fraud.

There are many factors which may affect the range of possible outcomes, and the resulting financial impact (if any), of the various Madoff-related proceedings, including (but not limited to) the circumstances of the fraud, the multiple jurisdictions in which the proceedings have been brought and the number of different plaintiffs and defendants in such proceedings. The cases where HSBC companies are named as a defendant are at an early stage. For these reasons, HSBC is unable to reliably estimate the aggregate liabilities, if any, or ranges of liabilities, that might arise as a result of all such claims. In any event, HSBC considers that it has good defences to these claims and will continue to defend them vigorously.

29 Related party transactions

The group classifies the Directors of the Bank and the members of the Senior Management Committee as the key management personnel of the group.

Particulars of transactions, arrangements and agreements entered into by the group with its key management personnel, connected persons and companies controlled by them or the group are as follows:

	Loans and mortgages	Deposits
Balance at 1 January 2009	4,648	8,657
Advances during the year	4,298	-
Repayments during the year	(742)	-
Other movements	-	2,199
Balance at 31 December 2009	<u>8,204</u>	<u>10,856</u>
Advances during the year	5,050	-
Repayments during the year	(1,086)	-
Other movements	-	6,291
Balance at 31 December 2010	<u>12,168</u>	<u>17,147</u>

The above transactions were made in the ordinary course of business and substantially on the same terms, including interest rates and security, as for comparable transactions with other employees of the group which are at favourable rates. Normal banking risks are associated with these transactions.

Other compensation to key management personnel

	2010	2009
Short-term employee benefits	9,614	10,227
Post-employment benefits	836	795
Share-based payments	2,739	2,602
	<u>13,189</u>	<u>13,624</u>

Amounts included in balance sheet due from HSBC and affiliated companies

	2010	2009
Derivatives	7,064	3,592
Loans and advances to banks	771,141	999,545
Financial investments	341,459	573,788
Prepayments and accrued income	-	9,086
Other assets	2,245	133,982

Amounts included in balance sheet due to HSBC and affiliated companies

	2010	2009
Deposits by banks	20,192	107,368
Derivatives	185	5,216
Liabilities under insurance contracts	-	216,943
Other liabilities	231	6,641

Amounts in income statement received from HSBC and affiliated companies

	2010	2009
Interest income	998	2,857
Fee income	9,564	16,645
Gross written insurance premiums	48,846	176,632
Other operating income	4,392	4,509

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Amounts in income statement paid to HSBC and affiliated companies

	2010	2009
Interest expense	177	1,459
Fee expense	2,500	2,561
Gross insurance claims and underwriting expenses incurred	43,481	108,793
General and administration expenses	37,315	32,895

There are no individually assessed loan impairment allowances in respect of outstanding balances in 2010 (2009: \$NIL). No impairment charges were recognised during the year in respect of loans to related parties (2009: \$NIL).

Segregated assets and liabilities

As part of the group's insurance holdings, the group owns HSBC Insurance (SAC) Limited ('SAC') which is a Bermuda incorporated company registered under the Segregated Accounts Companies Act 2000 and HSBC Insurance PCC Limited ('PCC') which is a Guernsey incorporated company registered under The Companies (Guernsey) Law, 2008. Both companies provide 'rent-a-captive' services including segregated cell arrangements. These programs cover professional indemnity, personal accident and travel, medical malpractice, property, casualty, workers compensation, marine and general liability risks. In 2010, there were 59 (2009: 42) segregated cell agreements in place and SAC agreed to write insurance for the participants and keep separate books of accounts for each program (the numbers of cell agreements are exact and not shown to the nearest thousand).

The assets and liabilities of the rent-a-captive program participants are legally segregated. Assets and liabilities amounting to \$104,767 (unaudited) (2009: \$159,172) of the unrelated participants are segregated from the general assets and liabilities of the group; are not under the control of the group and therefore are not consolidated into the accompanying income statement, statement of comprehensive income, balance sheet, statement of cash flows and statement of changes in equity of the group.

30 Equity

(a) Called up share capital and share premium

The total number of authorised ordinary shares at 31 December 2010 was 140,000,000 (2009: 140,000,000) with a par value of \$1 per share (2009: \$1 per share). The total number of shares issued and fully paid at 31 December 2010 was 30,026,671 (2009: 30,026,671). These figures and amounts are exact (not rounded or shown to the nearest thousand). Share premium comprises additional paid in capital in excess of the par value. Share premium is not ordinarily available for distribution.

(b) Dividends

A final dividend of \$80,000,000 (\$2.66 per ordinary share), was declared by the Board of Directors on 12 February 2010 in respect of the 2009 financial year. An interim dividend of \$60,300,000 (\$2.01 per ordinary share), was declared by the Board of Directors on 4 August 2010 in respect of the 2010 financial year. These figures and amounts are exact (not rounded or shown to the nearest thousand).

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