



## The HSBC Group

HSBC is one of the world's largest banking and financial services organisations, with around 6,600 offices in both established and faster-growing markets. HSBC aims to be where the economic growth is, connecting customers to opportunities, enabling businesses to thrive and economies to prosper, and ultimately helping people to fulfil their hopes and realise their ambitions.

HSBC serves around 58 million customers through four global businesses: Retail Banking and Wealth Management, Commercial Banking, Global Banking and Markets, and Global Private Banking. Its network covers 81 countries and territories in six geographical regions: Europe, Hong Kong, Rest of Asia-Pacific, Middle East and North Africa, North America and Latin America. HSBC's aim is to be acknowledged as the world's leading international bank.

Listed on the London, Hong Kong, New York, Paris and Bermuda stock exchanges, shares in HSBC Holdings plc are held by over 220,000 shareholders in 129 countries and territories.

In 2012, HSBC's reported profit before tax was USD 20,649 million and the underlying profit before tax was USD 16,385 million. Profit attributable to shareholders of the parent company was USD 14,027 million. Group total assets were USD 2,692 billion at 31 December 2012.

### Geographical distribution of results - Contribution to profit before tax:

Year ended 31 December 2012

|                              | USDm    | %      |
|------------------------------|---------|--------|
| Europe                       | (3,414) | (16.5) |
| Hong Kong                    | 7,582   | 36.7   |
| Rest of Asia-Pacific         | 10,448  | 50.6   |
| Middle East and North Africa | 1,350   | 6.5    |
| North America                | 2,299   | 11.1   |
| Latin America                | 2,384   | 11.6   |
| Profit before tax            | 20,649  | 100.0  |



This Registration Document was registered with the *Autorité des marchés financiers* on 25 April 2013 in accordance with article 212-13 of its General Regulation. It may be used in support of a financial transaction when supplemented by a Transaction Note that has received approval from the *Autorité des marchés financiers*. This document has been prepared by the issuer and is binding on its signatories.

## Annual Report and Accounts 2012

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## Report of the Board of Directors to the Annual General Meeting

*HSBC France is the subsidiary of one of the most solid banking groups in the world, the HSBC Group, which aims to be the world's leading international bank. In France, HSBC aims to become the partner of reference to assist French companies in their international development and individuals in the management of their assets.*

*In France, the business performance of Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets reflects the relevance of the global strategy of the HSBC Group.*

### **The businesses of HSBC France and developments in its organisation and structures**

#### Principal activities

HSBC France's strategy is based on a universal banking model and relies on a comprehensive range of banking and financial services aimed at a business and retail clientele wishing to benefit from the infrastructure and network of the HSBC Group, one of the world's leading financial organisations. HSBC France capitalised on the HSBC Group's strengths – its international presence, its solid financial position and its innovation in banking and technology. Its business activities are organised into four business units.

Retail Banking and Wealth Management includes Personal Financial Services, Asset Management and Insurance activities. Personal Financial Services offers individual services to personal and business customers with a holistic approach to their financial needs. Capitalising on the HSBC Group strengths, HSBC France continues its expansion policy in its target segment, wealth management. With a strong presence in the largest French cities, with almost 315 branches, including 32 HSBC *Premier* Centres and direct banking services, HSBC France is supported by teams of experts specialised according to customer profile and proposals meeting our customers' aspirations: HSBC *Premier* and HSBC Advance, as well as for their private or professional needs.

Private Banking offers products and services tailored to the needs of resident and international high-net-worth individuals, through the expertise of its discretionary and advisory management teams and strong synergies with HSBC France's other business lines, particularly with Commercial Banking and Global Banking.

Commercial Banking offers an extensive range of domestic and international products and services providing daily support to businesses ranging from very small enterprises to multinationals. It is supported by a recognised expertise in accompanying businesses in their international development, particularly in emerging markets, by the HSBC network throughout the world, by specialists in Cash management, Trade services and Factoring, by a domestic network specialised by type and size of business (11 Corporate Banking Centres, 51 "Centres d'Affaires Entreprises" dedicated to SMEs and 15 "Pôles Entrepreneurs" dedicated to very small enterprises) and by direct banking services for very small enterprises and associations.

HSBC's global and local scale makes it an ideal partner for large corporations and institutional investors, their projects and transactions, both in France and worldwide. HSBC offers a complete range of services both in Global Markets and Global Banking activities.

#### 2014 Strategic Plan

In 2011, HSBC France reiterated its aim to develop as a universal bank, through its 2014 Strategic Plan. This plan is in line with that of the HSBC Group and follows on from the strategy adopted by HSBC France in 2005, which aims to accelerate its growth while improving efficiency by:

- focusing on wealth management for personal customers;
- bolstering international connectivity for business customers;
- strengthening Global Banking and Markets positioning in Paris as a strategic hub for the HSBC Group; and
- strengthening synergies between businesses.

With this plan, HSBC France is aiming for greater efficiency by simplifying procedures and adapting the organisational structure of each business line. Implementation will not involve any forced redundancies. Furthermore, performances will be improved on the basis of a generally more competent organisational structure, made possible by an unprecedented training drive. More than 1,500 employees are to undergo training, primarily in commercial and reception activities.

In Retail Banking and Wealth Management, the plan aims to:

- improve the investment and advice offering in multi-management, discretionary management, advisory management, annuities solutions and brokerage platform to support the long-term investment needs of customers, particularly within the framework of preparations for retirement;
- further develop the wealth management expertise of staff, particularly within HSBC *Premier*, providing customers with products and services tailored to their individual expectations;
- address the demand for multi-channel services and increase HSBC France's *Premier* customer base by a third.

HSBC France aims to accelerate growth of its Private Banking activity in France through the opening of three new regional offices (bringing the network to six Private Banking regional offices), strengthening sales teams and increasing the synergies between the different businesses, in particular Commercial Banking.

Commercial Banking aims to continue to strengthen international capabilities by increasing the number of customer managers with an international focus, by strengthening Payments and Cash Management and Trade services teams dedicated to international and by developing the direct banking model, offering dedicated customer managers, longer branch opening hours and attractive banking packages for small business clients.

The Strategic Plan aims to consolidate the Global Banking and Markets platform so that it is able to fulfil its role as a strategic platform for Continental Europe and a centre of excellence in euro products and equity derivatives, in particular by increasing synergies with other countries and broadening the products offered to large corporate clients.

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#### Further simplification of the HSBC France group

The programme to simplify the HSBC France group structures continued, with the aim of dissolving units that no longer serve a purpose and selling or merging structures within the group in order to optimise and simplify the organisation. In 2012, 14 direct or indirect subsidiaries of HSBC France have left its organisational chart.

Therefore, in line with of the strategic review undertaken by the HSBC Group in early 2010 on the Asset Management business, the groupings of entities continued and resulted, on 31 October 2012, in the merger of the companies HSBC Wealth Managers and HSBC Global Asset Management Financial Services with HSBC Global Asset Management (France).

In addition, the company Valeurs Mobilières Elysées has completed the removal by the complete transfer of assets and liabilities of three of its subsidiaries. The company Foncière Elysées has done the same for two of its subsidiaries and has completed the liquidation of a third one.

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### The bank's performance in 2012

#### Economic situation

The eurozone sovereign debt crisis was preeminent in the first half of 2012 and eased gradually during the year as investors got convinced of the European Central Bank's (ECB) intervention willingness.

In February, the ECB conducted its second long-term refinancing operation (LTRO), allowing some respite for eurozone governments to restore their creditworthiness. This was pursued through fiscal tightening, which created a near-term drag on growth and did not ease pressures on Spain, Italy and especially Greece.

In June, the European Council set out a broad outline for a single supervisory mechanism for banks and integrated frameworks for fiscal and economic policy, which was followed by a commitment by the ECB President to do "whatever it takes" to preserve the euro, resulting in a bond rally. The December European Council meeting agreed the single banking supervisor to be in place at the earliest and by March 2014.

At the end of 2012, deleveraging was continuing, austerity continued to intensify in some countries, unemployment was rising and the recession deepening. More positively, there was an improvement in the economic environment as sentiment indicators stabilised.

In this uneven environment, HSBC in France's banking and Wealth Management operations resisted well, whereas Market activities benefitted from financial markets stabilisation.

The performance is analysed below from three different perspectives, prepared in accordance with IFRS standards as defined in Note 1<sup>1</sup> of the consolidated financial statements:

- HSBC's operations in France (managed perimeter);
- HSBC France's consolidated financial statements (legal perimeter);
- the country "France" as considered by HSBC Holdings plc in the contribution to the global results by geography.

Moreover, the performance of the perimeter of individual financial statements of HSBC France, prepared in accordance with principal accounting policies applicable in France to credit institutions<sup>2</sup>, is analysed in the Note "2012 Highlights" of the parent company financial statements, page 195.

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#### Contribution of France to the results of HSBC Group operations (managed perimeter)<sup>3</sup>

Under this perimeter, profit before tax was EUR 559 million compared with EUR 191 million in 2011. This good performance was mainly due to the strong increase in Global Banking and Markets activities and notably Rates activities, which suffered from a difficult situation in the second half of 2011 and benefitted from stabilisation in 2012.

All business lines display increasing profit before tax except Private Banking subject to an important restructuring spread over the years 2011 and 2012.

<sup>1</sup> See Note 1 of the consolidated financial statements page 106.

<sup>2</sup> See Note 1 of the parent company financial statements page 196.

<sup>3</sup> The comments on pages 3 to 5 relate to the contribution of France to the results of HSBC Bank plc operations, which includes the HSBC France group, including the results of entities legally owned by HSBC France but located outside France, i.e. the legal scope in its entirety, and also the Paris branch of HSBC Bank plc, which is engaged in equity derivative activities, as well as HSBC Assurances Vie (France) and HSBC Assurances IARD (France), to the exclusion of the costs of funding and the debt on acquisition recognised by HSBC Bank plc Paris Branch. The financial figures are presented according to the IFRS as adopted by the HSBC Group.

## Report of the Board of Directors to the Annual General Meeting (continued)

Net operating income showed a 16 per cent increase to EUR 2,391 million. The bulk of this arising from Markets activities, which benefitted from narrowing credit spreads for sovereign eurozone issuers. In a difficult environment, revenues slightly increased for Retail Banking, individuals and corporates. The impact of credit spreads on the fair value of own debt from EUR +124 million in 2011 to EUR -118 million in 2012, reflecting the decrease in HSBC France issuer credit spread, partially offsets the businesses' operational recovery.

Client related cost of risk, at EUR 117 million, after restatement of the impairment of Greek sovereign debt held by the Insurance business, slightly increased by 7 per cent compared with 2011, which had benefitted from releases in large corporates impairments. Despite the poor economic environment, loan loss rate remained at a low level globally (0.32 per cent of the loan book, after 0.30 per cent in 2011 and 0.39 per cent in 2010) notably in respect of individuals (with a 0.16 per cent of the loan book) and decreasing for SMEs.

Operating expenses decreased by 2 per cent to EUR 1,715 million, driven by the non-recurrence of restructuring costs incurred in 2011. The recurring cost base is well under control and only certain performance-related expenses increased in 2012 in relation with the strong revenue increase. Moreover, the bank is negatively impacted by the rise in some taxes. The cost efficiency ratio improved from 85 per cent to 72 per cent.

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### Performance by global business

Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets all enjoyed improved business momentum in France, reflecting the relevance of the deployment in France of HSBC Group's global strategy.

#### Retail Banking and Wealth Management

The Group's strategic decision to focus on Wealth Management clients enabled HSBC France to generate further business growth and improve its financial performance.

#### *Continued growth in HSBC Premier clientele*

Following the Group's strategic decision to focus clearly on Wealth Management, HSBC Premier continued to enjoy a strong business drive in France, with almost 45,000 new Premier relationships during 2012, a similar performance to the previous year.

The number of Premier clients totalled around 371,000 by the year-end, representing about 45 per cent of the entire retail customer base. In other words, almost one retail customer in every two is now an HSBC Premier client.

#### *Strong growth in residential mortgage lending*

In a French mortgage market down 32 per cent<sup>1</sup> in terms of new lending, HSBC France reported strong growth with EUR 2.7 billion in new residential mortgage loans, an increase of 39 per cent compared with 2011. The total customer loan book grew by 8 per cent over the year.

#### *Good momentum in life insurance*

HSBC in France also bucked the trend in life insurance, with gross new business of EUR 2 billion and positive money inflows throughout the year, in a French market down 8 per cent<sup>2</sup>.

#### *International capability makes the difference in Asset Management*

The Group's international expertise is increasingly appreciated by a Wealth Management clientele continuously seeking further diversification and performance, as witnessed by the 58 per cent growth in World Selection funds to EUR 723 million.

In Asset Management, the asset mix was more favourable, with a 9 per cent increase in medium and long-term funds and a strong growth in fixed-income products. This qualitative improvement is to be seen in a context of assets under management at EUR 68 billion at the end of December 2012 (-3 per cent compared to December 2011), with a 27 per cent fall in money market funds in a context of historically low interest rates, in line with a negative growth market at -1 per cent<sup>3</sup>.

#### *Growth in deposits*

In line with previous years, 2012 saw further growth in the deposit base, with an increase of 5 per cent to EUR 12.9 billion.

Assets managed for personal customers of the HSBC in France branch network rose from EUR 31.1 billion to EUR 32.8 billion.

#### *Strong business performance reflected in results*

Driven by this strong business momentum and despite pressure on deposit margins due to falling interest rates and a continued decline in asset management, Retail Banking and Wealth Management in France posted a 110 per cent increase in profit before tax to EUR 105 million and a 4 point improvement in the cost efficiency ratio compared to 2011.

#### Commercial Banking

In a subdued economic environment, Commercial Banking in France continued to develop, driven by the Group's strategy of combining local service with international capability.

#### *Stronger commitment to business expansion*

HSBC in France continued to support businesses in their growth, increasing its average commercial loan book from EUR 9.6 billion in 2011 to EUR 9.9 billion in 2012.

1 Banque de France.

2 Fédération Française des Sociétés d'Assurance.

3 Les Cahiers de l'Épargne.

Factoring confirmed further strong growth, with average factored receivables rising by 23 per cent over the year and revenue by 16 per cent.

For 2013, an additional lending envelope of EUR 1 billion has been allocated to business clients to support them in their international development.

#### *Continued breakthrough in international expansion*

The ability to support companies in their international growth enabled the bank to achieve, in 2012, a further 16 per cent increase in revenue generated outside France with French customers.

Trade Services reported further substantial growth of 24 per cent.

HSBC France now has 150 relationship managers covering the main economic growth areas in France specifically trained to provide SMEs with international support, in addition to the international network of business experts specialising in cross-border transactions coordinated by International Directors in the 20 countries that represent almost 80 per cent of the world's trade.

#### *A strategy now producing results*

Despite a poor macroeconomic environment in France, business activity and the bank's good name and reputation enabled Commercial Banking in France to post profit before tax of EUR 158 million, an increase of 14 per cent compared with 2011.

Despite heightened competition in deposits, the average deposit book grew by 6 per cent to EUR 10.6 billion and sight deposits by 10 per cent.

In a sluggish environment, loan impairment charges fell by 6 per cent to EUR 78 million in 2012 thanks mainly to strong risk management discipline, bringing the loan loss rate down to 0.7 per cent of the loan book compared with 0.8 per cent in 2012.

### **Global Banking and Markets**

In a more favourable economic climate in the eurozone, Global Banking and Markets in France continued to develop its business with a clientele of major corporates and institutional investors.

#### *Activity focusing on customer service*

Due to the preeminent market maker position of HSBC France in 13 of the 17 eurozone countries, there was substantial growth in fixed-income vanilla products compared with 2011, driven by narrowing sovereign credit spreads in the eurozone countries as a result of the ECB's forceful policy, coupled with the bank's strategic aim of being a leading player in the sovereign debt market. HSBC France ranked 5<sup>th</sup> among the primary dealers (*Spécialistes en Valeurs du Trésor* - SVTs) in 2012<sup>1</sup>.

Activity in structured fixed-income and equity products grew in 2012, with a notably good performance in Asia.

Other activities for major clients (corporate lending and structured finance, transaction banking, real estate, corporate finance and FX) enjoyed substantial growth.

Revenue from financial transactions, such as M&A and IPOs, were affected by the sluggish markets and the general downturn in these activities in 2012. However, HSBC France continued to support its corporate clients in some major deals such as Renault Nissan's acquisition of an interest in AvtoVAZ, Russia's leading car manufacturer, Charterhouse's sale of Fives, French leader in industrial engineering, and UnibailRodamco's EUR 750 million convertible bond issue.

The league tables and rankings reflect the bank's expertise in these activities. Examples include:

- global corporate bond issues in euros<sup>2</sup>: #4;
- public sector bond issues in Europe<sup>2</sup>: #2;
- convertible bond issues in France<sup>2</sup>: #3;
- rights issues in France<sup>2</sup>: #4;
- local authority bond issues in France<sup>2</sup>: #1.

#### *Return to a trend performance level*

In a more favourable macroeconomic climate, Global Banking and Markets turned the tide and generated pre-tax profit of EUR 410 million in 2012, a strong recovery compared to 2011.

By continuing to support French companies in their international development, the HSBC in France network was able to increase its revenue derived outside France with French clients by 8 per cent compared with 2011 to nearly USD 580 million.

### **Private Banking**

The process of reorganising Private Banking, which took place during 2011 and 2012, is now complete. Thanks to its clear focus on the strategic high-net-worth client segment, this business was able to generate renewed growth.

With its improved capability, Private Banking can now provide its clients with a broad, diversified range of investment and lending solutions, strengthened by synergies with the HSBC Group network.

Through its integration with HSBC France, Private Banking now has access to leading-edge operating platforms and economies of scale, helping to improve profitability.

1 Agence France Trésor.

2 Dealogic year 2012.

## Report of the Board of Directors to the Annual General Meeting (continued)

### HSBC France's consolidated results (legal perimeter)

The HSBC France's consolidated profit before tax amounts to EUR 388 million compared with EUR 59 million the previous year.

HSBC France reported a net operating income of EUR 2,096 million, increasing by 18 per cent compared with 2011. This good performance was mainly due to the strong increase in Markets activities and notably euro-denominated sovereign debt markets. Banking and Asset Management activities showed resilience in a sluggish environment.

The impact of credit spreads on the fair value of own debt burdened results, EUR -118 million in 2012 compared with a positive impact of EUR +124 million in 2011.

Loan impairment charges amount to EUR 117 million, an increase of 7 per cent over to the previous year, due to releases in some large corporates impairments recorded in 2011. Global delinquency rate is 0.32 per cent of the loan book.

Operating expenses at EUR 1,591 million, decreased by 1 per cent, reflecting the non-recurrence of restructuring costs incurred in 2011 offset by increase in certain taxes and performance-related expenses.

Net profit attributable to shareholders of the parent company amounted to EUR 320 million, 2.6 times greater than last year.

The liquidity ratio is 124 per cent at end 2012, well above the French regulatory requirements of 100 per cent. Advances to Core Funding Ratio<sup>1</sup>, internal to the HSBC Group, forerunner to future Basel III NSFR is 97 per cent, attesting HSBC France's solid liquidity position.

HSBC France's Core Tier One equity rose by EUR 201 million to reach EUR 4,133 million at end 2012. This includes a dividend payment of EUR 240 million proposed for approval to the Board of Directors in February 2013 then to the Annual General Meeting on 30 April 2013.

Risk-weighted assets before Basel I floor impact fell by EUR 6.4 billion to EUR 30.5 billion, mainly due to market risk-weighted assets, which decreased by EUR - 4.4 billion. Consequently, the Core Tier One ratio rose from 10.7 per cent to 13.5 per cent, well above the regulatory minimum. After the impact of Basel I floor, Core Tier 1 ratio stands at 12.6 per cent.

### Estimated Impact of the Basel committee's new rules

HSBC France had approximately EUR 1 billion of excess capital at 31 December 2012<sup>2</sup>. The bank considers it should be able to meet the stricter Basel III requirements. It is to be noted that the implementation of this reform planned on 1 January 2013 is delayed and the foreseeable date might be 1 January 2014.

<sup>1</sup> Ratio displaying loans and advances to customers as a percentage of the total of core customer deposits and term funding with a remaining maturity over one year.

<sup>2</sup> Measuring the capital requirement at 9 per cent of risk-weighted assets.

<sup>3</sup> The contribution of the country "France" to the results of HSBC Group includes the HSBC France group, excluding the results of entities legally owned by HSBC France but located outside France, and also includes the Paris branch of HSBC Bank plc, which is engaged in equity derivative activities, as well as HSBC Assurances Vie (France) and HSBC Assurances IARD (France), and including the costs of funding and the debt on acquisition recognised by HSBC Bank plc Paris Branch.

### Financial results for the country "France"<sup>3</sup> as considered by HSBC Holdings plc in the contribution to the global results by geography

In 2012, the country "France", as considered by the HSBC Group, contributed to the global profit before tax to USD 578 million (EUR 450 million), a strong increase compared to the year 2011.

Retail Banking and Wealth Management posted a USD 135 million (EUR 105 million) profit before tax, rising from 2011, thanks to a strong business drive and despite historically low interest rates.

Commercial Banking displayed a record profit before tax to USD 203 million (EUR 158 million), continuously supporting French corporates.

Pre-tax profit for Global Banking and Markets reached USD 514 million (EUR 400 million) in 2012, a strong recovery compared to 2011, driven by a strong performance in Global Markets activities.

### Proposed resolutions

The Board of Directors has drawn up the following resolutions presented at the Combined General Meeting on 30 April 2013.

#### Ordinary business

In Resolution 1, the Board proposes that the shareholders, having read the Board's management report, the Auditors' report on the financial statements and the reports of the Chairman and the Statutory Auditors on the practices of the Board and internal control and risk management procedures, approve the annual financial statements for the year ended 31 December 2012 as well as the transactions reflected in those statements or summarised in those reports.

Resolution 2 concerns the allocation of the 2012 net profit of EUR 601,189,983.50. Along with retained earnings of EUR 2,785,467,451.71, the profit available for distribution amounts to EUR 3,386,657,435.21. The dividend to be paid to the shareholders would be EUR 3.56 per share, for a total distribution of EUR 240,078,664.12. Therefore, retained earnings would amount to EUR 3,146,578,771.09. As the proposed dividend equals the interim dividend decided by the Board on 27 February 2013, there would be no final payment.

Resolution 3 proposes that the shareholders approve the consolidated financial statements at 31 December 2012, so as to comply with article L. 225-100 of the French Commercial Code, after having heard the Statutory Auditors' report on consolidated financial statements.



Resolution 4 proposes that the shareholders approve the related party agreements covered by article L. 225-38 of the French Commercial Code, after having heard the Statutory Auditors' report on these agreements.

Resolutions 5 and 6 propose that the shareholders ratify the Board's co-optations on 22 November 2012 of Mr Samir Assaf and on 27 February 2013 of Mr Lindsay Gordon, as Directors, to respectively replace Mr Stuart Gulliver and Mr Peter Boyles who have resigned.

Resolutions 7 to 10 propose that the shareholders renew the directorships of Mr Lindsay Gordon, Mr Thierry Moulounguet, Mr Peter Shawyer and Mr Jacques Veyrat for a term of three years ending with the Annual General Meeting that will be called to approve the financial statements of the year ending in 2015.

Resolution 11 proposes that the shareholders take note of the expiry of term of office of Mr Marcel Roulet as Director.

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#### Special business

As part of the harmonisation of practices in governance within the HSBC Group, it is proposed, in Resolution 12, to reduce from four to three years the term of office of Directors appointed or renewed in their mandates as from 30 April 2013.

To enable the company to build up its equity capital if necessary, or to take advantage of investment opportunities that may arise, Resolution 13 seeks authorisation for the Board to increase the company's share capital by up to EUR 100 million. The proposed resolution also allows this to be done by incorporation of reserves and share premiums.

Under article L. 225-129-6, indent 1 of the French Commercial Code, whenever the shareholders delegate authority to the Board to make a cash capital increase, the shareholders must also, at the same Extraordinary General Meeting, consider a draft resolution to make a capital increase under the conditions set forth in articles L. 3332-18 and following of the French Labour Code, that is reserved for participants in an employee share-ownership plan.

Furthermore, under Article L. 225-129-6, indent 2 of the French Commercial Code, every three years the shareholders must consider a draft resolution to make a capital increase reserved for employees of the company and its affiliated companies under the conditions set forth in article L. 3332-18 of the French Labour Code, if the shares held collectively or individually during the lock-up period by employees of the company and companies affiliated with it within the meaning of article L. 225-180 of the French Commercial Code represent less than 3 per cent of the share capital. At 31 December 2012, employees held no equity interest in the company under the conditions of article L. 225-102 of the French Commercial Code. The most recent previous resolution submitted to you pursuant to article L. 225-129-6, indent 2 of the French Commercial Code, resulted from the Annual General Meeting of 11 May 2010.

To comply with the aforementioned legal requirements, we ask you in Resolution 14 to decide on the principle of granting an authority to the Board to increase the share capital by issuing shares reserved for participants in the employee share ownership plan.

This resolution is presented to you to meet a legal obligation, but your Board is not disposed to make a capital increase of this kind, given that employees of the company are already able to participate in capital increases reserved for them under the Employee Share Ownership Plan of the HSBC Group. You are therefore requested to reject this resolution.

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#### Powers (Resolution 15)

The 15<sup>th</sup> and last resolution is intended to grant full powers to the bearer of an original, a copy or an excerpt of the minutes of this General Meeting to carry out the required formalities.

## Senior Executives

### Directors and members of the Executive Committee



#### **Jean Beunardeau**

*Chief Executive Officer, Head of Global Banking and Markets France.*

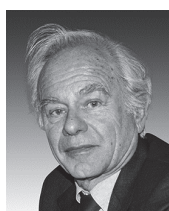
Age 51. Graduated from Ecole Polytechnique, Telecom engineer and Master of Economy, he began his career at the Ministry of Finance, mainly at the Treasury. He became Technical Advisor to the Prime Minister in 1995. He joined HSBC France in 1997 in Corporate Finance and became Managing Director in 2000. He was appointed co-Head of CIBM mainly in charge of Corporate and Investment Banking in March 2004. In 2005, he was appointed Senior Corporate Vice-President. In September 2007, he was appointed Head of Global Banking and Markets. Since 1 February 2010, he has been appointed Deputy CEO and Deputy to the CEO, in addition to his current role as Head of Global Banking and Markets France. In November 2010, he was appointed Head of Global Banking, Continental Europe, HSBC Group. Since 10 January 2012, he has been appointed CEO and retains his role as Head of Global Banking and Markets France.



#### **Gilles Denoyel**

*Deputy Chief Executive Officer, Deputy to the CEO, Chief Risk Officer.*

Age 58. Graduate of the Ecole des Mines de Paris, the Institut d'Etudes Politiques and the Ecole Nationale d'Administration. In 1981, he was appointed *Inspecteur des Finances* (Financial Controller) at the Ministry of Finance. In 1985, he entered the French Treasury, where he successively held responsibilities on the Interministerial Committee for Industrial Reconstruction (CIRI) and in the Insurance Department, before being put in charge of the French Privatisation Programme. In June 1996, he joined HSBC France as Chief Financial Officer. He became Group General Secretary, member of the Executive Committee, put in charge of Logistic and Operations in 1998 and was appointed Senior Corporate Vice-President Finance in March 2000. In March 2004, he was appointed Deputy Chief Executive Officer of HSBC France, in charge of the support functions and the finance support services. In January 2006, he was appointed Deputy Chief Executive Officer of HSBC France, in charge of the Asset Management activities, the Insurance activities and the non-finance support services. Since September 2007, he has been responsible for all risk management and control activities, and also for relations with the regulatory supervisors. Since 10 January 2012, he has been appointed Deputy to the CEO.



#### **Philippe Pontet**

*Chairman Investment Banking.*

Age 70. He joined HSBC France in 2005 as Vice-Chairman of Corporate Finance Europe. In February 2005, he was appointed member of HSBC France's Board. At the end of August 2007, he was appointed member of HSBC's New European Advisory council. Over the last 30 years he has held a number of leading positions in the French banking and industrial sectors, including Chairman and CEO of the banking group Crédit Industriel et Commercial; Chairman and CEO of Framatome; and Chairman of AREVA prior to joining HSBC in January 2005. Since September 2007, he has been Chairman Investment Banking.

## Other members of the Executive Committee

|                               |   |
|-------------------------------|---|
| <b>Edward Archer</b>          | Head of Private Banking   |
| <b>Anne-Lise Bapst</b>        | Head of Communication   |
| <b>Miguel Barrieras</b>       | Head of Commercial Banking  |
| <b>Marine de Bazelaire</b>    | Head of Corporate Sustainability  |
| <b>Xavier Boisseau</b>        | Head of Global Markets  |
| <b>Loïc Bonnat</b>            | Head of Principal Investments   |
| <b>Hubert Bouxin</b>          | Co-Head of Global Banking   |
| <b>Anne-Catherine Colleau</b> | Head of Operational Risk and Internal Control   |
| <b>Myriam Couillaud</b>       | Head of Human Resources   |
| <b>Laurent Facque</b>         | Head of Compliance  |
| <b>Matthieu Kiss</b>          | Chief Financial Officer   |
| <b>Marc de Lapérouse</b>      | Head of Legal   |
| <b>Mathilde Lemoine</b>       | Chief Economist - French Economic Research Department   |
| <b>Nathalie Léonard</b>       | Head of Tax   |
| <b>Malachy McAllister</b>     | Co-Head of Global Banking   |
| <b>Philippe Moiroud</b>       | Chief Operating Officer, HSBC France,<br>and Chief Operating Officer, Global Banking and Markets France |
| <b>François Mongin</b>        | Head of Group Audit France  |
| <b>Matteo Pardi</b>           | Head of Asset Management  |
| <b>Emmanuel Rémy</b>          | Head of Credit  |
| <b>Pierre Ruhlmann</b>        | Head of Retail Banking and Wealth Management  |
| <b>Jean-Pierre Wiedmer</b>    | Head of Insurance   |

## Composition of the Board of Directors

### Composition of the Board of Directors of HSBC France on 27 February 2013<sup>1</sup>

**Samir Assaf** *Born in 1960*

Holds 1 HSBC France share. First elected: 2012. Term ends: 2016.

*Principal position:*

Member of the Group Management Board. Chief Executive Officer Global Banking and Markets, HSBC Group. Chairman of the Board of Directors, HSBC France (since 22 November 2012). Member of the HSBC France Nomination and Remuneration Committee.

*Other directorships in the HSBC Group:*

Member of the Supervisory Board, HSBC Trinkaus & Burkhardt AG. Directorship expired in 2012: Director, HSBC Bank Egypt S.A.E.

*Résumé:*

Joined CCF in 1994 from Group Total, where he was Head of Treasury. At CCF, he was appointed Head of Markets in 1998. He joined HSBC in 2000 when the bank acquired CCF. Started at HSBC as Head of Global Markets at HSBC France and Head of Fixed Income Trading, Europe. In 2006, promoted to Head of Global Markets, Europe and Middle-East. In January 2008, he became Head of Global Markets and a Group General Manager in May 2008. On 1 January 2011, he was appointed Group Managing Director and a member of the Group Management Board. Since 22 November 2012, he has been appointed Chairman of the Board of Directors of HSBC France.

**Jean Beunardeau** *Born in 1962<sup>2</sup>*

Holds 1 HSBC France share. First elected: 2008. Last re-elected: 2010. Term ends: 2014.

*Principal position:*

Chief Executive Officer, HSBC France (since 10 January 2012).  
Head of Global Banking and Markets, France.

*Other directorships in the HSBC Group:*

Chairman of the Board, HSBC Global Asset Management (France) (since 10 February 2012). Director, Valeurs Mobilières Elysées. Director, HSBC Assurances Vie (France) (since 14 March 2012). Directorships expired in 2012: Deputy CEO, HSBC France. Director, HSBC Real Estate Leasing (France). Director, HSBC Global Asset Management (France) (permanent representative of HSBC France).

*Other directorships outside of the HSBC Group:*

Director, Institut de la Gestion Déléguée. Director and Treasurer, Fondation ESTP (since March 2012). Directorship expired in 2012: Chairman, X-Banque.

**Gilles Denoyel** *Born in 1954<sup>2</sup>*

Holds 1 HSBC France share. First elected: 2004. Last re-elected: 2010. Term ends: 2014.

*Principal position:*

Deputy CEO, Deputy to the CEO, Chief Risk Officer, HSBC France.

*Other directorships in the HSBC Group:*

Vice-Chairman of the Board, HSBC Assurances Vie (France). Director, HSBC Assurances IARD (France). Director, HSBC Bank A.S. (since 24 January 2012). Director, HSBC Global Asset Management (France) (permanent representative of HSBC France) (since 10 February 2012). Directorship expired in 2012: Director, HSBC Global Asset Management (France).

*Other directorships outside of the HSBC Group:*

Director, DCNS. Director, Fonds de Garantie des Dépôts. Director, MEDEF (permanent representative of HSBC France). Director and Treasurer, Association Française des Banques. Chairman, Groupement des Banques Etrangères en France.

<sup>1</sup> As far as their directorship at HSBC France is concerned, the address of HSBC France's Directors and Senior Executives is the company's registered office, 103 avenue des Champs-Élysées, 75419 Paris Cedex 08, France.

<sup>2</sup> Résumé available on page 8.

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**Véronique Duquesne** *Born in 1964*

Holds 1 HSBC France share. First elected: 2012. Term ends: 2016.  
Director elected by employees.

*Principal position:*

Processing Officer in Administration and Support Unit at Global Banking Agency and Operations, HSBC France.

*Résumé:*

Joined HSBC France in 1986.

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**Michel Gauduffe** *Born in 1959*

Holds 1 HSBC France share. First elected: 2008. Last re-elected: 2012. Term ends: 2016.  
Director elected by employees.

*Principal position:*

Deputy Head of the Limoges branch, HSBC France.

*Other directorships in the HSBC Group:*

Deputy Chairman of the Board, Institution de Prévoyance Vernet. Deputy Chairman of the Board, Institut de Gestion des Retraites Supplémentaires de la Caisse de Retraites HSBC France. Member of the Supervisory Board, France Actionnariat Fonds.

*Other directorship outside of the HSBC Group:*

Director, APICIL – ARC.

*Résumé:*

Joined HSBC France in 1981.

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**Martine Gerow** *Born in 1960*

Holds 1 HSBC France share. First elected: 2012. Term ends: 2016.  
Independent Director. Member of the HSBC France Audit and Risk Committee.

*Principal position:*

Executive Vice-President Finance, PagesJaunes Groupe.

*Résumé:*

Internal Auditor at PPG Industries in France and in the USA (1983-1985) and Strategy Consultant within The Boston Consulting Group in New York until 1989. From 1989 to 2002, held various positions within the Strategy and Development Department of the Pepsico Group then Chief Financial Officer of Pepsico in France. From 2002 to 2007, Chief Financial Officer - Beverage Division then Group Financial Controller of the Danone Group. From 2008 to 2010, Chief Financial Officer of the Smithfield Group then Chief Financial Officer of the Campofrio Food Group. In 2010, Executive Vice-President in charge of Finance, Purchasing and IT of the PagesJaunes Group.

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**Lindsay Gordon** *Born in 1952*

Holds 1 HSBC France share. First elected: 2013. Term ends: 2013<sup>1</sup>.  
Independent Director. Member of the HSBC France Audit and Risk Committee.

*Other directorships:*

Co-Chair, University of British Columbia Capital Campaign. Governor and Co-Founder, C.H.I.L.D. Foundation.

*Résumé:*

British and Canadian nationality. He joined HSBC Bank Canada in 1987 and has served in various roles in Toronto and Vancouver including Senior Executive Vice-President, Chief Credit Officer, Senior Vice-President and Head of Special Credit, and Vice-President Toronto Commercial Banking. He was appointed Chief Operating Officer in December 1999 then President and Chief Executive Officer of HSBC Bank Canada from October 2003 to 5 January 2013, date of his retirement.

<sup>1</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.

## Composition of the Board of Directors (continued)

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### **Philippe Houzé** *Born in 1947*

Holds 1 HSBC France share. First elected: 1999. Last re-elected: 2012. Term ends: 2016.

Independent Director. Chairman of the HSBC France Nomination and Remuneration Committee.

*Principal position:*

Chairman of the Management Board, Groupe Galeries Lafayette.

*Other directorships<sup>1</sup>:*

Chairman, Union du Grand Commerce de Centre-Ville (UCV). Member of the Board of Directors, National Retail Federation (NRF-USA). Elected member, Chambre de Commerce et d'Industrie de Paris. Directorships expired in 2012: Director, HSBC Bank plc. Director, Casino, Guichard-Perrachon.

*Résumé:*

Director of Galeries Lafayette since 1974. Chairman of Monoprix since 1994. Chairman of UCV and member of the Chambre de Commerce et d'Industrie de Paris since 2005.

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### **Anne Méaux** *Born in 1954*

Holds 1 HSBC France share. First elected: 2011. Term ends: 2015.

Independent Director.

*Principal position:*

Chairman, Image 7.

*Other directorships:*

Chairman, Com Sept Finance. Chairman, Image 8 (since May 2012). Managing Director, Anne Méaux Conseil. Member of the Advisory Committee, Women's Forum. Deputy Chairman, Association Force Femmes.

*Résumé:*

Attached to the press relations department of the Elysée palace from 1976 to 1981 then Communication Officer for Valéry Giscard d'Estaing, former President of the French Republic and for the UDF parliamentary group in the French National Assembly from 1981 to 1986. From 1986 to 1988, Communication Officer to the cabinet of Alain Madelin (French Ministry of Industry). Since 1988, Chairman of Image 7 which she founded in 1988.

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### **Thierry Moulouquet** *Born in 1951*

Holds 1 HSBC France share. First elected: 2009. Term ends: 2013<sup>2</sup>.

Independent Director. Chairman of the HSBC France Audit and Risk Committee.

*Other directorship in the HSBC Group:*

Independent Director, HSBC Bank plc (since July 2012).

*Other directorships outside of the HSBC Group:*

Director, Fimalac. Director, Fitch Rating Group Inc. Director, Groupe Lucien Barrière. Director, Valéo. Directorship expired in 2012: Director, SsangYong Motor Co. Ltd.

*Résumé:*

After having held several positions in the French public service, he joined the Finance Department of Renault in 1991. From 1999 to 2003, Senior Vice-President, Chief Financial Officer, Member of the Executive Committee and of the Board of Directors of Nissan. Until 30 June 2010, Executive Vice-President and Chief Financial Officer of the Renault Group, and then, until 31 March 2011, Director and Special Adviser to the President of the Renault-Nissan Alliance.

<sup>1</sup> For the most part, appointments held in companies which do not belong to the group in which the Director holds his principal position.

<sup>2</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.

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**Philippe Pontet** *Born in 1942*<sup>1</sup>

Holds 1 HSBC France share. First elected: 2005. Last re-elected: 2011. Term ends: 2015.

*Principal position:*

Chairman Investment Banking, HSBC France.

*Other directorship in the HSBC Group:*

Director, Valeurs Mobilières Elysées.

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**Guillaume Praud** *Born in 1976*

Holds 1 HSBC France share. First elected: 2012. Term ends: 2016.

Director elected by employees.

*Principal position:*

Head of the branch Premier International Direct, HSBC France.

*Résumé:*

Joined HSBC France in 2000.

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**Philippe Purdy** *Born in 1958*

Holds 1 HSBC France share. First elected: 2004. Last re-elected: 2012. Term ends: 2016.

Director elected by employees.

*Principal position:*

Customer service, Mandelieu branch, HSBC France.

*Résumé:*

Joined HSBC France in 1982.

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**Marcel Roulet** *Born in 1933*

Holds 1 HSBC France share. First elected: 1996. Last re-elected: 2009. Term ends: 2013<sup>2</sup>.

Independent Director.

*Other directorships:*

Chairman of the Supervisory Board, Gimar & Cie SCA. Directorship expired in 2012: Censor, Eurazeo.

*Résumé:*

*Ingénieur général des télécommunications.* Honorary Chairman of France Télécom. Chairman of France Télécom from 1991 to 1995. Chairman and Chief Executive Officer of Thomson from 1996 to 1997 and Thomson CSF (now Thales) from 1996 to 1998.

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**Peter Shawyer** *Born in 1950*

Holds 1 HSBC France share. First elected: 2005. Last re-elected: 2009. Term ends: 2013<sup>3</sup>.

Independent Director. Member of the HSBC France Audit and Risk Committee.

*Other directorships in the HSBC Group:*

Independent Director, Member of the Audit Committee and Member of the Risk Committee, HSBC Bank plc.

*Other directorships outside of the HSBC Group:*

Chairman, British International Holdings Limited. Chairman, Ingenious Media Holdings. Chairman, Ingenious Asset Management Limited. Director, Ingenious Asset Management International Limited. Director, FP Holdings Limited.

*Résumé:*

British nationality. He dedicated his entire career to Deloitte & Touche. He was Managing Partner and member of the Executive Committee at Deloitte & Touche in London until 2004.

<sup>1</sup> *Résumé available on page 8.*

<sup>2</sup> *Director retiring by rotation and not standing for re-election at the Annual General Meeting to be held on 30 April 2013.*

<sup>3</sup> *Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.*

## Composition of the Board of Directors (continued)

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### **Antonio Simoes** *Born in 1975*

Holds 1 HSBC France share. First elected: 2012. Last re-elected: 2012. Term ends: 2016.

*Principal position:*

Deputy Chief Executive Officer, HSBC Bank plc and Head of the bank in the United Kingdom (since 1 November 2012).  
Head of Retail Banking and Wealth Management, Europe, HSBC Bank plc (since 1 January 2012).

*Other directorships in the HSBC Group:*

Director, HSBC Bank plc (since 1 February 2012). Director, HSBC Bank A.S. (since 24 January 2012). Director, HSBC Life UK Limited (from 1 November to 13 December 2012). Director, HSBC Assurances Vie (France) (from 22 October to 13 December 2012).

*Résumé:*

Portuguese nationality. Joined HSBC in 2007 from McKinsey & Co, where he was a Partner in the London office. From September 2007 to September 2011, Group Head of Strategy, HSBC Holdings plc; from October 2009 to December 2011, Group Head of Strategy and Planning and Chief of Staff to the Group CEO, HSBC Holdings plc. Appointed Group General Manager in 2011.

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### **Brigitte Taittinger** *Born in 1959*

Holds 1 HSBC France share. First elected: 2008. Last re-elected: 2012. Term ends: 2016.  
Independent Director.

*Other directorships:*

Director, Ensemble Orchestral de Paris. Director, Opéra Comique. Directorship expired in 2012: Chairman and CEO, Annick Goutal.

*Résumé:*

Advertising Manager for Publicis from 1984 to 1988. Marketing Department of Groupe du Louvre from 1988 to 1990. Chairman and CEO of Annick Goutal from 1991 to 2012.

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### **Jacques Veyrat** *Born in 1962*

Holds 1 HSBC France share. First elected: 2009. Term ends: 2013<sup>1</sup>.  
Independent Director. Member of the HSBC France Nomination and Remuneration Committee.

*Principal position:*

Chairman, Impala SAS.

*Other directorships:*

Director, Poweo Direct Energie. Director, Imerys. Director, ID Logistics Group. Member of the Supervisory Board, Eurazeo. Directorship expired in 2012: Director, Direct Energie.

*Résumé:*

After having held various positions of responsibility in several French ministries, he joined the Louis Dreyfus Group in 1995. In 1998, he set up LDCOM, renamed Neuf Telecom in 2004 and Neuf Cegetel in 2005. In April 2008, he left Neuf Cegetel when it was sold to SFR. In May 2008, he was appointed Chairman of the Louis Dreyfus Group. In 2011, he left the Louis Dreyfus Group and created the Impala Group.

<sup>1</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.



## Directorships held<sup>1</sup> by the members of the Board of Directors (composition at 27 February 2013)

Information as at 31 December of each year from the year of appointment at the HSBC France Board of Directors.

| Director's name<br>Principal position   | First<br>elected | Term<br>ends | 2012   | 2011   | 2010  | 2009  | 2008  |
|---|------------------|--------------|--|--|---|---|---|
| <b>Samir Assaf</b><br>Member of the Group<br>Management Board.<br>Chief Executive<br>Officer, Global<br>Banking and Markets,<br>HSBC Group.<br>Chairman of the<br>Board of Directors,<br>HSBC France. | 2012             | 2016         | Directorships in<br>the HSBC Group:<br>Chairman of the<br>Board of Directors,<br>HSBC France.<br>Member of the<br>Supervisory Board:<br>HSBC Trinkaus &<br>Burkhardt AG.   | –  | –   | –   | –   |
| <b>Jean Beunardeau</b><br>Chief Executive<br>Officer, HSBC France<br>Head of Global<br>Banking and Markets,<br>France.  | 2008             | 2014         | Directorships in<br>the HSBC Group:<br>Director and CEO:<br>HSBC France.<br>Chairman of the<br>Board: HSBC Global<br>Asset Management<br>(France).<br>Director: Valeurs<br>Mobilières Elysées,<br>HSBC Assurances<br>Vie (France).<br>Directorships<br>outside of the<br>HSBC Group:<br>Director: Institut<br>de la Gestion<br>Déléguée. Director<br>and Treasurer:<br>Fondation ESTP. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Director: Valeurs<br>Mobilières Elysées,<br>HSBC Global Asset<br>Management<br>(France) (permanent<br>representative of<br>HSBC France),<br>HSBC Real Estate<br>Leasing (France).<br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman:<br>X-Banque.<br>Director: Institut<br>de la Gestion<br>Déléguée. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Chairman of the<br>Board: Foncière<br>Elysées.<br>Director: Nobel,<br>HSBC Global Asset<br>Management<br>(France) (permanent<br>representative of<br>HSBC France),<br>HSBC Real Estate<br>Leasing (France).<br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman:<br>X-Banque.<br>Director: Amicale<br>des Anciens Elèves<br>de Polytechnique,<br>Institut de la<br>Gestion Déléguée. | Directorships in<br>the HSBC Group:<br>Director:<br>HSBC France,<br>HSBC Epargne<br>Entreprise (France),<br>Nobel, HSBC Global<br>Asset Management<br>(France) (permanent<br>representative<br>of HSBC France).<br>Chairman of the<br>Board: Foncière<br>Elysées.<br>Directorships<br>outside of the<br>HSBC Group:<br>Director: X-Banque,<br>Amicale des<br>Anciens Elèves de<br>Polytechnique,<br>Institut de la<br>Gestion Déléguée. | Directorships in<br>the HSBC Group:<br>Director:<br>HSBC France,<br>HSBC Epargne<br>Entreprise (France),<br>Nobel, HSBC Global<br>Asset Management<br>(France) (permanent<br>representative<br>of HSBC France).<br>Chairman of the<br>Board: Foncière<br>Elysées.<br>Directorships<br>outside of the<br>HSBC Group:<br>Director: X-Banque,<br>Amicale des<br>Anciens Elèves de<br>Polytechnique,<br>Institut de la<br>Gestion Déléguée. |

<sup>1</sup> For the most part, appointments held in companies which do not belong to the group in which the Director holds his principal position.

## Composition of the Board of Directors (continued)

| Director's name<br>Principal position   | First<br>elected | Term<br>ends | 2012  | 2011  | 2010  | 2009  | 2008   |   |
|---|------------------|--------------|---|---|---|---|--|---|
| <b>Gilles Denoyel</b><br>Deputy CEO,<br>Deputy to the CEO,<br>Chief Risk Officer,<br>HSBC France. | 2004             | 2014         | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>HSBC Assurances<br>IARD (France),<br>HSBC Bank A.S.,<br>HSBC Global Asset<br>Management<br>(France) (permanent<br>representative of<br>HSBC France).<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative of<br>HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Treasurer:<br>Association<br>Française des<br>Banques.<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>HSBC Assurances<br>IARD (France),<br>HSBC Global Asset<br>Management<br>(France).<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative of<br>HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Treasurer:<br>Association<br>Française des<br>Banques. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>Halbis Capital<br>Management<br>(France),<br>HSBC Assurances<br>IARD (France),<br>HSBC Global Asset<br>Management<br>(France),<br>Sinopia Asset<br>Management.<br>Member of the<br>Supervisory Board:<br>HSBC Private<br>Bank France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative of<br>HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Treasurer:<br>Association<br>Française des<br>Banques. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>Halbis Capital<br>Management<br>(France),<br>HSBC Assurances<br>IARD (France),<br>HSBC Global Asset<br>Management<br>(France),<br>Sinopia Asset<br>Management.<br>Member of the<br>Supervisory Board:<br>HSBC Private<br>Bank France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative of<br>HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Treasurer:<br>Association<br>Française des<br>Banques. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>Halbis Capital<br>Management<br>(France),<br>HSBC Assurances<br>IARD (France),<br>HSBC Global Asset<br>Management<br>(France),<br>Sinopia Asset<br>Management.<br>Member of the<br>Supervisory Board:<br>HSBC Private<br>Bank France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative of<br>HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Treasurer:<br>Association<br>Française des<br>Banques.<br>Member of the<br>Orientation<br>Committee:<br>Euronext. | Directorships in<br>the HSBC Group:<br>Director and Deputy<br>CEO: HSBC France.<br>Vice-Chairman of<br>the Board:<br>HSBC Assurances<br>Vie (France).<br>Director:<br>Halbis Capital<br>Management<br>(France),<br>HSBC Assurances<br>IARD (France),<br>HSBC Global Asset<br>Management<br>(France),<br>Sinopia Asset<br>Management.<br>Member of the<br>Supervisory Board:<br>HSBC Private<br>Bank France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: Société de<br>Financement de<br>l'Economie<br>Française, DCNS,<br>Fonds de Garantie<br>des Dépôts,<br>MEDEF (permanent<br>representative<br>of HSBC France).<br>Chairman:<br>Groupement des<br>Banques Etrangères<br>en France.<br>Member of the<br>Board and<br>Treasurer:<br>Association<br>Française<br>des Banques.<br>Member of the<br>Orientation<br>Committee:<br>Euronext. |
| <b>Véronique Duquesne</b><br>Processing Officer<br>in ASU at GBAO,<br>HSBC France.                | 2012             | 2016         | Director elected<br>by employees:<br>HSBC France.   | -   | -   | -   | -  |   |

| Director's name<br>Principal position  | First<br>elected | Term<br>ends | 2012   | 2011  | 2010  | 2009  | 2008   |
|--|------------------|--------------|--|---|---|---|--|
| <b>Michel Gauduffe</b><br>Deputy Head of the<br>Limoges branch,<br>HSBC France.                | 2008             | 2016         | Directorships in<br>the HSBC Group:<br>Director elected<br>by employees:<br>HSBC France.<br>Vice-Chairman of<br>the Board:<br>Institution de<br>Prévoyance Vernet,<br>Institut de Gestion<br>des Retraites<br>Supplémentaires<br>de la Caisse<br>de Retraites<br>HSBC France.<br>Member of the<br>Supervisory Board:<br>France Actionnariat<br>Fonds.<br><br>Directorship<br>outside of the<br>HSBC Group:<br>Director:<br>APICIL - ARC.           | Directorships in<br>the HSBC Group:<br>Director elected<br>by employees:<br>HSBC France.<br>Vice-Chairman of<br>the Board,<br>Institution de<br>Prévoyance Vernet,<br>Institut de Gestion<br>des Retraites<br>Supplémentaires<br>de la Caisse<br>de Retraites<br>HSBC France.<br>Member of the<br>Supervisory Board:<br>France Actionnariat<br>Fonds.<br><br>Directorship<br>outside of the<br>HSBC Group:<br>Director: AGIRA.  | Directorships in<br>the HSBC Group:<br>Director elected<br>by employees:<br>HSBC France.<br>Vice-Chairman of<br>the Board,<br>Institution de<br>Prévoyance Vernet,<br>Institut de Gestion<br>des Retraites<br>Supplémentaires<br>de la Caisse<br>de Retraites<br>HSBC France.<br>Directorship<br>outside of the<br>HSBC Group:<br>Director: AGIRA.  | Directorships in<br>the HSBC Group:<br>Director elected<br>by employees:<br>HSBC France.<br>Chairman of the<br>Board: Institution<br>de Prévoyance<br>Vernet.<br><br>Directorship<br>outside of the<br>HSBC Group:<br>Director: AGIRA.  | Directorships in<br>the HSBC Group:<br>Director elected<br>by employees:<br>HSBC France.<br>Chairman of the<br>Board: Institution<br>de Prévoyance<br>Vernet.<br>Member of the<br>Supervisory Board:<br>HSBC France<br>Sécurité Régularité<br>Equilibre<br>Dynamique.<br><br>Directorship<br>outside of the<br>HSBC Group:<br>Director: AGIRA.   |
| <b>Martine Gerow</b><br>Executive Vice-<br>President Finance,<br>PagesJaunes<br>Groupe.        | 2012             | 2016         | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.   | -   | -   | -   | -  |
| <b>Philippe Houzé</b><br>Chairman of the<br>Management Board,<br>Groupe Galeries<br>Lafayette. | 1999             | 2016         | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Management<br>Board: Groupe<br>Galeries Lafayette.<br>Chairman:<br>Union du Grand<br>Commerce de<br>Centre-Ville (UCV).<br>Member of the<br>Board of Directors:<br>National Retail<br>Federation<br>(NRF-USA).<br>Elected member:<br>Chambre de<br>Commerce et<br>d'Industrie de Paris. | Directorships in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Management<br>Board: Groupe<br>Galeries Lafayette.<br>Director: Casino,<br>Guichard-<br>Perrachon.<br>Chairman:<br>Union du Grand<br>Commerce de<br>Centre-Ville (UCV).<br>Member of the<br>Board of Directors:<br>National Retail<br>Federation<br>(NRF-USA).<br>Elected member:<br>Chambre de<br>Commerce et<br>d'Industrie de Paris. | Directorships in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Management<br>Board: Groupe<br>Galeries Lafayette.<br>Director: Casino,<br>Guichard-<br>Perrachon.<br>Chairman:<br>Union du Grand<br>Commerce de<br>Centre-Ville (UCV).<br>Member of the<br>Board of Directors:<br>National Retail<br>Federation<br>(NRF-USA).<br>Elected member:<br>Chambre de<br>Commerce et<br>d'Industrie de Paris. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Management<br>Board: Groupe<br>Galeries Lafayette.<br>Director: Casino,<br>Guichard-<br>Perrachon.<br>Vice-Chairman:<br>Union du Grand<br>Commerce de<br>Centre-Ville (UCV).<br>Member of the<br>Board of Directors:<br>National<br>Retail Federation<br>(NRF-USA).<br>Elected member:<br>Chambre de<br>Commerce et<br>d'Industrie de Paris. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Management<br>Board: Groupe<br>Galeries Lafayette.<br>Director: Casino,<br>Guichard-<br>Perrachon.<br>Member of the<br>Executive Board:<br>MEDEF.<br>Member: Union du<br>Grand Commerce<br>de Centre-Ville<br>(UCV),<br>Association<br>Internationale des<br>Grands Magasins.<br>Member of the<br>Board of Directors:<br>National Retail<br>Federation<br>(NRF-USA).<br>Elected member:<br>Chambre de<br>Commerce et<br>d'Industrie de Paris. |

## Composition of the Board of Directors (continued)

| Director's name<br>Principal position   | First<br>elected | Term<br>ends      | 2012   | 2011   | 2010   | 2009   | 2008   |
|---|------------------|-------------------|--|--|--|--|--|
| <b>Anne Méaux</b><br>Chairman,<br>Image 7.  | 2011             | 2015              | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: Image 7,<br>Image 8, Com Sept<br>Finance.<br>Managing Director:<br>Anne Méaux<br>Conseil.<br>Member of the<br>Advisory<br>Committee:<br>Women's Forum.<br>Deputy Chairman:<br>Association Force<br>Femmes. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: Image 7,<br>Com Sept Finance.<br>Managing Director:<br>Anne Méaux<br>Conseil.<br>Member of the<br>Advisory<br>Committee:<br>Women's Forum.<br>Deputy Chairman:<br>Association Force<br>Femmes. | -  | -  | -  |
| <b>Thierry Moulouquet</b><br>Company Director.  | 2009             | 2013 <sup>1</sup> | Directorships in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: Fimalac,<br>Fitch Rating<br>Group Inc, Groupe<br>Lucien Barrière,<br>Valéo.   | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: Fimalac,<br>Fitch Rating Group<br>Inc, Groupe Lucien<br>Barrière, SsangYong<br>Motor Co. Ltd,<br>Valéo.  | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France. | -  |
| <b>Philippe Pontet</b><br>Chairman Investment<br>Banking,<br>HSBC France.                     | 2005             | 2015              | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>Valeurs Mobilières<br>Elysées.   | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>Valeurs Mobilières<br>Elysées.   | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>Nobel.     | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>Nobel.     | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>Nobel. |
| <b>Guillaume Praud</b><br>Head of the branch<br>Premier International<br>Direct, HSBC France. | 2012             | 2016              | Director elected<br>by employees:<br>HSBC France.  | -  | -  | -  | -  |
| <b>Philippe Purdy</b><br>Customer service,<br>Mandelieu branch,<br>HSBC France.               | 2004             | 2016              | Director elected<br>by employees:<br>HSBC France.  | Director elected<br>by employees:<br>HSBC France.  | Director elected<br>by employees:<br>HSBC France.                              | Director elected<br>by employees:<br>HSBC France.                              | Director elected<br>by employees:<br>HSBC France.                          |

<sup>1</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.

| Director's name<br>Principal position  | First<br>elected | Term<br>ends      | 2012   | 2011  | 2010  | 2009   | 2008   |
|--|------------------|-------------------|--|---|---|--|--|
| <b>Marcel Roulet</b><br>Company Director.  | 1996             | 2013 <sup>1</sup> | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Supervisory Board:<br>Gimar & Cie SCA.  | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Supervisory Board:<br>Gimar<br>Finances SCA.<br>Censor:<br>Eurazeo.  | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Supervisory Board:<br>Gimar<br>Finances SCA.<br>Director:<br>France Télécom.<br>Censor:<br>Eurazeo.  | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Supervisory Board:<br>Gimar<br>Finances SCA.<br>Member of<br>the Supervisory<br>Board:<br>Eurazeo. Director:<br>France Télécom.<br>Censor: Thomson. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman of the<br>Supervisory Board:<br>Gimar<br>Finances SCA.<br>Member of the<br>Supervisory Board:<br>Eurazeo. Director:<br>France Télécom,<br>Thales<br>(permanent<br>representative<br>of TSA).<br>Censor: Cap<br>Gemini, Thomson. |
| <b>Peter Shawyer</b><br>Company Director.  | 2005             | 2013 <sup>2</sup> | Directorships in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: British<br>International<br>Holdings Limited,<br>Ingenious Media<br>Holdings, Ingenious<br>Asset Management<br>Limited.<br>Director: Ingenious<br>Asset Management<br>International<br>Limited, FP<br>Holdings Limited. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: British<br>International<br>Holdings Limited,<br>Ingenious Media<br>Holdings, Ingenious<br>Asset Management<br>Limited.<br>Director: Ingenious<br>Asset Management<br>International<br>Limited, FP<br>Holdings Limited. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: British<br>International<br>Holdings Limited,<br>Ingenious Media<br>Holdings, Ingenious<br>Asset Management<br>Limited.<br>Director: Ingenious<br>Solar UK VCT 1 plc. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: British<br>International<br>Holdings Limited,<br>Ingenious Media<br>Holdings.  | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France,<br>HSBC Bank plc.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman: British<br>International<br>Holdings Limited,<br>Ingenious Media<br>Holdings.  |
| <b>Antonio Simoes</b><br>Deputy Chief<br>Executive Officer,<br>HSBC Bank plc<br>and Head of the bank<br>in the United Kingdom. | 2012             | 2016              | Directorships in the<br>HSBC Group:<br>Director:<br>HSBC France,<br>HSBC Bank plc,<br>HSBC Bank A.S.   | –   | –   | –  | –  |

<sup>1</sup> Director retiring by rotation and not standing for re-election at the Annual General Meeting to be held on 30 April 2013.

<sup>2</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.

## Composition of the Board of Directors (continued)

| Director's name<br>Principal position             | First<br>elected | Term<br>ends      | 2012   | 2011  | 2010  | 2009  | 2008   |
|---|------------------|-------------------|--|---|---|---|--|
| <b>Brigitte Taittinger</b>                        | 2008             | 2016              | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Director: Ensemble<br>Orchestral de Paris,<br>Opéra Comique.   | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Annick Goutal.<br>Director: Ensemble<br>Orchestral de Paris,<br>Opéra Comique.   | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Annick Goutal.<br>Director: Ensemble<br>Orchestral de Paris,<br>Opéra Comique.   | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Annick Goutal.<br>Director: Ensemble<br>Orchestral de Paris,<br>Opéra Comique.<br>Member of the<br>Board:<br>Ensemble<br>Intercontemporain.                            | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Annick Goutal.<br>Director: Ensemble<br>Orchestral de Paris,<br>Opéra Comique.<br>Member of the<br>Board:<br>Ensemble<br>Intercontemporain. |
| <b>Jacques Veyrat</b><br>Chairman,<br>Impala SAS. | 2009             | 2013 <sup>1</sup> | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman Impala<br>SAS.<br>Director: Poweo<br>Direct Energie,<br>Imerys, ID Logistics<br>Group.<br>Member of the<br>Supervisory Board:<br>Eurazeo. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman Impala<br>SAS.<br>Director: Direct<br>Energie, Imerys,<br>ID Logistics Group,<br>Poweo.<br>Member of the<br>Supervisory Board:<br>Eurazeo. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Louis Dreyfus SAS.<br>Director: Direct<br>Energie, Imerys.<br>Member of the<br>Supervisory Board:<br>Eurazeo.<br>Chairman of the<br>Supervisory Board:<br>Kurosawa BV. | Directorship in the<br>HSBC Group:<br>Independent<br>Director:<br>HSBC France.<br><br>Directorships<br>outside of the<br>HSBC Group:<br>Chairman and CEO:<br>Louis Dreyfus SAS.<br>Director: Direct<br>Energie, Imerys.<br>Member of the<br>Supervisory Board:<br>Eurazeo.<br>Chairman of the<br>Supervisory Board:<br>Kurosawa BV. | –  |

<sup>1</sup> Director standing for re-election at the Annual General Meeting to be held on 30 April 2013.

## Chairman's report on corporate governance and internal control and risk management procedures

*Under article L. 225-37 of the French Commercial Code, the Chairman of the Board of Directors of any French company issuing financial instruments admitted for trading on a regulated market is required to report to shareholders annually on the composition of the Board of Directors and on the application of the principle of balanced representation of men and women on the Board, the preparation and organisation of the Board's work, the internal control and risk management procedures and any restrictions on the powers of the Chief Executive Officer. This report is attached to the report referred to in articles L. 225-100, L. 225-102, L. 225-102-1 and L. 233-26.*

*I am pleased to present my report in this respect for the year ended 31 December 2012. Management is responsible for defining and implementing adequate and effective internal control and risk management procedures with oversight by the Board of Directors. This report has been drawn up in close collaboration with the main divisions concerned and in association with the Statutory Auditors.*

*The first part of this report, regarding corporate governance, was submitted to the Nomination and Remuneration Committee on 27 February 2013 and the second part, on internal control and risk management procedures to the Audit and Risk Committee, on 21 February 2013. The Board then approved the whole report on 27 February 2013.*

*The internal control and risk management regulations and procedures described herein apply to HSBC France and to all its consolidated subsidiaries.*

### CHAIRMAN'S REPORT ON CORPORATE GOVERNANCE

#### Corporate Governance Code

In accordance with law no. 2008-649 of 3 July 2008 concerning the adaptation to French law of Directive 2006/46/EC of 14 June 2006, the company shall, as a priority, refer to the Corporate Governance Code for listed companies published in December 2008, and amended in April 2010, by the AFEP and the MEDEF, taking account of its status as an unlisted subsidiary, in preparing the report required under article L. 225-37 of the French Commercial Code. This code may be viewed at the head office.

The HSBC Group attaches a great deal of importance to respecting corporate governance rules, both for itself and for its subsidiaries. However, as HSBC France is a 99.9 per cent owned subsidiary of the HSBC Group and as its capital securities are not admitted to trading on a regulated market, some principles of the Corporate Governance Code have been adapted as for example some of the duties of the Nomination and Remuneration Committee. HSBC France's Board of Directors therefore no longer decides on share award plans as the shares awarded to HSBC France employees are now HSBC shares. HSBC France applies the British corporate governance rules (the Combined Code on Corporate Governance) referred to by parent company HSBC Holdings plc in certain areas, in particular as regards share awards.

Other exceptions to the compliance with the Corporate Governance Code's recommendations for listed companies are specified below in this Report.

#### Board of Directors

##### Composition of the Board

At 31 December 2012, the Board of Directors had 17 members, including:

- the Chairman of the Board of Directors; the Chief Executive Officer; the Deputy Chief Executive Officer;
- the Investment Banking Chairman of HSBC France; the Deputy Chief Executive Officer of HSBC Bank plc;
- eight Directors having no special relationship with the company and who may be deemed independent with respect to all criteria defined in the AFEP/MEDEF report, particularly regarding banking relationships; however, two of their numbers have been serving as a Director for more than twelve years. Nonetheless, the Nomination and Remuneration Committee found that this criterion alone did not call into question their independence of judgement *vis-à-vis* the company, even though it constitutes an exception to the criteria defined in the AFEP/MEDEF report;
- four Directors elected or re-elected by the employees in 2012 for a term of four years, in accordance with the provisions of the French order of 21 October 1986.

Two Directors are non-French nationals. Other than the Directors elected by employees, the Board comprises three women and ten men. The average age of the Directors in office is 55.6.

In 2012, the Board's composition changed as follows:

- on 10 January 2012, the Board of Directors appointed Jean Beunardeau as Chief Executive Officer of HSBC France, for the term of his directorship, replacing Christophe de Backer who resigned;
- on 22 February 2012, the Board of Directors co-opted Antonio Simoes as a Director. On 15 May 2012, the Annual General Meeting (AGM) then ratified this co-opting and renewed his appointment for a period of four years;
- on 15 May 2012, the AGM renewed the term of office of Stuart Gulliver, Philippe Houzé, Antonio Simoes and Brigitte Taittinger for a period of four years; the directorship of Igor Landau ended at this meeting;
- on 15 May 2012, the AGM appointed Martine Gerow as a Director for a period of four years from 1 November 2012;
- at the election on 26 September 2012, Véronique Duquesne and Guillaume Praud were elected as Directors by employees and Michel Gauduffe and Philippe Purdy were re-elected;
- on 22 November 2012, the Board of Directors co-opted Samir Assaf as a Director and appointed him as Chairman of the Board, replacing Stuart Gulliver who resigned.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

At each of the meetings of 10 January and 22 November 2012, the Board of Directors has confirmed the decision made since July 2007 to separate the functions of Chairman of the Board of Directors and Chief Executive Officer.

In accordance with the recommendations of the AFEP-MEDEF report, the Nomination and Remuneration Committee reviewed the position of the Directors whose term of office expired at the AGM on 15 May 2012, and proposed that the Board vote to re-appoint them, taking into account their skills and active contribution to the work done by the Board.

Since the Combined General Meeting held on 12 April 2000, the Directors' term of office has been four years. The expiry dates of the terms of office are staggered so as to ensure a smooth transition when they are renewed. In order to align the Directors' terms of office within the HSBC Group, a resolution will be submitted to the shareholders at the Combined General Meeting to be held on 30 April 2013 to reduce this term from four to three years.

### The Board's work in 2012

As a general rule, before each Board meeting, the Directors receive an agenda together with the draft minutes of the previous Board meeting. In the week prior to the meeting, they also receive background information on agenda items, and a few days ahead of the meeting, a summary of key financial indicators. In the case of highly confidential issues, which cannot be disclosed in advance, the information is provided during the meeting itself. Furthermore, Directors are regularly advised of significant events affecting the company and receive the relevant documents.

The Board of Directors met five times during 2012, with an average attendance rate of 87.3 per cent compared with 96.5 per cent in 2011:

- 10 January 2012 (attendance rate: 88.9 per cent),
- 22 February 2012 (attendance rate: 76.5 per cent),
- 15 May 2012 (attendance rate: 82.4 per cent),
- 25 July 2012 (attendance rate: 94.1 per cent),
- 22 November 2012 (attendance rate: 94.4 per cent).

In 2012, the Board of Directors reviewed the quarterly, half-yearly and annual financial statements and approved the half-yearly and annual accounts. During each meeting, the Board reviewed the operations, results and balance sheet of HSBC France. In particular, it also reviewed the bank's liquidity situation, and at the meeting held on 15 May 2012, the Board approved the budget for 2012. The Board reviewed the liquidity contingency plan (meeting on 22 November 2012).

At each of its meetings, the Board of Directors examined the group's results, business growth and position for each of its activities. It was informed on a regular basis by the Chairman of the Board of Directors, who is also Chief Executive Officer of the HSBC Group, of the HSBC Group's development and results, as well as its latest news. Independent Directors shared with the Board their view of the economic situation and economic conditions in their business sector.

With respect to changes to organisational structures, the Board of Directors approved the dissolution without liquidation of Vernet Expansion by means of universal transfer of its assets to HSBC France, as this company no longer had any activity (meeting on 22 February 2012). At its meeting on 25 July 2012, the Board approved the projects to merge HSBC Private Wealth Managers and HSBC Global Asset Management Financial Services with HSBC Global Asset Management (France), in keeping with the restructuring of the Asset Management business line, of which the Board had been kept informed since 2010.

At each meeting, the Board of Directors discussed the consequences of the crisis affecting the eurozone on the bank's activities. It examined the group's situation with regard to risks: credit risk, market risk with, in particular, monitoring of exposure to eurozone government bonds, results of the internal stress tests conducted by HSBC France, as well as litigation, compliance, operational risks and information security risk. It was informed of the main projects of regulatory changes and of their impacts on HSBC France. At each of its meetings, the Board of Directors examined the risk appetite statement making it possible to assess performance as regards the level of risk accepted by the Board.

At its meeting on 15 May 2012, the Board reviewed the Annual Report prepared in accordance with articles 42, 43 and 43-1 of regulation 97-02, sent to the *Autorité de contrôle prudentiel*. It was kept informed of audits and investigations carried out by various authorities, in particular the *Autorité de contrôle prudentiel*, the *Autorité des marchés financiers* and the Financial Services Authority, along with their findings and replies from HSBC France. It approved the Chairman's report on corporate governance and internal control and risk management procedures (meeting on 22 February 2012). It also examined the mediator's report concerning his activity during 2011 (meeting on 15 May 2012).

At each meeting, the CEO commented on the Internal audit work, in particular audit reports graded "not satisfactory" and changes in the number of open recommendations.

In the area of human resources, the Board was informed of the talent management policy (meeting on 22 February 2012).

At the meeting on 25 July 2012, HSBC France's sustainability policy and its key initiatives were commented.

The work of the Board Committees was set out in periodic, detailed reports from their respective Chairmen and was debated during Board meetings. Within this framework, the Board was kept informed about the various points of action identified by the Audit and Risk Committee, particularly as regards how risks are taken into account in the remuneration policy, business continuity, anti-money laundering and third-party introducers.

Apart from these major issues, the Board also discussed various other issues which are legally its responsibility.



## Board committees

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### Nomination and Remuneration Committee

#### Composition of the Nomination and Remuneration Committee

Chairman:

- Philippe Houzé (independent) Appointed 1999 and 2009 as Chairman

Members :

- Jacques Veyrat Appointed 2010
- Stuart Gulliver Appointed 2009 until November 2012
- Samir Assaf Appointed November 2012

In November 2012, the Board appointed Samir Assaf as a member of the Nomination and Remuneration Committee, replacing Stuart Gulliver, because although he is Chairman of the Board of Directors, he is not an executive officer of HSBC France and receives no remuneration or directors' fees from HSBC France for serving in his capacity as Chairman of the Board. The Board therefore considered him to be independent for purposes of giving his opinion on HSBC France's remuneration policy and discussing the remuneration of its Executive Directors. Moreover, he lends the Committee his experience in the area of compensation of financial market professionals, among others, and his knowledge of the rules defined by the HSBC Group. He can also make valuable contributions in drawing up succession plans for the management team.

#### The Nomination and Remuneration Committee's missions

The Committee's main tasks are as follows:

- making proposals to the Board of Directors regarding the appointment of Directors and members and Chairmen of the Board's specialist committees according to the desired balance in the composition of the Board as well as to the specific skills and reputation of the applicants;
- proposing a Chairman and a CEO to the Board, and proposing Deputy CEOs to the Board on the CEO's recommendation, for succession planning purposes or in the event of a vacancy;
- examining all remuneration of Executive Directors;
- making proposals and recommendations to the Board concerning remuneration, pension and protection plans, additional pension contributions, benefits in kind and various cash entitlements of Executive Directors;
- making recommendations on Directors' remuneration and, in particular, the distribution of Directors' fees;
- issuing opinions and recommendations on the executive remuneration policy and particularly on the remuneration structure;
- in accordance with regulation 97-02, carrying out an annual review of the remuneration policy and more particularly, the share of variable compensation paid to

market professionals and Executive Directors, to ensure that they are consistent with the HSBC Group's policy and comply with French standards;

- making preparations for the Board's examination of corporate governance issues.

The Committee's recommendations on Executive Directors' remuneration are presented after prior approval by the Remuneration Committee of HSBC Holdings plc.

Moreover, in carrying out these duties and responsibilities, the Committee may consult any adviser or expert as it deems appropriate.

#### The Nomination and Remuneration Committee's work in 2012

The Committee met five times in 2012, with an attendance rate of 80 per cent. Its main work was as follows:

- it made proposals to the Board on changes in Senior Management's composition, following Christophe de Backer's resignation: appointment of Jean Beunardeau as Chief Executive Officer of HSBC France and renewal of Gilles Denoyel as Deputy Chief Executive Officer, and proposals to the Board on the conditions of Christophe de Backer's departure (meeting on 10 January 2012);
- it made proposals to the Board on chairmanship's change, following Stuart Gulliver resignation: appointment of Samir Assaf as Chairman of the Board of HSBC France and renewal of Jean Beunardeau as Chief Executive Officer and of Gilles Denoyel as Deputy Chief Executive Officer (meeting on 21 November 2012);
- it made proposals to the Board on changes in the Board's composition, with a concern for gender balance of the Board, and on the appointments of new Directors in 2012: Antonio Simoes (meeting on 22 February 2012) and Martine Gerow (meeting on 7 May 2012), and of an additional Director in 2013 (meeting on 21 November 2012);
- it made proposals to the Board on renewing the term of office of four Directors at the Annual General Meeting. A proposal was made to renew the term of office of Brigitte Taittinger (Director since 2008), Stuart Gulliver (Director since 2009), Philippe Houzé (Director since 1999) and Antonio Simoes (Director since 2012) (meeting on 22 February 2012);
- it reviewed each Director's independence on the basis of the criteria defined in the AFEP-MEDEF code, to which HSBC France chose to refer, but also of criteria regarding skills and independence of thought (meeting on 22 February 2012);
- it made proposals to the Board on changes in Board Committees' composition: appointments of Martine Gerow as a Member of the Audit and Risk Committee and of Samir Assaf as a member of the Nomination and Remuneration Committee (meeting on 21 November 2012);
- it made proposals to allow the Board to approve, in agreement with HSBC Holdings plc, the terms of the remuneration of Jean Beunardeau and Gilles Denoyel,

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

setting out the fixed and variable elements of their remuneration and the number of shares without performance conditions, to be awarded to them (see section "Directors' remuneration") (meeting on 22 February 2012);

- it reviewed the 20 highest remunerations (meeting on 22 February 2012);
- it reviewed HSBC's general remuneration policy in France, taking into account regulations concerning in particular risk control and the contribution of the Risk Management and Compliance functions to the process for determining bonuses (meeting on 25 January 2011). At its meeting on 22 February 2012, the Committee reviewed the list of employees identified as not entirely complying with the risk and compliance rules and their associated remuneration;
- it reviewed the first part of the Chairman's report on corporate governance (meeting on 22 February 2012).

The Chairman of the Committee reported to the Board on its work at the Board meetings on 10 January, 22 February, 15 May and 22 November 2012. All of the Committee's work was submitted to the Board for approval.

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### Audit and Risk Committee

#### Composition of the Audit and Risk Committee

Chairman:

- Thierry Moulouquet Appointed 2009  
and 2010 as Chairman  
(independent)

Members:

- Martine Gerow Appointed November 2012  
(independent)
- Peter Shawyer Appointed 2005  
(independent)

The three Committee members are highly qualified in the areas of finance and accounting, in risk analysis and in internal control, as they serve or have in the past served in the capacity of audit committee member, finance director or auditor.

#### The Audit and Risk Committee's missions

The Audit and Risk Committee's main duties were reviewed, for the last time, in November 2011 and are defined in the Board's internal rules.

The Committee is responsible to assist the Board by overseeing audit and risk matters:

- key responsibilities in relation to audit:
  - examining the integrity of the financial statements submitted to the Board of Directors in order to ensure that the data and information provided give a true and fair view of the company's operations and position,
  - reviewing financial and accounting policies and practices,
  - reviewing and discussing with management the effectiveness of internal control systems relating to financial reporting,

- monitoring and reviewing the effectiveness of the internal audit function, considering the major findings of internal investigations and management's response, and ensuring that the internal audit function is adequately resourced and has appropriate positioning,
- discussing with the Statutory Auditors the financial statements, the scope of audits, restatements made, compliance with accounting principles, market rules, legal and regulatory requirements, and the impact of any changes in accounting principles and practices,
- making recommendations to the Board of Directors regarding the appointment, renewal or removal of the Statutory Auditors, their fees and any other issues concerning their duties,
- assessing the independence and objectivity of the Statutory Auditors, including supervision of the turnover of the signing partners and the effectiveness of the audit process,
- applying the code of conduct and the HSBC Group policy concerning the provision of non-audit services by the Statutory Auditors,
- reviewing the Statutory Auditors' management letter together with management's response to it, and to monitor the implementation of recommendations made in the letter,
- ensuring compliance of the company and its subsidiaries with directives issued by the supervisory authorities and with regulations applicable to them;
- key responsibilities in relation to risk:
  - overseeing and advising the Board on all high-level risk related matters,
  - advising the Board on risk appetite and tolerance in determining strategy,
  - advising the Board and/or the Nomination and Remuneration Committee on alignment of remuneration with risk appetite,
  - examining regular reports on risk management related to the group's activity, the way in which risks are controlled and monitored by management, and on emerging risks,
  - examining the effectiveness of the group's risk management framework internal control systems,
  - approving the appointment and removal of the Chief Risk Officer and ensuring his effective role,
  - reviewing any issue which arises from any report from internal audit, the Statutory Auditors' annual report and any queries raised by the Statutory Auditors, and responses from management, which relates to the management of risk or internal control,
  - examining management's reports and statements on the internal control system.

The Committee meets the Statutory Auditors and the Head of Internal Audit in private at least once per year to ensure that there are no unresolved issues or concerns. In carrying out these duties and responsibilities, the Committee may consult any adviser or expert as it deems appropriate.

To give itself sufficient time to review the accounts before they are reviewed by the Board, the Audit and Risk Committee generally meets four days before the Board.

As required under the HSBC Group rules, the Audit and Risk Committee provides a half-yearly certificate to the Audit Committee and Risk Committee of HSBC Bank plc, HSBC France's direct shareholder, confirming, in particular, that the accounts were reviewed by the Committee and that the internal control system seems to be appropriate.

#### **The Audit and Risk Committee's work in 2012**

The Audit and Risk Committee met four times in 2012, with an attendance rate of 100 per cent, as in 2011:

- 16 February 2012 (attendance rate: 100 per cent);
- 11 May 2012 (attendance rate: 100 per cent);
- 19 July 2012 (attendance rate: 100 per cent);
- 16 November 2012 (attendance rate: 100 per cent).

Each meeting was also attended by the Statutory Auditors, the Deputy CEO in charge of risk, the Chief Financial Officer, the Chief Accounting Officer and the Head of Audit. The Deputy Chairman and the Chief Executive Officer attended Committee meetings to answer any questions. HSBC France executives also attend Committee meetings covering any subjects falling under their responsibility. Audit and Risk Committee members also met with the Statutory Auditors in private sessions prior to the Board meetings held to review the half-yearly and year-end accounts (meetings of 16 February and 19 July 2012).

Against a backdrop of crisis affecting the eurozone and in compliance with regulations, the Committee dedicated again in 2012 a substantial part of its work to the review of major risks. It monitors the organisation of the risk control system on a regular basis. In this context, the new organisation of Risk functions was presented to the Committee (meeting on 16 November 2012).

In each of its meetings, the Audit and Risk Committee continued to review major risks with each of the persons in charge of controlling these risks, in particular:

- credit risk, with an individual review of major exposures, changes in credit outstandings by business, changes in and optimisation of risk-weighted assets and evolution in cost of risk and the worry list;
- market risk, including market risk trends compared with limits, the fixing of limits, changes in risk-weighted assets of market activities, control instruments and procedures in place. At each meeting, it specifically reviewed the bank's exposure to the eurozone government bonds and the results of the stress tests conducted on market risk. At its meeting on 16 February 2012, a comprehensive presentation was given on Vanilla rates activity. At each meeting, the Committee was informed of discussions regarding market risk with regulators. In particular, it reviewed the findings of the audit conducted by the Financial Services Authority on Market activities, and especially on Rate activities, and the comments made by the HSBC Group and HSBC France on these findings;

- legal and litigation risks;
- operational risks;
- security and fraud risk, including information security and business continuity.

The Committee was informed, at each of its meetings, of the progress of the work undertaken by the Operational Risk and Internal Control Department and of operational losses that occurred during the quarter. It reviewed the risk mapping updated by all the business lines (meeting on 16 February 2012), and, at each meeting, the most significant risks along with the action plans implemented. It examined, at each of its meetings, the dashboard concerning the bank's risk appetite, particularly the indicators failing to comply with the established objectives, and the results of recurrent or specific stress-testing exercises conducted.

In 2012, the Audit and Risk Committee continued to watch closely the progress of the implementation of internal models according to Basel II regulation.

In accordance with regulation 97-02 and professional standards, at its meeting on 16 February 2012, the Committee reviewed the links between risk and remuneration in the remuneration policy, and in particular, the involvement of Risk functions in remuneration policy and taking account of risks in determining remunerations.

At its meeting on 11 May 2012, it reviewed the Annual Report to the *Autorité de contrôle prudentiel* on internal control, in accordance with regulation 97-02.

The second aspect of the Committee's work involved an in-depth review of the annual, half-yearly and quarterly financial statements prior to their presentation to the Board. The Audit and Risk Committee reviewed the parent-company and consolidated accounts and analysed the impact of changes in the accounting scope of consolidation on the results. The 2011 consolidated financial statements were presented according to IFRS, with a distinction drawn between the legal and French managerial scope of consolidation<sup>1</sup>. Parent company financial statements for 2011 were presented according to French GAAP. The Committee discussed the choices made by the company and presented by the Finance Department in drawing up its financial statements. The Statutory Auditors commented on their management letter and the aspects subject to particular attention at the time of preparing the 2011 financial statements (meeting on 16 February 2012). They presented their limited review on the financial statements at 31 March 2012, 30 June 2012 and 30 September 2012 (meetings on 11 May, 19 July and 16 November 2012). The Committee discussed the Statutory Auditors' programme and independence, approved the fees paid in 2011 by the HSBC France group to the Statutory Auditors and reviewed their renewal (meeting on 16 February 2012). The Committee also examined, at each of its meetings, the bank's regulatory and liquidity ratios and its liquidity and funding situation. It also closely monitored, at each meeting, the project implementation of a new accounting information system for the bank. Finally, at its meeting on 16 November 2012, the Committee was informed of the liquidity contingency plan and updated on HSBC France's rating by rating agencies.

<sup>1</sup> See footnote 3 page 3.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

The last aspect of the Committee's work was internal audit, internal control, compliance and relations with the regulatory authorities. The Audit and Risk Committee looked at the results of controls conducted on financial statements. Within this framework, it reviewed the work carried out as part of the application of Sarbanes Oxley: the list of procedures concerned and its development, identified weaknesses, their impact and monitoring. It reviewed the points raised in the quarterly suspense account reconciliation certificates prepared at the request of the HSBC Group and in the Statutory Auditors' management letters follow-up. The Committee also verified the adequacy of provisions for identified risks.

It also regularly examined internal audit work and reviewed the main audit assignments, particularly those deemed insufficient. It paid particular attention to audit recommendations follow-up, progress in implementing them and the monitoring of the recommendations not yet implemented. The new system to monitor audit recommendations, which aims to improve their implementation, was presented to the Committee (meetings on 19 July and 16 November 2012). It approved the 2012 annual audit plan (meeting on 16 February 2012) and then reviewed the progress of this plan at each subsequent meeting. Finally, the Committee was systematically informed of salient points discussed by the audit committees of HSBC France subsidiaries.

The Committee reviewed quarterly compliance reports, which state the main new Compliance issues and those already discussed at previous meetings, and reports issued to regulators: the Annual Report on the organisation and operation of the investment services control system for the *Autorité des marchés financiers*, the report on the protection of customer assets sent to the *Autorité des marchés financiers*, the annex to the internal control report on the general procedure for the control of customer protection rules (meeting on 19 July 2012), the Ombudsman's report and the annual report on cheque controls (regulation 2002-01) (meeting on 16 February 2012). It examined the compliance action plan for 2012. A specific presentation on anti-money laundering and "know your customer" procedures was given at the meeting held on 16 November 2012.

The Committee was informed of the findings of various audits carried out by the regulators: *Autorité des marchés financiers*, *Autorité de contrôle prudentiel* and Financial Services Authority, and of the action plans initiated to implement their recommendations. It reviewed the Chairman's report on internal control and risk management procedures (meeting on 16 February 2012) and the annual report to the *Autorité de contrôle prudentiel* on the functioning of the internal control systems (permanent control and periodic control), as required under regulation 97-02 (meeting on 11 May 2012). Finally, the Committee was regularly informed of the various regulatory reforms adopted or under discussion, particularly regarding capital requirement and liquidity risk management (Capital Requirements Directive 4 (CRD4) and Basel III), derivatives, ring-fencing of Retail Banking, tax reforms and initial estimations of their impact on HSBC France.

The Chairman of the Audit and Risk Committee reported on the key points of the Committee's work at the Board meetings held on 22 February, 15 May, 25 July and 22 November 2012.

### Compensation

#### Compensation and advantages of Executive Directors

##### Remuneration policy

The remuneration of Executive Directors is adopted each year by the Board of Directors upon the recommendation by the Nomination and Remuneration Committee, after approval by the Remuneration Committee of HSBC Holdings plc. It includes a fixed component and a variable component.

The fixed component is determined in accordance with, on one hand, market practices with the help of specialist consulting firms and the other hand, Group references.

The variable component is determined on the basis of a number of objective performance indicators covering financial aspects (profit before tax, cost efficiency ratio, return on equity and on risk-weighted assets, etc.) and non-financial aspects (observance of compliance, reputational risk, customer relationship quality, brand reputation, recommendations and market share, talent retention, implementation of strategic decisions, etc.). These indicators are analysed in comparison with the previous year or relative to the budget for the year. To these criteria, is added, henceforth, an appreciation of individual behaviour with regard to the Group's values which are dependability, openness, listening, courage and integrity.

The variable component also takes account of market practices and, if necessary, changes in regulations. In accordance with the HSBC Group's deferral rules, this variable component is paid partly in non-deferred and partly in deferred remuneration and partly in cash and partly in shares.

##### Award of shares

In 2012, Executive Directors benefited from the allocation of bonus shares in HSBC Holdings plc in accordance with the HSBC Group's general policy.

The HSBC Group awards various categories of bonus shares:

- Group Performance Shares, which are subject to performance criteria and are awarded to Executives of the HSBC Group;
- Restricted Shares, which are not subject to specific performance criteria but which are definitively awarded to employees still with the HSBC Group at the end of a two or three-year period, which is the period in force for France.

With respect to 2012, no HSBC France Executive Director, except Stuart Gulliver then Samir Assaf who do not receive any remuneration from HSBC France, has received any Group Performance Shares. They did receive Restricted Shares, for which the only criterion is to be with the company after a period of two or three years.

### **Supplementary pension scheme**

The Executive Directors of HSBC France have a defined benefits supplementary pension scheme. This plan guarantees members a pre-determined absolute supplementary pension income based on their length of service. In the event that the beneficiary dies, 60 per cent of this pension is payable to the surviving spouse. It is increased every year in line with the average rate applied to French State pension scheme.

At 31 December 2012, Jean Beunardeau had accrued pension rights representing 6 per cent of his fixed 2012 salary and 2 per cent of his total 2012 cash remuneration. At 31 December 2012, Gilles Denoyel had accrued pension rights at HSBC France representing 26 per cent of his fixed 2012 salary and 14 per cent of his total 2012 cash remuneration.

The provision corresponding to the present value of these HSBC France pension commitments has been recorded in the HSBC France accounts at 31 December 2012, for an amount of EUR 4.7 million.

It should be noted that in the context of his resignation as Chief Executive Officer, endorsed by the Board of Directors on 10 January 2012, Christophe de Backer has lost all his rights under this pension plan.

### **Remuneration**

The Chairman of the Board of HSBC France, Stuart Gulliver until 22 November 2012 then Samir Assaf from this date, does not receive any compensation or fees from HSBC France and is not a beneficiary of the HSBC France supplementary pension scheme. He has an employment contract with another company of the HSBC Group and has access to a pension fund of the HSBC Group.

The remuneration of Christophe de Backer, CEO of HSBC France until 10 January 2012, Jean Beunardeau, Deputy CEO then CEO of HSBC France from 10 January 2012, and Gilles Denoyel, Deputy CEO of HSBC France, is detailed on pages 28 to 34.

Regarding employment contracts, the Corporate Governance Code published by the AFEP and the MEDEF considers that the withdrawal of the Executive Directors' employment contract does not apply to unlisted subsidiaries. Therefore, it is considered that this recommendation does not apply to HSBC France, which is an unlisted subsidiary of HSBC Holdings plc.

Lastly, the Executive Directors are also provided with a company car, with the exception of Jean Beunardeau who uses a car made available to him by the company for his professional needs.

The following information is published in accordance with the provisions of article L. 225-102-1, paragraphs 1, 2 and 3 and article L. 225-184 of the French Commercial Code. It concerns remuneration paid by HSBC France, the companies it controls and the companies that control it (the HSBC Group). The remuneration of Executive Directors below is presented in accordance with the AFEP and the MEDEF Corporate Governance Code as applied by HSBC France, as well as the *Autorité des marchés financiers* recommendations of December 2008<sup>1</sup>.

<sup>1</sup> Table numbers refer to table models provided by the Autorité des marchés financiers in its 22 December 2008 recommendation concerning information to be provided in registration documents concerning Directors' compensation.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### Summary of compensation and options and shares awarded to each Executive Director (Table 1)

| <i>(in euros)</i>  | 2011                 |                                | 2012                 |                                |
|--|----------------------|--------------------------------|----------------------|--------------------------------|
|  | Amounts paid in 2011 | Amounts due in respect of 2011 | Amounts paid in 2012 | Amounts due in respect of 2012 |
| <b>Christophe de Backer</b>  |                      |                                |                      |                                |
| <i>Chief Executive Officer</i> <sup>1</sup>                          |                      |                                |                      |                                |
| Compensation (detailed in table 2) .....                             | 1,293,592            | 605,736                        | <b>50,421</b>        | <b>50,421</b>                  |
| Value of the options awarded (detailed in table 4) .....             | –                    | –                              | –                    | –                              |
| Value of the shares awarded (detailed in table 6) <sup>2</sup> ..... | 1,087,783            | –                              | –                    | –                              |
| <b>Total</b> .....   | <b>2,381,375</b>     | <b>605,736</b>                 | <b>50,421</b>        | <b>50,421</b>                  |
| <b>Jean Beunardeau</b>   |                      |                                |                      |                                |
| <i>Chief Executive Officer</i> <sup>3</sup>                          |                      |                                |                      |                                |
| Compensation (detailed in table 2) .....                             | 694,595              | 1,162,439                      | <b>1,038,086</b>     | <b>1,357,263</b>               |
| Value of the options awarded (detailed in table 4) .....             | –                    | –                              | –                    | –                              |
| Value of the shares awarded (detailed in table 6) <sup>2</sup> ..... | 1,030,653            | 812,439                        | <b>812,439</b>       | <b>857,263</b>                 |
| <b>Total</b> .....   | <b>1,725,248</b>     | <b>1,974,878</b>               | <b>1,850,525</b>     | <b>2,214,526</b>               |
| <b>Gilles Denoyel</b>  |                      |                                |                      |                                |
| <i>Deputy CEO</i>  |                      |                                |                      |                                |
| Compensation (detailed in table 2) .....                             | 754,190              | 691,390                        | <b>741,847</b>       | <b>777,822</b>                 |
| Value of the options awarded (detailed in table 4) .....             | –                    | –                              | –                    | –                              |
| Value of the shares awarded (detailed in table 6) <sup>2</sup> ..... | 350,000              | 430,800                        | <b>430,800</b>       | <b>323,175</b>                 |
| <b>Total</b> .....   | <b>1,104,190</b>     | <b>1,122,190</b>               | <b>1,172,647</b>     | <b>1,100,997</b>               |

<sup>1</sup> Chief Executive Officer until 10 January 2012.

<sup>2</sup> With the exception of those awarded to C de Backer in 2011, as the HSBC France Executive Directors are not awarded Group Performance Shares (see page 26), this line shows the shares without performance conditions.

<sup>3</sup> Deputy CEO then Chief Executive Officer from 10 January 2012.

## Detailed breakdown of compensation paid to each Executive Director (Table 2)

| (in euros)                                   | 2011                 |                                | 2012                     |                                |
|--|----------------------|--------------------------------|--------------------------|--------------------------------|
|  | Amounts paid in 2011 | Amounts due in respect of 2011 | Amounts paid in 2012     | Amounts due in respect of 2012 |
| <b>Christophe de Backer</b>                  |                      |                                |                          |                                |
| <i>Chief Executive Officer</i> <sup>1</sup>  |                      |                                |                          |                                |
| Fixed remuneration .....                     | 600,000              | 600,000                        | <b>50,000</b>            | <b>50,000</b>                  |
| Variable remuneration in cash .....          | 687,856              | –                              | –                        | –                              |
| Director's fees .....                        | – <sup>2</sup>       | – <sup>2</sup>                 | – <sup>2</sup>           | – <sup>2</sup>                 |
| Benefits in kind.....                        | 5,736 <sup>3</sup>   | 5,736 <sup>3</sup>             | <b>421<sup>3</sup></b>   | <b>421<sup>3</sup></b>         |
| <b>Total</b> .....                           | <b>1,293,592</b>     | <b>605,736</b>                 | <b>50,421</b>            | <b>50,421</b>                  |
| <b>Jean Beunardeau</b>                       |                      |                                |                          |                                |
| <i>Chief Executive Officer</i> <sup>4</sup>  |                      |                                |                          |                                |
| Fixed remuneration .....                     | 350,000              | 350,000                        | <b>500,000</b>           | <b>500,000</b>                 |
| Variable remuneration in cash .....          | 344,295              | 324,976                        | <b>324,976</b>           | <b>342,905</b>                 |
| Deferred variable remuneration in cash ..... | –                    | 487,463                        | <b>213,110</b>           | <b>514,358</b>                 |
| Director's fees .....                        | – <sup>2</sup>       | – <sup>2</sup>                 | – <sup>2</sup>           | – <sup>2</sup>                 |
| Benefits in kind.....                        | –                    | –                              | –                        | –                              |
| <b>Total</b> .....                           | <b>694,595</b>       | <b>1,162,439</b>               | <b>1,038,086</b>         | <b>1,357,263</b>               |
| <b>Gilles Denoyel</b>                        |                      |                                |                          |                                |
| <i>Deputy CEO</i>                            |                      |                                |                          |                                |
| Fixed remuneration .....                     | 400,000              | 400,000                        | <b>450,000</b>           | <b>450,000</b>                 |
| Variable remuneration in cash .....          | 350,000              | 287,200                        | <b>287,200</b>           | <b>323,175</b>                 |
| Director's fees .....                        | – <sup>2</sup>       | – <sup>2</sup>                 | – <sup>2</sup>           | – <sup>2</sup>                 |
| Benefits in kind.....                        | 4,190 <sup>3</sup>   | 4,190 <sup>3</sup>             | <b>4,647<sup>3</sup></b> | <b>4,647<sup>3</sup></b>       |
| <b>Total</b> .....                           | <b>754,190</b>       | <b>691,390</b>                 | <b>741,847</b>           | <b>777,822</b>                 |

1 Chief Executive Officer until 10 January 2012.

2 Renounced the payment of his fees by HSBC France (see page 33).

3 Company car.

4 Deputy CEO then Chief Executive Officer from 10 January 2012.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### Share options awarded during the year to each Executive Director by HSBC France and any company of the HSBC Group (Table 4)

|                     | Number of the plan and date of award | Type of options | Value of the shares under the method used for the consolidated accounts | Number of options awarded during the year | Exercise price | Period of exercise |
|---------------------|--------------------------------------|-----------------|---|---|----------------|--------------------|
| None (see page 26). |                                      |                 |   |   |                |                    |

### Share options exercised during the year by each Executive Director (Table 5)

#### CCF options exercised in 2012

|       | Number of options exercised | Exercise price EUR/share | Date of award | Expiry date |
|-------|-----------------------------|--------------------------|---------------|-------------|
| None. |                             |                          |               |             |

#### HSBC Holdings plc options exercised in 2012

|       | Number of options exercised | Exercise price EUR/share | Date of award | Expiry date |
|-------|-----------------------------|--------------------------|---------------|-------------|
| None. |                             |                          |               |             |

### Shares awarded to each Executive Director in 2012 in respect of 2011 (Table 6)

#### HSBC Holdings plc shares without performance conditions

In respect of 2011, no HSBC France Executive Director, except Stuart Gulliver who does not receive any remuneration from HSBC France, has been awarded shares with performance conditions ("Group Performance Share").

|   | Date of award | Number of shares awarded | Value of the shares under the method used for the consolidated accounts | Vesting date                              | Date of availability                      |
|---|---------------|--------------------------|---|---|---|
| Jean Beunardeau .....                   | 12.03.2012    | 73,457                   | EUR487,463  | 12.03.2014 for 66% and 12.03.2015 for 34% | 12.03.2016 for 66% and 12.03.2017 for 34% |
| Jean Beunardeau .....                   | 12.03.2012    | 48,972                   | EUR324,976  | 12.03.2012 for 100%                       | 12.09.2012 for 100%                       |
| Gilles Denoyel.....                     | 12.03.2012    | 64,919                   | EUR430,800  | 12.03.2014 for 66% and 12.03.2015 for 34% | 12.03.2016 for 66% and 12.03.2017 for 34% |
| Christophe de Backer <sup>1</sup> ..... | 12.03.2012    | –                        | –   | N/A                                       | N/A                                       |

<sup>1</sup> Resignation on 10 January 2012.



## Shares awarded to each Executive Director in 2013 in respect of 2012 (Table 6)

### HSBC Holdings plc shares without performance conditions

In respect of 2012, no HSBC France Executive Director, except Stuart Gulliver, then Samir Assaf since 22 November 2012 but who do not receive any remuneration from HSBC France, has been awarded shares with performance conditions (“Group Performance Share”).

|                       | Date of award | Number of shares awarded | Value of the shares under the method used for the consolidated accounts | Vesting date                                 | Date of availability                         |
|-----------------------|---------------|--------------------------|---|--|--|
| Jean Beunardeau ..... | 11.03.2013    | 60,671                   | EUR514,358  | 11.03.2015 for 66%<br>and 11.03.2016 for 34% | 11.03.2017 for 66%<br>and 11.03.2018 for 34% |
| Jean Beunardeau ..... | 11.03.2013    | 40,447                   | EUR342,905  | 11.03.2013 for 100%                          | 11.09.2013 for 100%                          |
| Gilles Denoyel.....   | 11.03.2013    | 38,120                   | EUR323,175  | 11.03.2015 for 66%<br>and 11.03.2016 for 34% | 11.03.2017 for 66%<br>and 11.03.2018 for 34% |

## Performance shares which became available for each Executive Director (Table 7)

|       | Date of award | Number of shares which became available during the year | Vesting conditions |
|-------|---------------|---|--------------------|
| None. |               |   |                    |

### HSBC Holdings plc shares, without performance conditions, which vested for each Executive Director (Table 7)

The shares awarded in 2010 were vested for 50 per cent in 2012.

|                       | Date of award | Number of shares vested <sup>1</sup> | Vesting conditions (in case of special conditions) |
|-----------------------|---------------|--------------------------------------|--|
| Jean Beunardeau ..... | 01.03.2010    | 94,661                               |  |
| Jean Beunardeau ..... | 12.03.2010    | 48,971                               |  |
| Gilles Denoyel.....   | 01.03.2010    | 19,715                               |  |
| Gilles Denoyel.....   | 28.05.2010    | 1,327                                |  |

<sup>1</sup> The shares awarded under the French sub-plan are available two years after the vesting. The shares awarded under the British plan are available at the vesting.

## 10 highest awards of options to employees who are not Executive Directors and 10 highest exercises of options (Table 9)

|   | Number of options awarded/ exercised | Average exercise price | Date of award | Expiry date |
|---|--------------------------------------|------------------------|---------------|-------------|
| CCF options awarded during the year, by the issuer and by any company of its group to its ten employees whose number of awarded options is the highest .....  | None                                 |                        |               |             |
| HSBC options awarded during the year, by the issuer and by any company of its group to its ten employees whose number of awarded options is the highest ..... | None                                 |                        |               |             |
| CCF options exercised during the year by the ten employees and former employees whose number of exercised shares is the highest.....                          | None                                 |                        |               |             |
| HSBC options exercised during the year by the ten employees and former employees whose number of exercised shares is the highest.....                         | 309,260                              | GBP6.45                | 02.05.2003    | 02.05.2013  |

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### HSBC Holdings plc free shares, without performance conditions, awarded in 2012 in respect of 2011, to the ten employees whose number of awarded shares is the highest

|  | Date of award | Number of shares awarded | Value of the shares under the method used for the consolidated accounts | Vesting date                                 | Date of availability                         |
|--|---------------|--------------------------|---|--|--|
| Total value of the 10 highest awards of shares (employees or former employees) ..... | 12.03.2012    | 439,638                  | EUR2,917,437  | 12.03.2014 for 66%<br>and 12.03.2015 for 34% | 12.03.2016 for 66%<br>and 12.03.2017 for 34% |

### HSBC Holdings plc free shares, without performance conditions, awarded in 2013 in respect of 2012, to the ten employees whose number of awarded shares is the highest

|  | Date of award | Number of shares awarded | Value of the shares under the method used for the consolidated accounts | Vesting date <sup>1</sup>   | Date of availability <sup>1</sup>   |
|--|---------------|--------------------------|---|---|---|
| Total value of the 10 highest awards of shares (employees or former employees) ..... | 11.03.2013    | 505,212                  | EUR4,283,081  | 11.03.2015 for 66%<br>and 11.03.2016 for 34%<br>or<br>11.03.2013 for 100% | 11.03.2017 for 66%<br>and 11.03.2018 for 34%<br>or<br>11.09.2013 for 100% |

<sup>1</sup> Part of the free shares awarded to the target population, "code staff" and "reinforced-rule population", identified by the group, vests immediately and is available after six months of vesting.

### HSBC Holdings plc free shares, without performance conditions, vested in 2012 for the ten employees whose number of awarded shares is the highest

|  | Dates of awards                                    | Number of shares vested <sup>1</sup> | Vesting dates   |
|--|--|--------------------------------------|---|
| Total value of the 10 highest awards of shares, vested in 2012 (employees or former employees) ..... | 01.03.2010<br>or<br>15.03.2011<br>or<br>12.03.2012 | 1,544,599                            | 2012 for 50%<br>and 2013 for 50%<br>or<br>2012 for 33%<br>2013 for 33%<br>and 2014 for 34%<br>or<br>2012 for 100% |

<sup>1</sup> Including the shares awarded under the British plan, for which, the dates and vesting rules are different or the non-deferred shares. The free shares are available, either two years after the vesting, or at the vesting date in the case of the British plan, or after six months of vesting in the case of immediate shares.

## Other information required by the Corporate Governance Code (Table 10)

| Executive Director<br>Function<br>First appointed<br>Term ends   | Employment<br>contract <sup>1</sup> | HSBC France<br>supplemen-<br>tary pension<br>scheme <sup>2</sup> | Compensation<br>or benefits<br>due or that<br>may be due<br>upon<br>termination<br>or change<br>in duties | Compensation<br>due under<br>terms of non-<br>competete<br>agreement |
|--|-------------------------------------|--|---|--|
| <b>Christophe de Backer</b><br>Chief Executive Officer<br>1 February 2010<br>10 January 2012           | Suspended                           | Rights lost  | No  | No   |
| <b>Jean Beunardeau</b><br>Chief Executive Officer <sup>3</sup><br>1 February 2010 <sup>4</sup><br>2014 | Suspended                           | Yes  | No  | No   |
| <b>Gilles Denoyel</b><br>Deputy CEO <sup>5</sup><br>1 March 2004<br>2014                               | Suspended                           | Yes  | No  | No   |

<sup>1</sup> See page 27.

<sup>2</sup> See page 27.

<sup>3</sup> Deputy CEO then CEO since 10 January 2012.

<sup>4</sup> Date of appointment as Deputy CEO.

<sup>5</sup> Deputy CEO since 1 February 2010.

### Directors' Fees

The maximum amount of Directors' fees payable each year was fixed at EUR 600,000, as decided by the Annual General Meeting of 21 December 2007.

Following a review of the level of Directors' fees paid, which had not been reviewed since 2005, and of sector practices, and in view of the increased amount of work required from Directors and members of the Board Committees, the Nomination and Remuneration Committee proposed to the Board of Directors to increase Directors' fees in 2011.

Hence, in its meeting on 15 February 2011, the Board of Directors decided to increase individual fees, in respect of the financial year 2011, as follows:

- each Director receives an annual flat fee of EUR 27,000 at the conclusion of the Annual General Meeting;
- the additional annual flat fee paid to Board Committees members amounts to:
  - EUR 12,000 for the members of the Nomination and Remuneration Committee,
  - EUR 14,000 for the Chairman of the Nomination and Remuneration Committee,
  - EUR 18,000 for the members of the Audit and Risk Committee,
  - EUR 30,000 for the Chairman of the Audit and Risk Committee.

Furthermore, within the HSBC Group, it is customary for Directors representing HSBC and Executive Directors to renounce Directors' fees from HSBC Group companies. This recommendation has been implemented by the Executive Directors of HSBC France and its subsidiaries.

In 2012, in respect of 2011, Christophe de Backer, Jean Beunardeau, Peter Boyles, Gilles Denoyel and Philippe Pontet renounced the payment of their fees. It has to be noted that, according to this rule, the Chairman of the Board of HSBC France (Stuart Gulliver until 22 November 2012 then Samir Assaf from that date) does not receive any fees from HSBC France for his office.

Moreover, in order to comply with the rules applied by the HSBC Group, the Directors' attendance record is not taken into account in calculating Directors' fees.

The net total Directors' fees to be paid in May 2013 in respect of 2012 amount to EUR 0.37 million, as in 2012 in respect of 2011.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### Directors' fees and other compensation paid to Non-Executive Directors by HSBC France, the companies it controls and the companies which control it (the HSBC Group) (Table 3)

|  | Directors' fees paid in 2011 in respect of 2010 | Directors' fees paid in 2012 in respect of 2011 | Other compensation paid in 2011 <sup>1</sup> | Other compensation paid in 2012 <sup>1</sup> |
|--|---|---|--|--|
| <b>Executive Directors of the HSBC Group companies</b> |   |   |  |  |
| Peter Boyles <sup>2,3</sup> .....                      | –   | –   | EUR725,104 <sup>2</sup>                      | EUR851,237                                   |
| Philippe Pontet.....                                   | –   | –   | EUR1,016,514                                 | EUR861,740                                   |
| Antonio Simoes <sup>2,4</sup> .....                    | –   | –   | –  | GBP856,462                                   |
| <b>Directors elected by the employees</b>              |   |   |  |  |
| Evelyne Cesari <sup>5</sup> .....                      | EUR22,000                                       | EUR27,000                                       |  |  |
| Véronique Duquesne <sup>6</sup> .....                  | –   | –   |  |  |
| Michel Gauduffe <sup>6</sup> .....                     | EUR22,000                                       | EUR27,000                                       |  |  |
| Thierry Jacquaint <sup>5,6</sup> .....                 | EUR22,000                                       | EUR27,000                                       |  |  |
| Guillaume Praud.....                                   | –   | –   |  |  |
| Philippe Purdy <sup>6</sup> .....                      | EUR22,000                                       | EUR27,000                                       |  |  |
| <b>Independent Directors</b>                           |   |   |  |  |
| Martine Gerow <sup>7</sup> .....                       | –   | –   | –  | –  |
| Philippe Houzé.....                                    | EUR32,000                                       | EUR41,000                                       | –  | –  |
| Igor Landau <sup>8</sup> .....                         | EUR22,000                                       | EUR27,000                                       | –  | –  |
| Anne Méaux <sup>9</sup> .....                          | –   | EUR6,750  | –  | –  |
| Thierry Moulouguet.....                                | EUR44,500                                       | EUR57,000                                       | –  | –  |
| Marcel Roulet.....                                     | EUR28,250                                       | EUR27,000                                       | –  | –  |
| Peter Shawyer.....                                     | EUR107,200 <sup>8</sup>                         | EUR139,729 <sup>10</sup>                        | –  | –  |
| Brigitte Taittinger.....                               | EUR22,000                                       | EUR27,000                                       | –  | –  |
| Jacques Veyrat.....                                    | EUR29,500                                       | EUR39,000                                       | –  | –  |

1 Fixed and variable remuneration and benefits in kind.

2 Emoluments shown are paid by other HSBC Group companies in respect of his executive functions within the Group.

3 Resignation as Deputy Chairman and Director on 10 December 2012.

4 Co-optation on 22 February 2012.

5 Appointment ended on 26 September 2012.

6 Directors' fees paid to a trade union organisation.

7 Appointment on 1 November 2012.

8 Appointment ended on 15 May 2012.

9 Appointment on 31 October 2011.

10 Of which EUR 35,500 paid by HSBC France, excluding withholding tax.

#### Compensation policy for employees whose professional activities have a significant impact on the risk profile of the business

The following information is published in accordance with article 43-2 of regulation 97-02 and the professional standards laid down by the *Fédération Bancaire Française* (FBF), the French Banking Federation, following the publication of the ministerial decree of 13 December 2010, on governance and variable compensation for employees whose professional activities have a significant impact on the risk profile of the business.

#### Decision-making process implemented to define the company's compensation policy

As HSBC France is part of an international banking group, its compensation policy is defined at the level of the parent company. As part of a delegation by the HSBC Group's Board of Directors, the HSBC Group's Remuneration Committee is responsible for approving the compensation policy for the HSBC Group as a whole.

The compensation policy in place in France falls within the framework of this general policy, while also ensuring that local professional standards and regulations are observed.

Two committees – the People Committee and the Nomination and Remuneration Committee – play a predominant role in the overall process of implementing this policy.

The People Committee, made up of the main Senior Executives of HSBC France (the Chief Executive Officer also in charge of Global Banking and Markets, the Deputy Chief Executive Officer in charge of the Risk Functions, the Chief Operating Officer and the Head of Human Resources), reviews the main aspects of the compensation policy for France and approves it. It ensures that this policy fits in with the general principles of the compensation policy set by the HSBC Group for all of its subsidiaries, and in the light of the specific directives set by the global business lines. Lastly, it gives an opinion on the policy's compliance with local professional standards and the recommendations of banking supervisory bodies in France such as the *Autorité de contrôle prudentiel*, the *Autorité des marchés financiers* and the *Fédération bancaire française*.

In addition, as regards variable compensation, it checks that all of the measures in place within the bank's various business lines adhere to the general principles defined in compensation policies by the HSBC Group, global business lines and in France, and meet the requirements of supervisory committees. It reviews the variable compensation budgets allocated to French staff by the global business lines on the basis of the performance of each business line and by taking account of risk and compliance. It approves the structure of these compensation budgets, *i.e.* the breakdown between cash and shares, in accordance with the HSBC Group's deferral rules and local professional standards.

Lastly, on an individual basis, it reviews and validates the consistency of compensation paid to the company's main Senior Executives, as well as the 20 highest compensation packages in collaboration with the HSBC Group's decision-making bodies and global business lines. It ensures that proposed individual compensation packages take into account any individual failures to meet the bank's operational, credit, compliance and reputation risk criteria.

On the basis of the compensation policy summary prepared by the *ad hoc* People Committee, the Nomination and Remuneration Committee, chaired by an independent Director, gives its opinion on the bank's policies and practices concerning compensation, ensuring their consistency with the HSBC Group policy and their compliance with applicable local standards, as well as that risk management and compliance issues are taken into account.

Its scope of intervention covers all compensation policies and practices in place within the company, although with a more in-depth review concerning professionals whose activities have a significant impact on the risk profile of the business and Executive Directors.

### **Main characteristics of the compensation policy**

The compensation policy takes into account, on one hand, the overall performance of the company and, on the other hand, the individual performance of employees.

The overall performance of the company is analysed by business lines and activities and measured by financial metrics, such as a comparison of revenue and cost trends, the cost efficiency ratio, the pre-tax profit and the return on equity. The risk dimension is incorporated by using risk indicators such as changes in risk provisions, the level of risk-weighted assets and the corresponding return, the liquidity ratio, and the amount of operational losses. The overall assessment of these indicators, analysed by comparison to the previous year and against the current year budget, allows the determination of variable compensation budgets with respect to the year in question.

These budgets are then individually granted according to the individual performance of each employee. A differentiating approach benefits the highest performing employees. The individual performance of an employee is appraised by the manager twice yearly (mid-year and at the year-end) and a performance rating of between 1 and 5 is awarded:

- rating 1: outstanding performance;
- rating 2: excellent performance;
- rating 3: targets achieved - good performance;
- rating 4: performance below expectation - unsatisfactory performance;
- rating 5: performance well below expectation - very unsatisfactory performance.

The performance appraisal is based on achieving targets set for the employee by the manager at the start of the year. These targets include collective and/or individual financial criteria (income growth, cost control, pre-tax profit, cost efficiency ratio, return on equity, etc.) and more qualitative non-financial criteria (observance of compliance and internal control rules, quality of service, amount operational losses, follow-up of audit points, compulsory training attendance rate, customer recommendations, cross-businesses synergies, winning customers, etc.). The indicators, which underpin these objectives, are a function of the position held and the level of responsibility, and are appraised by comparison to the previous year and against the current year budget.

All targets are formally documented at the beginning of the year, in annual employee target sheets (performance scorecards).

It is to be noted that Senior Executives (Group Classification 0 and 1) are also evaluated on their adherence to the Group's values (dependable, open, connected).

In compliance with the rules laid down by the regulators, the variable compensation of employees whose professional activities have a significant impact on the entity's risk profile is subject to specific rules on deferment of compensation, and on structuring variable compensation between cash and shares.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

As permitted under French regulations, HSBC France has opted to implement the HSBC Group's policy in these areas. This has resulted in the identification, at a global level, of a target population which is subject to all the rules set out in the Financial Services Authority's Remuneration Code, which closely resemble French rules.

This target population at the level of the HSBC Group ("code staff") includes the HSBC Group top management as well as any HSBC Group employee whose function may have a significant impact on the bank's risk profile, *i.e.* "Group Executive Directors", "Group Managing Directors", "Group General Managers", "Significant Influence Functions (SIFs)" and "risk holders" (mainly members of Group and Regional executive committees of the Global Banking and Markets activities). For the year 2012, it represents 314 employees.

In France, a list of three employees has been identified by the HSBC Group as belonging to this target population.

For this population, deferred variable remuneration accounts for at least 40 per cent of their variable remuneration and 60 per cent of the highest variable remunerations. Moreover, for this population, variable remuneration granted in the form of shares accounts for 50 per cent of variable remuneration granted; this 50 per cent applies to both the deferred component and to its immediately paid fraction.

In addition, it was decided that 50 additional employees, who do not belong to the target population defined at the HSBC Group level but who nevertheless play a significant role within HSBC France, would be subject to a large part of the rules applicable to the target population, in accordance with the principle of proportionality provided for in the regulations.

This additional population ("reinforced-rule population"), which is identified locally, includes financial market professionals considered to be risks takers, the Heads of the Finance function and the Risk functions, the Executive Directors of HSBC France and the Heads of HSBC France's various business lines.

It should be noted that out of these 50 employees, 15 are employees of the French branch of HSBC Bank plc.

This second category of "reinforced-rule population" is submitted to rules noticeably more restrictive than the rest of the other employees who are subject to deferral rules (higher deferred proportion, from 40 to 60 per cent, in most cases).

For these two categories of employees (*i.e.* a total of 53 employees), 45 per cent of variable remuneration is deferred, and variable remuneration represents 63 per cent of total remuneration (fixed + variable). The deferred share-based portion is not vested by the employee until after a period of two years for 66 per cent and after three years for the remaining 34 per cent. This is furthermore subject to a two-year retention period starting from vesting, and there is a prohibition on hedging it.

It should be noted that beyond these two employee categories, the great majority of the company's senior managers are affected by the minimum deferred compensation rules laid down by the HSBC Group which, for 2012, provide for deferred compensation in the form of shares of between 10 per cent and 50 per cent of variable compensation, and to which the above rules on vesting and retention apply.

Lastly, since 2010, a clawback system applies to all employees receiving deferred bonuses. This allows the HSBC Group's Remuneration Committee to cancel, reduce or amend all or part of bonuses awarded on the basis of the employee's behaviour or factors justifying such action.

Guaranteed bonuses are highly exceptional, limited to one year and only in a hiring context.

Consolidated quantitative information about compensation paid to executive members and financial market professionals, whose activities have a material impact on the company's risk exposure

Amounts are expressed in EUR and correspond to gross salary (excluding employer social security contributions and before deduction of payroll costs).

### Compensation granted in respect of the financial year

The tables show the remuneration of professionals that have a significant impact on risk as at 31 December 2012.

#### *Distribution between the fixed and variable portion*

|  | Number of people concerned | Total 2012 compensation (in EUR) | Total fixed compensation (in EUR) | Total variable compensation (in EUR) |
|--|----------------------------|----------------------------------|-----------------------------------|--------------------------------------|
| Executive members .....                                  | 2                          | 3,310,876                        | 950,000                           | 2,360,876                            |
| Professionals having a significant impact on risks ..... | 51                         | 27,211,860                       | 10,389,111                        | 16,822,749                           |

#### *Distribution between vested, paid or delivered amount and conditional deferred amount*

| <i>(in euros)</i>  | Vested, paid or delivered amount | Conditional deferred amount |
|--|----------------------------------|-----------------------------|
| Executive members .....                                  | 1,008,985                        | 1,351,891                   |
| Professionals having a significant impact on risks ..... | 9,470,845                        | 7,351,904                   |

#### *Distribution between payment in cash and payment in shares or in equivalent instruments*

| <i>(in euros)</i>  | Payments in cash | Payments in shares or equivalent instruments |
|--|------------------|--|
| Executive members .....                                  | 1,180,438        | 1,180,438                                    |
| Professionals having a significant impact on risks ..... | 9,686,205        | 7,136,544                                    |

### Outstanding variable compensation

| <i>(in euros)</i>  | Amounts of unvested deferred compensation in respect of the financial year | Amounts of unvested deferred compensation in respect of previous financial years |
|--|--|--|
| Executive members .....                                  | 1,351,891  | 3,668,666  |
| Professionals having a significant impact on risks ..... | 7,351,904  | 25,289,701   |

This shows outstanding deferred compensation corresponding to total unvested deferred compensation, *i.e.* compensation that has been awarded but not yet paid (cash) or delivered (securities) and which is still subject to a future clawback mechanism or early departure.

This must include unvested deferred compensation awarded in respect of the previous financial year (column 1), as well as unvested deferred compensation relating to prior years (column 2).

The sums paid or securities delivered – even if they are still subject to a holding requirement – after application of the clawback mechanism, are not included in outstandings.

Securities and equivalent instruments are valued on the basis of value at the award.

Outstanding vested compensation in respect of prior years can be impacted by departures from the company.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### Outstanding deferred compensation paid or reduced after adjustments according to results

| <i>(in euros)</i>  | Amount of deferred compensation paid | Amount of reductions made from deferred compensation |
|--|--------------------------------------|--|
| Executive members .....                                  | 1,093,335                            | –  |
| Professionals having a significant impact on risks ..... | 9,615,888                            | –  |

The first column corresponds to sums paid or to securities delivered (even if they are still subject to a holding requirement) adjusted according to the results of the financial year for each prior year.

The second column corresponds to the amount of reductions on deferred compensation due to the results of the considered year, whatever the year of securities granted.

Securities and equivalent instruments are valued on the basis of value at the award.

### Amounts paid in respect of hirings and terminations during the year

|  | Amount of severance payment paid and number of beneficiaries |                         | Amount of sums paid for hirings and number of beneficiaries |                         |
|--|--|-------------------------|---|-------------------------|
|  | Sums paid (in EUR)   | Number of beneficiaries | Sums paid (in EUR)  | Number of beneficiaries |
| Executive members .....                                  | –  | –                       | –   | –                       |
| Professionals having a significant impact on risks ..... | 76,924   | 2                       | –   | –                       |

The first column corresponds to all sums paid on termination of the employment contract (severance payment), which include redundancy compensation and contractual indemnities.

### Termination compensation guarantees

|  | Severance pay guarantees granted during the year |                         |                            |
|--|--|-------------------------|----------------------------|
|  | Total (in EUR)                                   | Number of beneficiaries | Highest guarantee (in EUR) |
| Executive members .....                                  | –  | –                       | –                          |
| Professionals having a significant impact on risks ..... | –  | –                       | –                          |

This is aimed at “promised” severance pay granted during the reference financial year.

### Conflicts of interest

To the bank's knowledge, there is no conflict of interest between the duties of Board members, including Executive Directors, with respect to the issuer and their private interests and/or other duties.

For information, it has to be noted that Stuart Gulliver was Chairman of the Board of HSBC France until 22 November 2012 and, from 1 January 2011, Group Chief Executive of HSBC Holdings plc, which owns 100 per cent of HSBC Bank plc, itself owning 99.99 per cent of the issuer. On 22 November 2012, Samir Assaf was appointed

Chairman of the Board of HSBC France and, since 1 January 2011, he has been Chief Executive of Global Markets for the HSBC Group and a member of the HSBC Holdings plc Group Management Board.

Article IV-2 of the Board of Directors' internal rules states that any Director who has a conflict of interest must report it to the Board and must abstain from voting on any corresponding motion, and that the Chairman may invite the Director not to attend the discussion.



## Board of Directors' internal rules

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The Board of Directors' internal rules were first established in 1996, and have been updated several times since their implementation.

These rules specify the Board's main duties:

- to discuss all issues relating to its legal and regulatory obligations and those arising from the company's articles of association;
- to determine the general direction of the company's activities and ensure that it is followed.

In addition, the rules confer certain duties on independent Directors sitting on the Board of Directors of a 100 per cent-owned subsidiary as follows:

- to discuss the strategy adopted by HSBC France;
- to oversee its implementation;
- to approve strategic investment and divestment plans and all transactions liable to have a significant impact on earnings;
- to oversee and control material risks;
- to ensure the quality of information provided to the shareholder and to the market through the financial statements and the Annual Report;
- to protect the reputation of the HSBC Group in France.

The Board's internal rules define the procedures for conducting Board meetings and providing information to the Board. They indicate the main duties and arrangements for exercising the function of Chairman, and the main duties of the Chief Executive Officer. Furthermore, the Board's internal rules define, in accordance with the HSBC Group rules, the duties, powers and responsibilities of the Audit and Risk Committee and the Nomination and Remuneration Committee (as stipulated above in the parts related to these Committees' assignments). They also incorporate a code of conduct to be followed by the Directors of HSBC France, setting out their rights and duties. Lastly, they define intervention rules on the HSBC Group listed securities for HSBC France Directors.

## Self-assessment

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In accordance with AFEP/MEDEF recommendations concerning assessment of the Board of Directors, HSBC has implemented a self-assessment process in 2011. This assessment was conducted internally, under the responsibility of the Nomination and Remuneration Committee and on the basis of Directors' answers to a detailed questionnaire. The main themes raised concerned the running and composition of the Board and its Committees, their effectiveness, the information available to Directors to perform their duties, relations between the Board and the bank and ways of improvement from Directors' point of view.

After analysis, a summary of answers given was presented to the Board in July 2011 by the Chairman of the Nomination and Remuneration Committee. The assessment process showed that Directors had a positive opinion of how the Board is run, as a more than 99 per cent-owned subsidiary of the HSBC Group. In order to respond to the wishes expressed by Directors concerning training, a training day intended for independent Directors focusing on strategy and the various business lines was held on 1 July 2011. In addition, an induction day will be organised in 2013 for recently appointed Directors in priority and also proposed to Directors already in office.

The Board's assessment procedure will be carried out regularly and the next one should be conducted in 2013.

## General Meeting

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Meetings are open to all shareholders. They are convened and transact business in accordance with the provisions of the law and regulations in force. According to article 22 of the Articles of Association, all shareholders, whatever the number of shares they own, are entitled to attend General Meetings and to take part in the deliberations, personally or through a representative, provided their shares are paid up in full for payments that are due and are registered on an account in their own name no later than midnight, Paris time, on the third business day preceding the General Meeting. However, the author of the notice to attend has the option at all times to reduce this period of time, as he so sees fit.

All shareholders can also vote by correspondence using a form which can be sent to them in accordance with the conditions specified by the notice to attend the Meeting.

The Board of Directors can decide that shareholders will be allowed to take part and vote in all General Meetings by video conference or by any means of telecommunications making it possible to identify them in accordance with the legal and regulatory provisions.

## Restrictions on the CEO's powers

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The CEO has the widest powers to represent the company in all circumstances within the limits of its corporate objects and subject to those powers expressly conferred by law on the collective body of shareholders and the Board of Directors.

In this respect, the Board of Directors has delegated its powers to issue bonds to Jean Beunardeau (Chief Executive Officer), Gilles Denoyel (Deputy Chief Executive Officer) and several Global Markets Officers. At present, there are no specific restrictions on the Chief Executive Officer's powers, but in practice, decisions involving the orientation of company activities are submitted to the Board of Directors for approval.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

The Chief Executive Officer has delegated certain powers to the Deputy Chief Executive Officer and Senior Corporate Vice-Presidents, who may in turn delegate some of these powers to agents holding general powers of attorney reporting directly to them.

These powers concern:

- representation of the bank,
- banking operations,
- bank-related operations,
- litigation.

Delegated powers must be exercised within the bounds of the person's responsibilities and in accordance with the HSBC Group principles and practices. A person with delegated powers may not individually commit HSBC France to sums above EUR 1,500,000.

There are specific delegated powers concerning credit<sup>1</sup> and market<sup>2</sup> risk, for which the CEO delegates his powers.

## CHAIRMAN'S REPORT ON INTERNAL CONTROL AND RISK MANAGEMENT PROCEDURES

### The general framework of internal control and risk management

#### Context

HSBC France has implemented a comprehensive and sound system of internal control and procedures adapted to the organisation and its various activities in order to:

- ensure optimal execution of its operations;
  - control all types of risk to which HSBC France is exposed;
  - control the quality and reliability of financial reporting and regulatory reporting;
  - ensure compliance with current laws and regulations;
  - ensure compliance with the HSBC Group standards.
- Internal control at HSBC France relies on:
- clear articulation of responsibilities of various actors and control levels;
  - organisation charts and job descriptions with appropriate delegations of authority as well as functional and hierarchical lines clearly defined;
  - segregation of duties;
  - teams dedicated to internal control within business lines and central departments;
  - transverse risk functions run by central departments;
  - monitoring of the resources dedicated to permanent control in order to verify the adequacy in terms of skills and number;
  - risk and control maps covering the entire scope of HSBC in France;
  - a code of conduct binding on all staff;
  - comprehensive procedures covering all activities and more particularly specifying control responsibilities;
  - outsourcing management policy;
  - a sound process on new products or services;
  - the existence of rules, tools and an organisation to assess, supervise and control the major risks;
  - quality, security and integrity of information systems;
  - quality and integrity of accounting and management information, based on accounting controls and an audit trail;
  - business recovery plans and IT recovery plans;
  - a reporting and committee framework ensuring effective coordination between different levels of control as well as a summary of assessments for the executive and decision-making bodies;
  - the assessment of this permanent control framework by an independent third-level control (periodic control).

<sup>1</sup> See Risk management page 76.

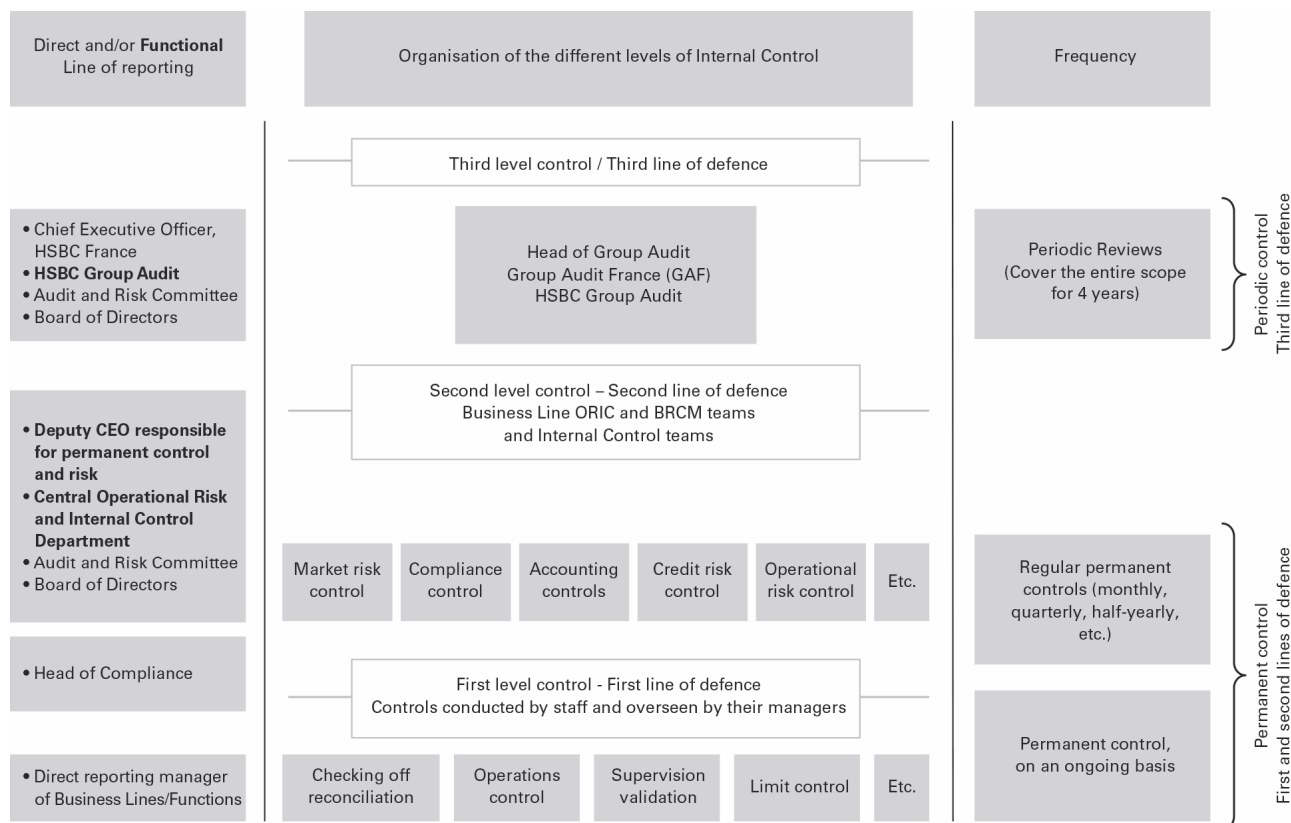
<sup>2</sup> See Risk management page 80.

The diagram below explains the three levels of control at HSBC France:

– the operational units;

– dedicated second level control teams;

– the periodic control teams, which assess the efficiency of permanent control



Permanent control relies both on business lines and functions with their own ORIC (Operational Risk and Internal Control) teams and on risk functions, the whole system being coordinated by the Central ORIC Department.

The Risk functions driven by central departments have a transverse view of their type of risk across all business lines of the HSBC Group in France and are 10 in number<sup>1</sup>:

– Financial risks:

- market function;
- credit function;
- structural interest rate, forex and liquidity risk function;

– Non-financial risks:

- compliance function;
- accounting function;
- legal affairs function;
- tax function;
- IT function;
- security and fraud function (including physical security, information security, business continuity and fraud);
- human resources function.

The HSBC Group has implemented an internal control and risk management framework in reference to COSO 2<sup>2</sup>. In France, the Deputy CEO in charge of risk and permanent control (in accordance with regulation 97-02) is also Chief Risk Officer (CRO).

<sup>1</sup> The management of each risk by its function is described in detail in the Risk management section pages 75 to 97.

<sup>2</sup> Committee of Sponsoring Organizations of the Treadway Commission (COSO).

## Chairman’s report on corporate governance and internal control and risk management procedures (continued)

### HSBC Group Manuals

The GSM (HSBC Group Standards Manual) sets out the standards that all HSBC Group companies must observe. It applies to all the HSBC Group’s business lines all over the world. No dispensation is granted without the specific agreement of the HSBC Group Chairman.

All the HSBC Group’s business activities must be fully documented in manuals or compendia of procedures. Functional Instruction Manuals (FIMs) contain detailed policies and procedures relating to a specific business line or function, product or activity, which must be adhered to throughout the HSBC Group, barring dispensation granted by the FIM’s owner for the HSBC Group. In addition, HSBC France and its subsidiaries are required to document their operating procedures and their specific practices (Business Instruction Manuals – BIMs – or equivalent, and internal circulars).

The adequacy and effectiveness of these manuals have to be reviewed at least once a year; managers are required to report annually on the implementation thereof, to confirm that their business activities are fully covered by them, that they are comprehensive, and that existing procedures have been reviewed over the past year. Based on these confirmations, the Chief Executive Officer of HSBC France provides an aggregate certificate to the HSBC Group.

### Handbook and Codes of Conduct

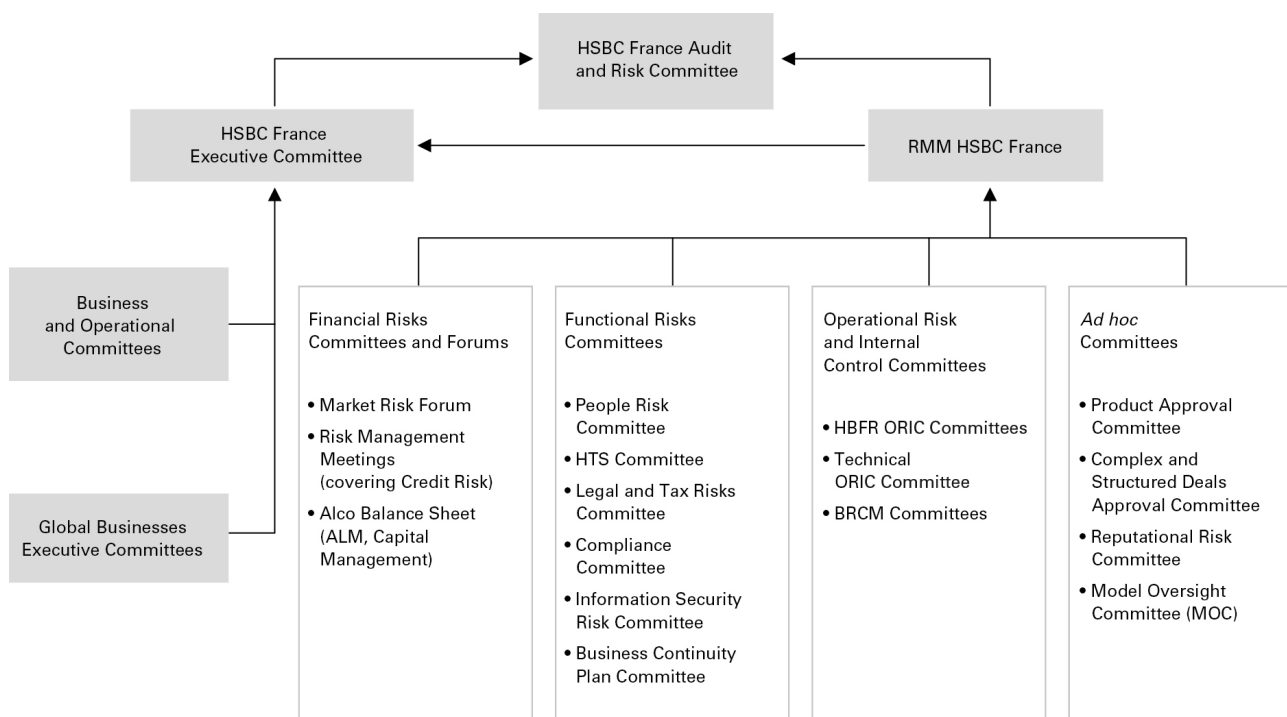
The Handbook features business ethics rules that apply to all staff, relating to confidentiality, compliance with laws and regulations and professional integrity. In addition to these rules, each of the bank’s business lines or activities may have a specific code of conduct and/or compliance manual that collates operational application procedures relating to staff business ethics and compliance with laws and regulations. Staff members working in functions regarded as sensitive are also subject to specific requirements relating to personal transactions.

### Internal circulars

Internal circulars are the key vehicle for communicating internal standards and rules derived from French regulatory requirements or HSBC Group standards that apply to several or all HSBC Group structures operating in France. They are readily available on the HSBC France Intranet, and are listed by nature, type and recipient. The drafting, circulation and storing of circulars are governed by precise rules (also formally set out in a circular) and are regularly updated.

### The internal committees

Risks are supervised by a number of dedicated committees, the general organisation of which is shown in the diagram below.



Senior Management is kept regularly informed of the organisation and findings of permanent and periodic controls, in particular through various dedicated committees.

Among these committees, the Risk Management Meeting (RMM), the Operational Risk and Internal Control (ORIC) Committees, and the Compliance Committee play a key part in coordinating the control framework, summarising controls and monitoring risks.

This framework is completed by special risk committees in each entity, business line and function, combining the three levels of internal control, in order to manage, monitor and control the risks specific to each HSBC activity in France and combining the three levels of Internal Control.

#### **The Risk Management Meeting (RMM)**

The RMM, which is chaired by the Chief Risk Officer and includes most of the Executive Committee and managers in charge of risk functions, is an overarching committee overseeing risk management and permanent control. It meets every month to analyse HSBC France's main risks, as established by a previously agreed agenda.

The RMM reports functionally to its European equivalent in the HSBC Group through the communication of minutes. Locally, all risk assessments presented to the RMM are also used by the HSBC France's Executive Committee and the Audit and Risk Committee. The RMM covers all entities operating in France.

The RMM makes use of the work of all dedicated committees and summarises their findings. In particular, these committees include:

- for credit risks:
  - the Risk Management Committees dedicated to each Global Business (Retail Banking and Wealth Management, Commercial Banking, Global Banking and Markets);
- for market, liquidity and global interest rate risks:
  - the Market Risk Forum,
  - the ALM Committee (“Balance Sheet ALCO”);
  - the Capital Management Forum (CMF);
- for “non-financial” risks:
  - the Legal and Tax Risks Committee,
  - the Compliance Committee,
  - the People Risk Committee, for risks relating to human resources,
  - HTS Committees,
  - the Major Risks and Security Committee; the Information Security Risk Committee and the Business Continuity Committee,
  - the HSBC France central ORIC (Operational Risk and Internal Control) Committees (ORIC Committee and Technical ORIC Committee);
- special committees:
  - the Product Examination Committee,
  - the Complex and/or Structured Deals Approval Committee,

- the Reputational Risk Committee,
- the Model Oversight Committee.

A report on resources dedicated to second level controls is carried out on a regular basis to check their adequacy in terms of skills and number.

#### **The HSBC France central ORIC (Operational Risk and Internal Control) Committees (ORIC Committee and Technical ORIC Committee)**

Management and supervision of permanent control, as defined by regulation 97-02, is the responsibility of the HSBC France ORIC Committee.

Its rules, drawn from those of the HSBC Group, are set out in a ToR (Terms of Reference) and have been adapted to the requirements of regulation 97-02. They are reviewed annually.

The ORIC Committee meets on a quarterly basis under the chairmanship of the Chief Risk Officer. The aim is to ensure that HSBC France's operating permanent control and operational risk management framework meets the requirements of the *Autorité de contrôle prudentiel* and the HSBC Group.

Within this framework, it is the committee's responsibility with regard to operational risk:

- to analyse the operational risks presented by the various business lines and risk functions (in particular major risks) by validating or adapting the controls proposed as necessary with a view to reducing the risks;
- to review the progress made in action plans, in particular those relating to risks deemed the most critical;
- to review major incidents (actual or potential losses and “near misses”) in terms of the amount or type of incident, as reported by the business lines and the central departments;
- to review the compliance of the operational risk framework in respect of regulatory requirements and the HSBC Group requirements (as defined in the GSM, the FIM or Group Circular Letters);
- to review cross-functional issues relating to operational risk management or methodological issues (such as risk assessment, monitoring tool), define and then periodically review operational risk monitoring indicators.

The ORIC Committee comprises:

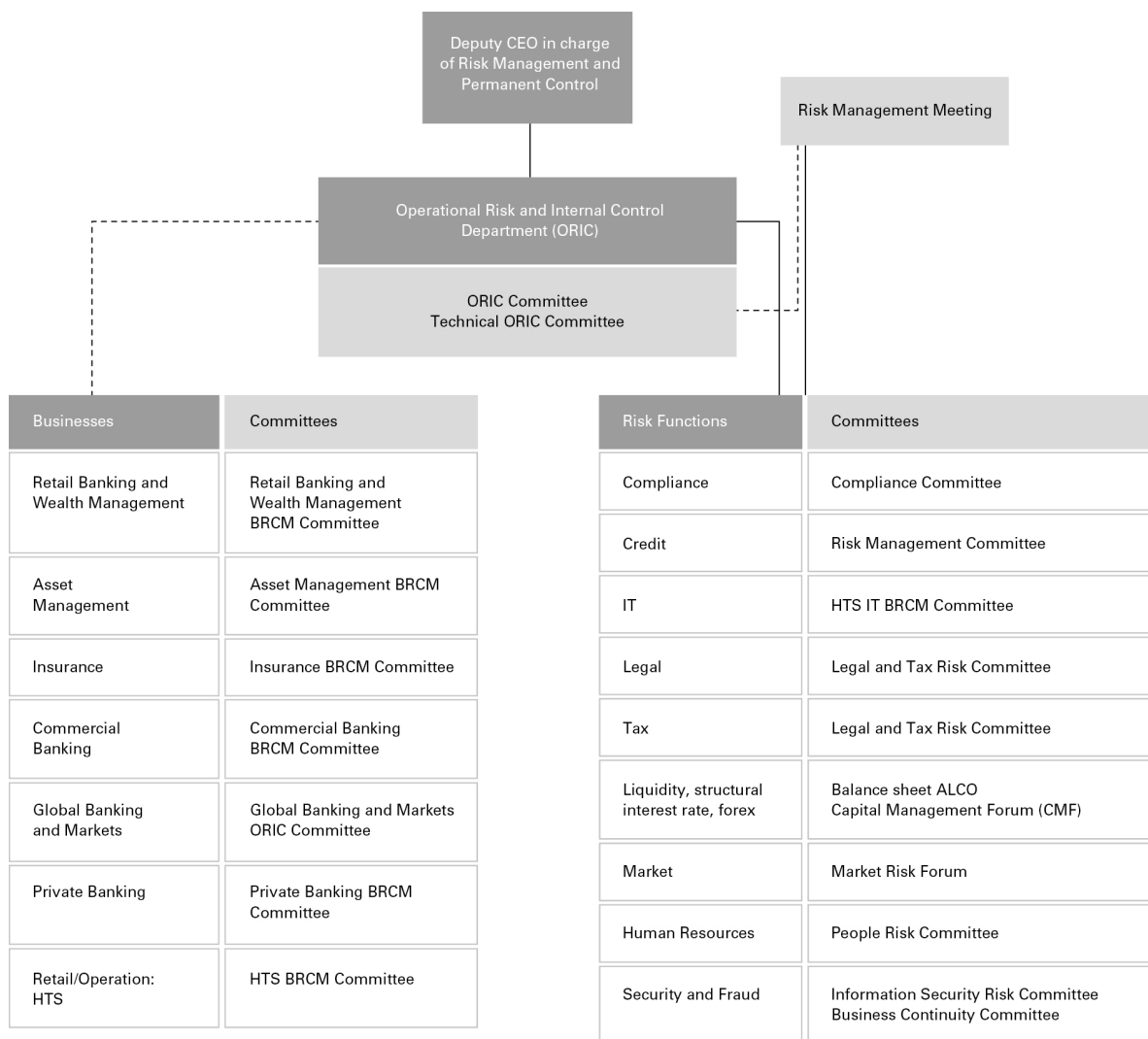
- Heads of HSBC France business lines (Retail Banking and Wealth Management, Commercial Banking, HSBC Technology and Services, Global Banking and Markets, Asset Management, Private Banking and Insurance);
- Heads of the main risk functions;
- the Head of Internal Audit, Head of Group Audit France (GAF);
- the Central ORIC (DCIRO) team, which coordinates the committee and acts as secretary;
- The HSBC France Company Secretary.

## Chairman’s report on corporate governance and internal control and risk management procedures (continued)

The summary of the work and findings of the ORIC Committee is periodically communicated to the Risk Management Meeting and the Audit and Risk Committee of the HSBC France group.

The work of the ORIC Committee is based primarily on the summary of the work of the HSBC France Technical ORIC Committee, which combines all internal control and operational risk management teams of HSBC France business lines and functions, in the presence of a representative of Internal Audit.

The HSBC France Technical ORIC Committee meets quarterly a few days before the ORIC Committee. Discussion of the issues raised allows the Central ORIC (DCIRO) to achieve a summary of the highlights, which constitutes the supporting material for the ORIC Committee. The operating rules of the HSBC France Technical ORIC Committee are described in a specific ToR, which is reviewed annually.



Each business line has an ORIC or BRCM (Business Risk and Control Management) committee, which convenes at least once quarterly. The permanent members of these business line’s ORIC committees include at least one manager of HSBC France’s executive body or the main entity of the business lines and the managers of the various functions contributing to the risk and permanent control framework. A Central ORIC representative attends the committee’s meetings.

Each risk function holds a monthly or quarterly permanent control committee meeting, chaired by the function’s manager, and attended by the function’s members

and experts, business line and Central ORIC representatives and, for some of them, the Deputy CEO.

### The Compliance Committee

The Compliance Committee convenes once quarterly under the chairmanship of the Chief Executive Office of HSBC France, in the presence of the Chief Risk Officer and the Executive Committee members responsible for the business lines. The role of this committee is twofold: it makes decisions relating to the coordination of the compliance control system, and reports to Senior Management about how the system is working, any incidents and the corrective measures applied.

## Permanent control

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### Principles

Permanent control is primarily based on controls carried out by the managers responsible for each activity. The purpose of these controls is to ascertain that the activity is conducted in accordance with all internal and external rules and is up to standard. The key responsibility for permanent control falls to the managers of the various business lines and functions, who must ensure that level-1 controls are conducted in a proper manner compliant with the HSBC Group Standards Manual (GSM), that states “controls should be considered as fully embedded in the activities”.

In addition to first level controls, HSBC France’s permanent control is based on a series of procedures, under the responsibility of the Deputy Chief Executive Officer. These comprise primarily:

- the Central Operational Risk and Internal Control Department (DCIRO), in charge of coordinating permanent control procedures. The DCIRO oversees the work carried out by the ORIC (Operational Risk and Internal Control) and BRCM (Business Risk and Control Management) teams within the business lines and central departments and reports hierarchically to these business line and department heads, as well as control teams within specialist risk functions.  
The hierarchical positioning of this department matches the organisational structure recommended by the HSBC Group as a whole, which combines coordination of permanent control framework (internal control) and supervision of operational risk framework within a single central team;
- the business lines and departments’ internal control and operational risk teams (ORIC or BRCM teams), responsible for coordinating permanent control for the heads to whom they report directly;
- the ten risk functions in charge of specific risks (Accounting, Compliance, Credit, Tax, IT, Legal, Markets, Human Resources, Security and Fraud, Structural interest rate, forex and liquidity). In particular, the Compliance function ensures that all HSBC France group entities control the risk of non-compliance as defined in article 4 p) of regulation 97-02. Pursuant to article 11 of the regulation, the Chief Compliance Officer ensures the consistency and efficiency of compliance control;
- and lastly, a number of committees that examine the results of controls and the main incidents.

In addition to its internal periodic control framework, and with a view to complying with the provisions of the American Sarbanes-Oxley law (SOX), the HSBC Group has implemented since 2006 a framework for documenting and assessing internal control, with regard to the processes and operations involved in drawing up financial statements.

HSBC France’s Finance Department is responsible for coordinating all SOX measures and summarising their results.

Twice a year, the “SOX 4 Way Meeting”, chaired by the Chief Financial Officer, and primarily comprising the Statutory Auditors, the Periodic Control Officer and the Chief Operating Officer (COO) of HSBC France, reviews:

- any deficiencies revealed by SOX control measures (documentation and “self-assessment” of business lines and function within the scope);
- the result of tests run by the Statutory Auditors;
- the progress made in action plans.

At each quarter, HSBC France’s Audit and Risk Committee is informed of the results of controls carried out for SOX compliance purposes and of progress made in the action plans.

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### The ORIC/BRCM framework

The Operational Risk and Internal Control (ORIC) Department is responsible for coordinating permanent control and for providing a forward looking and transverse overview of risks. This department oversees operational risk management and supervises the internal control work of the ORIC teams of the various business lines and departments with which a functional link has been formed.

Central ORIC keeps an up-to-date reference framework of permanent control and ensures a comprehensive coverage of risks.

This organisational structure, based on the model adopted by the HSBC Group, also meets specific French regulation requirements (regulation 97-02 in particular).

The Central ORIC Department team works closely with the business lines and departments’ internal control and operational risk management teams (ORIC and BRCM teams), as well as the various specialist risk functions. Its role is to consolidate and harmonise, covering all entities or structures reporting to HSBC France on key issues such as reviews of risk and control maps, the design and monitoring of action plans, elaboration of stress scenarios, incident declaration, monitoring the introduction of risk indicators, and even reviewing control plans, coordinating the formal definition of key controls and the contents of reports.

The strong functional relationship between the business lines and departments’ internal control and operational risk management teams is based on the following four principles:

- monthly bilateral meetings between the Central ORIC Department and the internal control and operational risk management teams of the business lines and departments (including those in charge of risk functions), at which the subjects discussed include developments in activity and risk trends, progress made in the annual control programme, major incidents (actual or potential losses and near misses), protection of information, etc. At least once a year, risk mapping (in particular operational risk) is more specifically reviewed, as is the draft control programme for the next year and the general assessment of resources allocated to permanent control;

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

- ORIC's participation in the committees, which include:
  - the ORIC and BRCM committees of the business lines,
  - the specialised risk function committees (Legal and Tax Risk, Compliance, IT, Permanent Control, Finance, etc.),
  - the Audit and Risk Committee of HSBC France and the Audit Committees of its subsidiaries;
- submission by the ORIC teams of Risk and Control maps (on an ongoing basis and at least once a year), support documents and minutes of the Audit Committees of HSBC France subsidiaries, annual contributions on internal control and risk management to the annual reports intended for the *Autorité de contrôle prudentiel* (articles 42 and 43 of regulation 97-02);
- other "meeting points":
  - dedicated groups (methods, indicators, risk scenarios, etc.),
  - training and awareness-raising schemes (technical and regulatory watch, "workshops" and seminars, etc.).

Finally, this team acts as an interface with the HSBC Group ORIC function, particularly at its European level. Notably, it is involved in the consolidation and dispatch required reports as well as disseminating in France instructions and best practices of the Group.

Reliability, strengthening and enhancement of internal control and operational risk framework continued in 2012, with a number of highlights. The Group ERF project (Enhanced Risk Framework Project) actively continued throughout the course of 2012, with notably:

- in terms of general governance, the implementation of the HSBC Group "three lines of defence" and the designation of Business Risk and Control Management (BRCM) teams in the HSBC France business lines and departments (redesignation of internal control and operational risk management teams);
- the continuous improvement of the new ORION system rolled out in November 2011. ORION is the sole risk management tool for risk maps and action plans. ORION is also designed to become the sole risk management tool for risk and control monitoring indicators and internal control plans, to be an Enterprise Risk Management tool;
- the roll-out into all business lines and departments of the new risk maps methodology, called the HSBC Group's Risk and Control Assessment (RCA), allowing prioritisation of risks and integrating extreme case scenario;
- the Risk and Control maps review in late 2012 by experts from risk functions and their submission by business lines and departments to the Chief Risk Officer. Early 2013, the Central ORIC Department (DCIRO) will review the Risk and Control maps and the business line and department relevant Heads will validate them. They will be regularly updated according to material events occurred during the year and changes in the risk profile will be submitted to ORIC and BRCM Committees.

RCA's serve as the basis of the ORIC risk management annual control programme;

- the renewal and reliability of some operational risk indicators, for a better risk monitoring;
- the monitoring of risk appetite on a monthly basis and the determination of annual tolerance on operating losses, through close collaboration between business lines and internal control and operational risk management teams;
- participation in the work initiated by the HSBC Group, in particular on stress testing and risk of fraud;
- the further enhancement of controls in areas such as information security and business continuity;
- the improvement in the supervision and control of third party services, including those provided by other HSBC Group entities;
- the updating of old circulars.

Awareness of all employees on risk management was continued in 2012 notably through regular meetings to raise awareness about topical issues or risk-related matters (Lunch & Learn).

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### Organisation of the Compliance function

The HSBC France group's permanent control framework of the risks of non-compliance is coordinated by the Compliance Department. Since March 2006, all compliance personnel within the HSBC France group report to the Compliance Department so as to ensure full independence of the compliance function from operational activities, as required by regulation 97-02. The HSBC France group's compliance control framework and the internal organisation of the Compliance Department are set out in two general implementation circulars, which are updated regularly.

The Chief Compliance Officer is responsible for compliance control at HSBC France, according to article 11 of the aforesaid regulation, and for coordinating the HSBC France group's compliance control framework. In addition, the Chief Compliance Officer also acts as the Compliance Officer for HSBC France's Investment Services (RCSI) according to article 313-4 of the *Autorité des marchés financiers* (AMF) general regulations. The Chief Compliance Officer reports to the Deputy CEO.

The Compliance Department is responsible for overseeing control of the risk of non-compliance, as defined by article 4 p) of regulation 97-02, for all HSBC France group entities. Although his scope of intervention in that capacity extends to all measures applying to banking and financial activities, supervising due observance of regulations in certain specific areas devolves on other risk functions in the HSBC France group, at level one, which have the necessary expertise and means (accounting standards, capital ratios, control of major counterparty risks, recommendations on the security of information system, etc.). In these specialised areas, compliance is controlled within the framework of the HSBC France group's ORIC (Operational Risk and Internal Control) Committee, to which the risk functions are accountable for the smooth running of the control framework in place and for any identified weaknesses and



failures thereof, as well as at the Risk Management Meeting (RMM), which is attended by the Chief Compliance Officer. The Compliance Department's area of competence does not extend to enforcing rules outside the sphere of banking and finance (labour and social security law, regulations on the safety of people and property, etc.), which are supervised by specialised entities of HSBC France.

The Compliance Department is composed of six divisions which report to the Compliance Officer: five divisions specialised by business line (Retail Banking and Wealth Management/Commercial Banking, Private Banking, Global Banking and Markets, Asset Management, Insurance) and a Central Compliance division. The Compliance Department (DCDO) is responsible for all employees in charge of Compliance, pursuant to regulation 97-02, and acting as Compliance Officers for Investment Services (RCSI) for the HSBC France group's legal entities concerned. In addition, some employees of the Compliance function are appointed as TRACFIN representatives for the HSBC France group's legal entities concerned.

The control of non-compliance risks is based on a permanent control system structured around the following themes:

#### **Staff training and awareness**

The Compliance Department, in connection with the Training Department, prepares an annual training plan for staff on non-compliance risks. Training sessions, on-site or through e-learning, are organised in the different business lines.

#### **Identification of non-compliance risk**

The Compliance Department relies in particular on the Legal and Tax Department's monitoring of legislative and regulatory changes and developments in case law that will have an impact on the HSBC France group, their analysis of such changes and definition of their methods of application.

The analysis of non-compliance risks is documented in risk assessments listing the laws, regulations, professional rules and the HSBC Group internal rules that apply to each business line or activity, and the procedures and controls that ensure compliance with these rules. Non-compliance risks affecting the HSBC France group's activities concern the following areas in particular: the struggle against money laundering, terrorist financing and corruption, customer protection, protection of the integrity and transparency of financial markets, professional secrecy and the protection of personal data, business ethics and the prevention of conflicts of interest. Compliance risk maps are updated at least every six months.

#### **Compliance review procedures and tools of detection and prevention**

The HSBC France group has for several years now had specific procedures in place to review compliance, in accordance with the provisions of articles 11-1 to 11-3 of regulation 97-02.

With regard to risks relating to new products and services, as well as to significant changes to existing products, current procedures call for predefined and formal due diligence to be performed by the business lines and

control functions concerned, including the Compliance Department, to ensure that all risks occasioned by the new product or service are duly analysed and taken into account. For that purpose, most of the business lines have set up bodies specifically to review commercial initiatives. At the HSBC France group level, new products and services that meet certain criteria are also subject to prior approval by the Product Examination Committee, which is chaired by the HSBC France CEO, and for which the Compliance Department serves as the secretariat. The Compliance Department is responsible for ensuring that the products comply with both legal and regulatory requirements and HSBC Group standards, and that the Committee's requests and decisions are taken into account before the products are launched.

Controlling compliance of operations relies, on the one hand, on tools of detection and prevention and on the other hand, on recurrent controls carried out by the Compliance Department and internal control and operational risk management teams. Control duties performed by Compliance Department teams (called compliance reviews) are aimed at ensuring due observance of regulatory provisions and the applicable internal rules within a particular activity. New products or services approved by the Product Examination Committee undergo a formal ex-post review within less than 6 months of their launch, coordinated by the internal control and operational risk management teams, to ensure they are marketed under the same conditions as those initially proposed to the Product Examination Committee, and that the related risks were fully comprehended during the approval process.

#### **Overseeing the activities and results of compliance control**

Operational oversight of the compliance control framework and follow-up on any identified discrepancies relies, first of all, on periodic and specific reporting procedures in the Compliance channel as well as the information conducted in the Compliance Committee. The Compliance Officers of each HSBC France group entity prepare a quarterly report on legal and regulatory compliance for the activity within the scope of his or her responsibility and send this report to the Head of Compliance for the business line concerned.

Compliance exceptions are the subject of a report prepared by the Compliance Officer of the relevant entity that is passed on to the appropriate level of the compliance function. Action taken to remedy these incidents is then monitored on a regular basis using a dedicated tool called IRIS (Integrated Regulatory Information System). As part of its consolidated approach to the risks of non-compliance, the Compliance Department also centralises and follows up on the recommendations issued by the supervisory authorities after their intervention in the HSBC France group entities.

The system's mode of operation and the main identified non-compliance risks are reviewed by dedicated control authorities, consisting of compliance representatives and operational managers.

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

### Organisation of accounting

#### Accounting procedures

The Finance Department is responsible for the proper application of the HSBC France group's accounting principles and accounting control procedures. It defines the procedures and controls to be applied under the responsibility of each legal entity's accounting department. This more particularly concerns accounting and reconciliation procedures designed to verify the existence and validity of balance sheets, off-balance sheet statements and, by construction, income statements.

Oversight of the accounting and regulatory audit trail is formally documented in a number of procedures and documents prepared under the responsibility of the departments of the Chief Accounting Officer (CAO) and Chief Operating Officer (COO). These are mainly documents relating to accounting tools and interfaces, accounting charts, certification of the financial statements, statements of user requirements, methods of operation for the audit trail.

The Finance Department maintains and disseminates accounting procedures manuals and circulars, that comply with French GAAP and International Financial Reporting Standards (IFRS). These principles are based essentially on the French Commercial Code, the fourth European Directive, IFRS and all CRC texts and recommendations. They are available on the HSBC France Intranet.

Internal circulars are also sent to the accounting and financial staff of HSBC France and its subsidiaries in order to standardise the level of knowledge and understanding of accounting standards in the group.

#### Organisation of accounting production

The vast majority of reporting documents are produced monthly and on both a non-consolidated and consolidated basis. These departments are responsible for drawing up budgets and action plans in line with guidance provided by Senior Management.

As part of its responsibility for managing accounting function, the Finance Department organised meetings in 2012 to discuss the budget procedure, certification of the financial statements and Sarbanes-Oxley measures.

HSBC France's accounting architecture is based on event-driven operating systems. At the end of each day, an interpreter converts the events into journal entries in the accounting system. As of July 2012, a new accounting software application, Peoplesoft General Ledger (PSGL), was introduced across the HSBC France perimeter. With PSGL, HSBC France has adopted the HSBC Group's chart of accounts, a common language for the accounting and financial function in France enabling better alignment of its processes with those of the Group.

The operating systems are comprised of specialised applications devoted to a particular activity (loans, credit, securities transactions, foreign exchange transactions, etc.). Some transactions, which are not managed by these systems or which are not ordinary events (taxes, provisions, etc.) are

entered into the accounting system using secure manual data entry tools under "Sundry transactions". Like the other operating systems, they send events to the accounting interpreter, thereby benefitting from the controls already in place.

Two sets of accounts are prepared, one under French GAAP and one under IFRS. The HSBC Group's integrated System 9 consolidation software produces IFRS-compliant consolidated financial reporting statements that also meet all the requirements of the *Autorité de contrôle prudentiel* and the parent company.

The introduction of a financial and balance sheet datawarehouse has facilitated reconciliation and ensures that accounting, financial, regulatory and management reports are consistent with financial accounting. The datawarehouse stores data from both HSBC France and its subsidiaries. It contains various types of data: accounting data, inventories, or detailed breakdowns of carrying values depending on the information required for internal and external disclosure. Consistency controls have been established within the datawarehouse, which feeds the consolidation software and is used to produce the various French regulatory reports via the Evolan Report software.

The Chief Accounting Officer's (CAO) teams developed a tool to make use of the audit trail produced by HSBC France's information system, in particular the "datawarehouse". This tool makes it possible to track down the initiating event of a transaction in the operating system. It is also in place for the accounting audit trail and used for financial statements (balance sheet and income statement) and for the SURFI "*Situation*" (financial position) and "*Compte de Résultat*" (earnings) statements. The tables that have been put in place and tested allow for the production of the book-keeping vouchers for all the aforesaid statements contract by contract on demand. Archiving procedures have been specified; financial position statements available online: M (current month), M-1, M-2, MAR (quarterly), JUN (half-yearly), SEP (quarterly), DEC (annual). The other financial position statements remain stored in the databases and are available on demand (36 months of history).

#### Accounting production controls

The bank's financial control environment is based on:

- a framework of monthly accounting certification;
- communication of results and performance management;
- Sarbanes-Oxley (SOX) internal financial control.

According to the HSBC Group's rules, HSBC France draws up a monthly certificate of accounting reconciliation which is sent to the HSBC Group Finance Division, Europe. This certificate attests that all balance sheets and off-balance sheets accounts are properly reconciled and summarises accounting reconciliation certificates provided by the various accounting and financial departments of HSBC France and its subsidiaries. These certifications are formally documented through AssureNET, the Group's accounting certification application, which has been used since the July 2012 close by HSBC France and subsidiaries that have the PSGL accounting software.

This monthly reporting is based on the principle that each general ledger account is assigned to a specific owner who is responsible for its reconciliation and validation. Any irregularities revealed by the reconciliation certificate give rise to the establishment of a corrective action plan by the relevant business lines and departments. The Finance Department's accounting control service conducts reviews in HSBC France departments and its subsidiaries to ascertain due application of control procedures and the quality of the supporting documents.

In addition, during its periodic audits of various entities and themes, Internal Audit systematically verifies the consistency of accounting charts and analyses samples of accounting entries to ensure that the quality of the reconciliation process implemented is adequate.

Statements to the supervisory authorities that contain accounting information are prepared directly by the HSBC France operational departments, *via* the central CAO Department, and the finance departments of the subsidiaries. Each accounting or finance officer examines and validates the information.

Financial reports are submitted to the Chief Financial Officer and Executive Committee of HSBC France and, before the financial statements are published, sent to the HSBC Group's Finance Department for presentation to the HSBC Bank plc's Executive Committee and HSBC Group Management Board (GMB).

Within the HSBC France group, financial control is decentralised at the operational department and subsidiary levels. Operational departments and subsidiaries report monthly to their own management and to the Finance Department. The CFO presents the results to the Executive Committee each month and reports to the HSBC France Board of Directors.

The HSBC France's Audit and Risk Committee examines the quarterly, interim and annual financial statements submitted to the Board of Directors.

In order to comply with the American Sarbanes-Oxley Act (SOX), which has been applicable to the HSBC Group since the 31 December 2006 close, HSBC France's management must carry out an in-depth assessment of the internal control procedures used in drawing up financial statements. The most significant processes in this respect are thus the subject of detailed documentation and specific controls, supervised on a regular basis as part of the quarterly review system. These detailed analyses of flows of transactions to accounts help improve audit trail control. Weaknesses identified by such controls must be corrected as soon as possible and a dedicated team has been set up to oversee and coordinate all such work.

Internal Audit plays an active role in ensuring that the SOX arrangements are properly applied, by carrying out independent tests on the corresponding controls performed during periodic control assignments. The SOX team – part of the Finance Department – has access via the HSBC Group's Audit Issues Database (AID) to the audit issues raised by the various audit teams, enabling it to follow up

the SOX recommendations issued by periodic controls across the entire accounting and financial scope. The Statutory Auditors, for their part, conduct an annual review of the work carried out on behalf of the HSBC Group Auditors, who in turn give their opinion on the SOX 404 report prepared by the management of HSBC Holdings plc. They also review SOX risks on a quarterly basis and audit the associated processes at the end of the year.

Each quarter, HSBC France's Audit and Risk Committee is informed of the results of controls carried out for SOX compliance purposes and of progress made in the action plans. A certificate signed by the CEO, the CFO, and the Head of Internal Audit is sent twice a year to HSBC Bank plc, attesting to the effectiveness of financial internal control procedures and where appropriate specifying any weaknesses undergoing correction as identified by those in charge of assessing controls.

## Periodic controls

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In accordance with regulation 97-02 as amended, periodic controls aim to ascertain the compliance of operations, the levels of risk actually incurred by the bank, due observance of the procedures and the efficiency and appropriateness of the permanent control frameworks, by means of independent investigations conducted by central agents qualified for this purpose. The periodic control framework applies to the entire company, including subsidiaries.

The INA 13 strategic review, initiated in 2010 by the HSBC Audit Group (Global Internal Audit – GIA) to develop and update the various audit structures and methods worldwide, was completed at the end of 2012. There are now ten global groups whose role is to provide expert coverage of the HSBC Group's core business lines and functions, which are themselves global. This new structure is designed to highlight for the Group Management Board (GMB) the material risks to which the Group may be exposed.

Alongside these specialised audit groups, there are five audit groups with regional competence (Europe, Middle-East, North America, Asia-Pacific and Latin America), as well as local audit groups. The local groups include Group Audit France (GAF), whose competence is restricted to the HSBC France scope. It reports to European Audit.

Responsibility for HSBC France's periodic controls is now shared by two separate though closely coordinated entities:

- Group Audit France (GAF), based in France, which mainly audits the central functions, Retail Banking and Wealth Management, Commercial Banking, banking operations and IT;
- HSBC Global Internal Audit (GIA), whose areas of involvement are:
  - Global Businesses and Functions and European Audit (IAF), responsible for auditing Global Banking and Markets, Insurance and pension costs, Asset Management and Private Banking. Its scope also encompasses asset and liability management,

## Chairman's report on corporate governance and internal control and risk management procedures (continued)

capital requirements, accounting, financial control and taxation, as well as oversight of the global functions and service delivery. IAF has regional competence for Europe,

- Risk and Asia-Pacific Audit (IAG), responsible for auditing Commercial Banking, Retail Banking and Wealth Management, and their associated services, credit risk for large corporates and strategy, operational risk management and permanent control, compliance, security and fraud. IAG has regional competence for Asia-Pacific,
- IT Audit, responsible for auditing infrastructures, information and communication systems, and applications projects and developments.

The respective scopes of local audit (GAF) and global audit (GIA) converge and are consolidated in the HSBC France audit plan. The teams have regular exchanges, based particularly on the agreement entered into for that purpose on 28 March 2011 between the HSBC Group's Chief Internal Audit Officer and the head of GAF.

Although the organisational structure of periodic controls has changed radically, its true purpose remains the same that is to check and assess the quality of risk management and control systems by ascertaining both due observance of national regulations applicable to the audited area and the correct application of standards and procedures in force within the HSBC Group. In the hierarchy of HSBC Group controls, Internal Audit is the "third line of defence", intervening after the first line of defence in the various business lines and central departments and then the permanent control teams (BRCM and ORIC).

All Audit work is performed in accordance with the HSBC Group's audit standards, as set out in particular in the Group Audit Standards Manual (GASM). The GASM is updated a number of times a year, and the consolidated version should be re-read by auditors at least once a year and its recommendations implemented during each audit.

In addition, the HSBC Group's auditing standards are set forth, in GAF, in internal procedures or appropriate operating procedures. The reference framework formed by all these documents is used by the audit teams to conduct their audits. This corpus has now been revised and updated, particularly in accordance with recommendations following the intervention of the *Autorité de contrôle prudentiel* (ACP) in September 2010 concerning HSBC France periodic control procedures.

The audit approach is based on an assessment of all risk components specific to each auditable item (entity, theme or project), and is implemented with the Audit Information System (AIS) tool developed by the HSBC Group. In 2012, HSBC France's audit plan was drawn up in close collaboration between GAF and GIA, drawing primarily on the results of the "Risk Calculator" tool, used to oversee risks and ensure their consistency across the entire HSBC France scope.

Lastly, the dual grading of audit reports, which was tested in early 2011, has subsequently been confirmed through:

- a grade covering the quality of controls implemented by the auditee ("Control Risk Grade"), based on an either/or choice (Satisfactory/Not satisfactory);
- a grade reflecting the degree of control over the auditee's risk by its management team (Management Awareness Grade – MAG) based on information provided by the management team in the Management Self-Identified Issues (MS-IIs), which are drawn up to back up the audit. The MAG is still established on the basis of a three-ratings scale (Acceptable / Needs improvement / Inadequate).

Audit reports and their dual grades are sent to the entity's management or the person in charge of the audited process, who is ultimately responsible for ensuring that Internal Audit's recommendations are implemented, as well as any recommendations made by the supervisory authorities or the Statutory Auditors. The Chief Operating Officer, Compliance Officer and Internal Control and Operational Risk Officer always receive a copy of the reports.

Lastly, all audit reports relating to HSBC France which receive an unfavourable Control Risk Grade and/or MAG are presented to HSBC France's Audit and Risk Committee by the head of Internal Audit. This Committee also monitors all high risk audit recommendations relating to the HSBC France scope.

*The set of procedures referred to in this report constitutes the basis of HSBC France's internal control system. Senior Management is responsible for overseeing the systems with support from the internal control function, particularly to ensure consistency.*

*Following major efforts throughout the HSBC France group, Senior Management now has the resources to comprehensively assess the quality of internal control.*

Samir Assaf  
Chairman

Paris, 27 February 2013

## **Statutory Auditors' report prepared in accordance with article L. 225-235 of the French Commercial Code, on the report prepared by the Chairman of the Board**

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*This is a free translation into English of a report issued in French and provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and is construed in accordance with, French law and professional auditing standards applicable in France.*

*Year ended 31 December 2012*

To the shareholders,

In our capacity as Statutory Auditors of HSBC France, and in accordance with article L. 225-235 of the French Commercial Code ("*Code de commerce*"), we hereby report on the report prepared by the Chairman of your company in accordance with article L. 225-37 of the French Commercial Code ("*Code de commerce*") for the year ended 31 December 2012.

It is the Chairman's responsibility to prepare, and submit to the Board of Directors for approval, a report on the internal control and risk management procedures implemented by the company and containing the other disclosures required by article L. 225-37 of the French Commercial Code ("*Code de commerce*") particularly in terms of the corporate governance measures.

It is our responsibility:

- to report to you on the information contained in the Chairman's report in respect of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information; and
- to attest that this report contains the other disclosures required by article L. 225-37 of the French Commercial Code ("*Code de commerce*"), it being specified that we are not responsible for verifying the fairness of these disclosures.

We conducted our work in accordance with professional standards applicable in France.

### **Information on the internal control and risk management procedures relating to the preparation and processing of accounting and financial information**

These standards require that we perform the necessary procedures to assess the fairness of the information provided in the Chairman's report in respect of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information. These procedures consisted mainly in:

- obtaining an understanding of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information on which the information presented in the Chairman's report is based and existing documentation;
- obtaining an understanding of the work involved in the preparation of this information and existing documentation;
- determining if any significant weaknesses in the internal control procedures relating to the preparation and processing of the accounting and financial information that we would have noted in the course of our engagement are properly disclosed in the Chairman's report.

On the basis of our work, we have nothing to report on the information in respect of the company's internal control and risk management procedures relating to the preparation and processing of accounting and financial information contained in the report prepared by the Chairman of the Board in accordance with article L. 225-37 of the French Commercial Code ("*Code de Commerce*").

### **Other disclosures**

We hereby attest that the Chairman's report includes the other disclosures required by article L. 225-37 of the French Commercial Code ("*Code de Commerce*").

Paris-La Défense and Paris, on 12 April 2013

KPMG Audit FS II  
Pascal Brouard  
*Partner*

BDO France – Léger & Associés  
Michel Léger  
*Partner*

## Corporate, social and environmental responsibility

### HSBC Group's Corporate Sustainability strategy

At HSBC Group, it is understood that long term success of business is closely connected to the environmental, social and economic landscape in which the Group operates. Corporate sustainability means achieving sustainable profit growth so that the HSBC Group can continue to reward shareholders and employees, build long-lasting relationships with customers and suppliers, pay taxes and duties in those countries where it operates, and invest in communities for future growth. The way the HSBC Group does business is as important as what it does. Its responsibilities to its customers, employees and shareholders as well as to the countries and communities in which it operates go far wider than simply being profitable.

HSBC France is fully committed to the course of action adopted by the HSBC Group, integrating these principles and practices in all its activities.

#### Business finance

The HSBC Group aims to build long-term customer relationships, around the world, through the provision of a consistent and high-quality service and customer experience. It uses the benefits of its scale, financial strength, geographical reach and strong brand value to achieve this.

It aims to take advantage of the opportunities and manage the risks presented by emerging global trends by developing sustainable business models to address them.

HSBC understands that the world is changing and the threats of climate change and its impact on availability of natural resources are becoming ever more real. Increasing urbanisation, a growing population and rising commodity prices, all raise concerns over potential resource constraints. For example, as recent HSBC research shows, climate change means that past hydrological trends are no longer indicative of future availability of freshwater. People face local water supply shortages as global demand increases.

HSBC plays a leading role in shaping the market response to these challenges, identifying how business can adapt in ways that bring both social and environmental benefits, while providing viable economic returns. Throughout 2012, its Climate Change Centre of Excellence has continued to research the likely effects that climate change, and the responses to it, will have on its business and those of its customers. In the last year, HSBC Global Research has published reports on "Water Stress – Analysing the global challenges" and "Less bread for your dough – The impact of rising food prices on the global economy".

HSBC's Climate Business Council in charge of the definition of the HSBC "Climate Business" strategy, supports Global Businesses to identify customer opportunities arising from the shift to a low carbon economy. HSBC's Global Banking and Markets teams played a leading role in some of the largest renewable energy projects announced in 2012.

In particular, HSBC provided a range of financial services to the largest offshore wind project in Europe and the most powerful wind farm in Latin America. The two projects combined will provide over 666 megawatts of clean energy, equivalent of enough electricity to power over half a million homes. These deals highlight the HSBC Group's credentials in providing asset finance within the low carbon energy market and the strength of commercial teams working across several markets.

#### Operational environmental efficiency

HSBC focuses its environmental initiatives primarily on addressing and responding to issues associated with climate change, including energy use, water and waste management. The Group continues to focus on the ten goals of its operational sustainability strategy announced at the end of 2011. Between 2012 and 2020, the aim is to reduce annual employee carbon emissions by one tonne, from 3.5 to 2.5 tonnes.

#### Community investment

The HSBC Group has a long-standing commitment to the communities in which it operates. Many of its key markets are emerging economies. Beyond its core business, the HSBC Group aims to encourage social and economic opportunity through community investment activities.

HSBC focuses on education and the environment because it is believed they are essential building blocks for the development of communities and are prerequisites for economic growth. These philanthropic programmes aim to involve employees in the work of local NGOs and charities. HSBC global education programmes focus on helping disadvantaged children, promoting financial literacy and environmental education and understanding.

In 2012, HSBC launched its new flagship environmental programme, the HSBC Water Programme. This is a five year, USD 100 million programme in partnership with three NGOs which rank amongst the world's most respected environmental and development organisations. Together with Earthwatch, WaterAid and WWF, the Programme will deliver the powerful combination of water provision, protection, information and education; resulting in the most ground-breaking water programme committed to by a financial organisation. The Programme will benefit communities in need and enable economics to prosper, driving development and social-economic growth. Following the success of the previous HSBC Climate Partnership, this programme will create a community of employees and opportunities for employee involvement and volunteering.

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## Employees

“Employee engagement” describes employees’ emotional and intellectual commitment to their organisation and its success. It is critical to the long-term ability of the HSBC Group to deliver the highest quality of financial services. At a global level, HSBC has conducted for six years now recurring institutional surveys among its staff members. Up to 2011, the Global People Survey (GPS) was the main element of this device. Conducted once a year, it covered all key dimensions of the company. HSBC’s employee survey process evolved in 2012 with the introduction of a supplementary study called “Pulse”. Refocused on issues related to the organisation’s development and conducted quarterly on a random sample of employees, Pulse measures the perception that employees have of their professional environment and the opportunities it offers them. In parallel, GPS is now carried out every other year. By establishing the opinions of its employees, the HSBC Group demonstrates its willingness to involve them as key players bound to the company’s strategy and encourages the development of a culture of dialogue and co-responsibility.

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## Sustainability governance

Along with its values, robust risk management and good governance, the HSBC Group commitment to operating sustainably guides the way it manages its business and helps to deliver value to its shareholders and customers.

The HSBC Group Corporate Sustainability Committee is responsible for overseeing the Group’s Corporate Sustainability policies (principally environmental, social and ethical matters) and for advising the Board, Committees of the Board and Executive Management on such matters.

HSBC has a global Corporate Sustainability function with Heads of Corporate Sustainability in each region and major country of operation. At an operational level, implementation of its sustainability policies is managed primarily by the Corporate Sustainability, Human Resources and Risk functions.

The HSBC Group reports on progress in developing and implementing its sustainability strategy annually in the HSBC Sustainability Report, which is independently assured.

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## HSBC France’s role in the economy and in favour of corporate sustainability

### HSBC France’s territorial, economic and social impact

Through its activity, HSBC France makes its own contribution to the financing of the economy and the smooth running of society. By ensuring a sound business base and sustainable income, the bank is able to distribute dividends to its shareholders, remunerate its employees, pay its suppliers and cover its tax liabilities. The bank supports the development of its retail, corporate and institutional

clients and also that of the French regional and local authorities, by granting loans, by providing for their future through investments, and *via* secure domestic and international transactions.

### HSBC France – distribution of income

| <i>(in millions of euros)</i>                                       | 2012 | 2011 |
|---|------|------|
| Net cash outflows in respect of taxes...                            | 458  | 323  |
| Distributions to shareholders<br>and non-controlling interests..... | 240  | 118  |
| Salaries and employee benefits.....                                 | 993  | 998  |
| General expenses .....  | 543  | 558  |

In a French mortgage market down 32 per cent<sup>1</sup> in terms of new lending, HSBC France Retail Banking and Wealth Management business reported strong growth with EUR 2.7 billion in new residential mortgage loans, an increase of 39 per cent compared with 2011. The total customer loan book grew by 8 per cent over the year.

HSBC in France Commercial Banking business continued to support businesses in their growth, increasing its average commercial loan book from EUR 9.6 billion in 2011 to EUR 9.9 billion in 2012. For 2013, an additional lending envelope of EUR 1 billion has been allocated to business clients to support them in their international development.

Also, since the beginning of the financial crisis, access to credit has become increasingly difficult for French regional and local authorities. Using capital markets enables them to optimise and diversify the cost of funding their investments (schools, transport, etc.), thus contributing to the appeal and dynamism of the areas under their responsibility.

Thus, 2012 was a record year for regional and local authorities for issuing bonds. HSBC France, which has unrivalled experience, in this respect, on disintermediated capital markets, conducted 16 out of 33 transactions in 2012 – two of which were SRI (Socially Responsible Investment) transactions, and 47 out of 133 transactions since 2000. HSBC is also the leader in arranging EMTN programmes and commercial paper programmes for regional and local authorities.

Finally, HSBC France continues to adapt its branches and websites to meet the needs of the disabled. In 2012, 155 of its 315 branches were accessible. The website [www.hsbc.fr](http://www.hsbc.fr), like all public sites of the HSBC Group, respects the “Web Content Accessibility Guidelines 2.0” (WCAG 2.0) defined by the World Wide Web Consortium (W3C). In addition to these rules, HSBC websites are regularly reviewed by an independent firm. These reviews are defined and conducted directly by the Marketing Department at Group level for public websites.

<sup>1</sup> Banque de France.

## Corporate, social and environmental responsibility (continued)

### Sustainability at HSBC France

#### Governance

In order to deploy and effectively implement this strategy in France, HSBC France created in 2008 a Sustainability Department, reporting to the Chief Executive Officer. Consisting of a team of eight, it coordinates the implementation of the action plans developed in collaboration with representatives in each of the business lines concerned.

A Sustainability Committee bring them together quarterly, with a main objective to report on progress or any constraints to the deployment of this strategy. In 2012, this committee was merged with the Corporate Sustainability Finance Committee set up in 2011, following the example of the HSBC Group's Climate Business Council, in order to share the decisions taken at HSBC Group level with the heads of business lines and to identify local opportunities able to contribute to the achievement of its objectives. Accordingly, the new quarterly Sustainability Committee alternately brings together heads of business lines in order to validate the strategic direction, and operational managers in charge of the implementation of the action plans.

In 2009, HSBC France rounded off the process by setting up a committee dedicated to the management of the operational environmental efficiency and which is responsible, in collaboration with the HSBC Group, for coordinating action plans for managing the Group's environmental footprint. It is comprised of business line managers who are responsible for these objectives: purchasing, IT, real estate, travel, logistics, communication and sustainability.

Finally, a Diversity Committee, set up in 2010, aims to deal with issues related to diversity in order to propose action plans to the People Committee France, whose role is to enable HSBC France Senior Management to address all strategic human resources issues on a monthly basis.

#### Action and reporting

In support of its activities, HSBC France is a member of the ORSE (*Observatoire de la Responsabilité Sociale de l'Entreprise*) and the steering committee of the *IMS-Entreprendre pour la Cité* organisation. These two independent institutions work with member companies, stakeholders from civil society and their transnational counterparts in order to fully define the issues and to identify good practices in the field of corporate responsibility. HSBC France also serves on the *Collège des Directeurs du Développement Durable – (C3D)*, an independent organisation set up to publicise the opinions of heads of Corporate Sustainability from medium-sized and large companies and organisations.

Finally, to report on its progress, since 2011 HSBC France has been publishing the *Revue de la Fondation HSBC pour l'Education* (HSBC Foundation for Education Review) and publishes a sustainability report alongside that of its parent company, HSBC Holdings plc. In France, these reference documents are available exclusively on the HSBC France website<sup>1</sup>.

Relations with individuals or organisations interested in the company's activities

#### Retail and corporate customer consultation

##### *Customer experience and satisfaction*

For HSBC France, the customer experience must meet expectations and be in line with the level of service demanded by the HSBC Group. In fact, HSBC aims to be the benchmark bank for wealth management and the leading commercial bank and strives for excellence in the quality of services provided to its target customers.

A dedicated team is responsible for monitoring the customer experience. For retail customers, a "customer's voice" enables to measure the performance of the bank in terms of customer satisfaction on a monthly and quarterly basis, and twice a year enables a comparison with competitors to be made. A survey into service quality at branch level is also conducted regularly. These results (client scores and comments from each branch) are submitted to branch managers, and, since 2011, have been part of the calculation of the variable remuneration element for all branch employees, as are the results of undercover branch visits.

2012 has been a year of development, to improve customer service and simplify their relations with the bank. Two main approaches have been implemented. The first consisted in developing new functionalities for "remote" banking channels to streamline the customer process, in particular the launch of the mobile application simplifying day-to-day banking and corresponding to new "consumption patterns". The reorganisation of branch telephone systems has also enabled a significant improvement to be made to the bank's telephone services, including immediate solutions as well as the centralisation of a number of administrative tasks to improve the quality and speed of processing. Increased expertise of branch advisors was the second development area. This notably resulted in the doubling of the number of investment advisors and of training programmes followed by the entire sales force towards 2011 and the creation of a new Direct branch dedicated to *Premier* customers. This complements the two other direct branches of the bank: *Premier International Direct* for non-resident and non-French speaking customers, and *Advance Direct*, dedicated to HSBC Advance customers. By the end of 2012, these three branches had 17,000 customers.

The retail customer satisfaction rate was relatively stable over the year. In the 4th quarter of 2012, the rating for very satisfied customers stood at 50 per cent<sup>2</sup>, putting HSBC above the average of its competitors. The score of customers who recommended HSBC during the past two years was 40 per cent, higher than in 2011, which keeps the bank at the top spot in the market<sup>2</sup>.

<sup>1</sup> [www.hsbc.fr/CorporateSustainability](http://www.hsbc.fr/CorporateSustainability) section.

<sup>2</sup> *Retail Banking and Wealth Management Barometer – HSBC, 4<sup>th</sup> quarter 2012.*



For corporate clients a “customer voice” system has been introduced for the most important customers in CAE (*Centre d’Affaires Entreprise*) and CBC (Corporate Banking Centre). This annual measurement called the “Client Engagement Programme” makes it possible to compare HSBC to clients’ other banks. Corporate clients are on average just as satisfied with HSBC as their other bank, and CAE clients are much more satisfied with HSBC than their other bank, whichever bank it may be. Customers particularly value the relationship they have (87 per cent of them for over one year) with their account manager.

#### *Customer service*

The Customer Relations Centre (CRC) was voted best customer service in 2012 by the Human Consulting Group. For four years now, this firm has been comparing businesses’ service quality. The study aims to identify, within the context of the current economic crisis, whether customer relations remain at the centre of companies’ marketing strategies. HSBC France was ranked among the leading companies in terms of Customer Service (moving up two places from 2011) and one of the top 5 companies in France (moving up one place from 2011).

The overall number of complaints recorded in 2012 by HSBC France decreased by 3 per cent. Retail and professional clients saw complaints decrease by 5 per cent, while the number of complaints from corporate clients increased by 6 per cent.

These complaints mainly related to account operation and pricing, representing 37 per cent of complaints: disputes, demands for refund of various charges and commissions and requests for explanation of account statements.

The next largest category (18 per cent) was for complaints relating to banking operations, mainly domestic or international transfers: lead times, currency exchange and transfer commissions and currency conversion rates.

Complaints about bank cards, although lower than the previous year, accounted for 9 per cent of the total. They concerned the management of fraud, ceiling limits, lead times for changing cards and rates for transactions carried out abroad.

Customer service and support complaints accounted for 8 per cent of the total, mainly due to the frequent changing of relationship manager or to difficulties experienced by customers in contacting their advisor.

Finally, loans accounted for 7.5 per cent of total complaints, relating to delays in processing applications, borrower insurance administration issues and issues related to negotiations of amended terms of credit.

Complaints addressed to HSBC France’s ombudsman decreased by 5 per cent from 2011 and the number of files directly processed (referral) by the ombudsman fell by 14 per cent, a reflection of improved handling of customer requests by the various levels of the complaints process within HSBC France.

#### **Employee consultation**

In addition to the GPS survey, which will be conducted for the next time in 2013, the Pulse survey covers 25 per cent of employees worldwide each quarter and serves as a management tool by providing a faster and more accurate measurement of the management of the business as viewed through a variety of indicators. One of the results shows that 90 per cent of French employees questioned consider that “managers/directors show a willingness to implement the Group strategy”, while only 68 per cent believe that they can focus their efforts on their priority tasks.

Employee consultation is also structured through the stress monitoring process and the system for detecting psycho-social risks<sup>1</sup>.

HSBC France has also performed a Philanthropic Assessment, carried out by CerPhi and Equitel. This survey showed that the bank’s commitment is perceived positively by employees. 62.1 per cent say they are familiar with the sponsorship activities of HSBC France and 87 per cent think that the actions and the themes of HSBC sponsorship policy are consistent with the company’s business and values.

#### **Industrial relations: discussions with employee representatives and summary of collective agreements**

The provisions of the company agreement regarding discussions with employee representatives, the purpose of which is to strengthen the dialogue process within the context of strategic reorganisation plans, were implemented at the time of the proposed optimisation of the Finance and Operations departments within Global Banking and Markets.

In addition to examining the impact of this project, work carried out with the various HSBC France employee representative bodies (the Central Works Council, Works Committees, Employee Representatives and the Health, Safety and Working Conditions Committees) resulted in 486 meetings taking place during 2012.

In addition, the 2014 Strategic Plan Monitoring Committee met six times in 2012, during which management presented to employee representatives progress updates of the Strategic Plan for each of the businesses concerned, as well as associated assistance measures (early retirement, supported retirement, internal mobility and training).

Negotiations with trades unions, meanwhile, resulted in the signing of four agreements and five amendments to existing agreements:

- Amendments 4-5-6 relating to the Reimbursement of Medical Expenses Collective Guarantee Scheme;
- HSBC France employee profit-sharing agreement;
- HSBC France employee incentive plan agreement;
- Agreement on HSBC France exceptional measure for 2012;
- Amendment 2 to the collective agreement relating to the HSBC France Company Savings Plan;

<sup>1</sup> See page 64.

## Corporate, social and environmental responsibility (continued)

- Record of disagreement relating to the HSBC France annual salary negotiations for the year 2013;
- Amendment to the Working Hours agreement of 15 October 2008 relating to the *compte épargne-temps* (working time savings accounts);
- Agreements relating to payment of reduced working hours (RTT).

Eight agreements were also signed relating to the elections of employee directors on the HSBC France Board of Directors, of employee representatives to the four works committees for Paris and the provinces, and of employee representatives.

### Subcontractor and supplier policy

By analysing the answers given by suppliers to five issues related to corporate sustainability and notably relating to their responsible practices and certifications from ISO (International Standard Organisation), FSC (Forest Stewardship Council) and the Diversity Label of AFNOR (*Association Française de Normalisation*), corporate sustainability criteria have become an integral part of the factors taken into account when selecting suppliers *via* tender.

In addition, all suppliers must be fully aware of the HSBC Group Code of Conduct and indicate their compliance by returning a signed copy.

Finally, when suppliers make use of one or more subcontractors to provide the service awarded to them, they must formally obtain prior agreement from HSBC under the terms of which they remain solely responsible for all their obligations.

In 2012 the use of the Group's back office platforms (Group Service Centers - GSC) continued for the main business lines of HSBC France (Commercial Banking, Retail Banking and Wealth Management, Global Banking and Markets and Service Delivery) as well as for some global functions (Compliance, Human Resources and Finance). The Krakow, Bangalore, Hyderabad and Cairo sites remain the main partners of the HSBC Group in France. For almost six years, HSBC France has established strong relationships with these teams in compliance with the principles of the HSBC Group and the pursuit of customer satisfaction.

The total number of HSBC colleagues working for France within GSC is in the order of 750 FTEs (Full-Time Equivalent) as of the end of 2012.

### Communications

To raise awareness of its commitment, HSBC France participates in targeted events in order to convey to a diverse audience, both internal and external, its vision of corporate sustainability, as well as information and data relating to its policy in this area. This approach promotes a rich dialogue with all stakeholders. Accordingly, HSBC France was, in particular, a partner for the sixth consecutive year in the *Ateliers de la Terre*, an annual international sustainable development forum; in Green Dating, a monthly sustainable economy meeting held at

HSBC France head office; in PEXE, a French eco-business association, and at the Global Water Forum which was held in Marseille in 2012. The bank also supported the publication of the book by Christian de Perthuis entitled "*Et si le changement climatique nous aidait à sortir de la crise ?*" ("What if climate change was able to help us out of the crisis?") released in January 2012, a study by the consultancy firm Utopies concerning new trends in extra-financial reporting and sustainable development, and the Terra Eco magazine for the 2011-2012 period.

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Fair commercial practices: ensure business integrity through governance, compliance and respect for human rights

### Governance

At HSBC France, corporate governance is one of the cornerstones of its strategy. Since its integration within the HSBC Group, the bank has continued to apply the corporate governance rules of listed companies, taking into account its unlisted subsidiary status. In accordance with French law no. 2008-649 of 3 July 2008, transposing the European directive 2006/46/EC of 14 June 2006, the company refers in the first instance to the Code of Corporate Governance for listed companies published in December 2008, and revised in April 2010, by the AFEP and the MEDEF.

However, HSBC France being a 99.9 per cent subsidiary of the HSBC Group and its shares not being listed on a regulated market, certain principles of the Code of Corporate Governance had to be adapted. In some areas, HSBC France applies rules of corporate governance from the United Kingdom (The Combined Code on Corporate Governance) to which its parent company, HSBC Holdings plc, refers.

On 31 December 2012, the Board of Directors of HSBC France consisted of seventeen Directors, two of whom hold positions within the HSBC Group, three members of the Executive Committee of HSBC France, eight independent Directors and four Directors elected by the employees. Not including Directors elected by the employees, three women and ten men. In addition, the Board of Directors is assisted by two committees: an Audit and Risk Committee composed of independent Directors and a Nomination and Remuneration Committee, chaired by an independent Director. The Board of Directors receives regular updates on the company's policy of corporate sustainability and on the way the bank's business lines manage the social and environmental impact of their activities.

### Compliance

The Compliance function, established at HSBC France in 2001, is responsible for ensuring that the company's activities are carried out with integrity and professionalism, complying with the laws, regulations and good practices that are in force in France.

In 2012, special attention was paid to the saver protection system, both within the context of implementing the recommendations of the ACP (French Prudential Supervisory Authority) and the AMF (Financial Markets Authority) regarding the processing of customer complaints, and also regarding customer access to information. Compliance teams worked on the strengthening of anti-corruption measures with the implementation of internal rules to evaluate the risk of relations with our suppliers.

In the sphere of anti-money laundering, a new tool to filter unusual client transactions within the HSBC France network supplements the aforementioned system in order to provide customers with an even more secure environment.

#### **Other actions in support of human rights**

The HSBC Group is a signatory of the Global Compact, which applies to all of its subsidiaries including HSBC France. Its commitment in support of human rights also finds expression in risk management policies related to climate change<sup>1</sup>, which stipulate HSBC Group requirements in this field. As an illustration, in the forestry sector, the approach of the HSBC Group is to safeguard the traditional or contractual rights of the communities living in the forests, including the protection of indigenous peoples' rights, the maintenance of relations with the community, the benefits for local communities, the protection of workers' rights and dispute resolution mechanisms.

### **2012 highlights**

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#### **Integration of corporate sustainability in business lines**

The three key trends that shape the integration of corporate sustainability issues into the banking business in France are the need to anticipate the impact of climate change on the bank's activities, the rising integration of environmental, social and governance issues in the assessment of company performance and the development of a social and solidarity-based economy.

#### **Risk management related to the impact of climate change**

In 2003, the HSBC Group signed up to the Equator Principles, which are a set of guidelines helping willing financial institutions to assess and monitor the social and environmental impact of infrastructure projects. The HSBC Group has expanded on its own initiative the Equator Principles to corporate loans, export financing and other project financing tools.

In addition, assessing the environmental and social impact of financing granted to the bank's customers has been integrated into the HSBC Group's risk management procedures, which are applied by all teams worldwide. To ensure consistency of the analysis and approval procedures, a system of environmental and social risk assessment was established to record and monitor client firms operating in sensitive sectors throughout the world, and to obtain more precise information on the Group exposure when managing risk over time.

The sectors identified as priorities and for which an internal policy has been developed in order to determine the manner in which they are supported, are the forest and its derivative products, fresh water, mining, chemistry, energy and defence<sup>2</sup>.

To improve its risk management, the HSBC Group regularly reviews its internal sector policies. The latest reviews focused on defence (HSBC Global Asset Management (France) publicly confirmed that cluster bombs are excluded from funds held under active and is working to the exclusion of this type of business in its trackers) and on chemistry (simplified policy).

The approach taken by HSBC for its business dealings in these sensitive sectors always involves dialogue with the client, to help him to comply with international standards. However, as a last resort, the Group ceases all relations with a client that does not meet its requirements or which has not made significant progress.

For two years now, HSBC has been measuring clients' compliance with its internal policies. In 2012, 0.10 per cent were non-compliant – a decline of 0.05 point from 2011. Furthermore, in 2012 the HSBC Group conducted an internal audit of account managers, in a number of countries including France, regarding their compliance with assessment procedures related to environmental and social risks associated with loan applications.

Apart from procedures required by the Group which involve the implementation of sector-specific guides, Global Banking and Markets and Commercial Banking teams are made aware of the sustainable development risks within the context of continuous training programmes, in coordination with the Sustainability Risk managers of the bank's credit risk teams.

#### **Opportunities related to the impact of climate change**

In late 2011, HSBC France identified the main economic sectors, locally, involved in the fight against climate change in order to better understand how the bank could support them in their domestic and international development. In practice, this initiative has resulted in the identification of a dedicated Business Climate Coordinator, of corporate, SME and risk experts, and in the establishment of a monthly cross-disciplinary committee. In support of the new system, the Sustainability Department has published technology guides (solar, wind, water, waste, eco-industries in France, biomass and electric vehicles), market summaries (financing, bank competition and legislative environment) and a client brochure.

In addition, in 2010 HSBC France introduced a mobilisation plan to continue the process of greater awareness among management, employees and customers within branches, and to integrate corporate sustainability as a factor contributing to the performance of day-to-day banking relationships. Two branches were chosen to run pilot projects, Borély in Marseille and Mathurins in Paris.

<sup>1</sup> See website [www.hsbc.fr](http://www.hsbc.fr) Corporate Sustainability section.

<sup>2</sup> These sector-specific guides are presented on the website [www.hsbc.fr](http://www.hsbc.fr) in the Corporate Sustainability section.

## Corporate, social and environmental responsibility (continued)

In 2012, an action plan was established for each of the three main areas of the HSBC Group's corporate sustainability policy: sustainable finance, operational environmental efficiency and community investment to positively influence team cohesion and to enhance customer perception.

Following a test carried out in the pilot branches, the staff branch and a few volunteer branches in order to measure the interest of the bank's retail customers, a proposition including an audit of customers' real estate energy performance will be deployed across the network by 2013. This offer has been developed in partnership with the *Bureau Veritas* certification company.

### Growing importance of the social, environmental and governance implications when assessing company performance

Article 225 of the Grenelle 2 law making it compulsory to supply and verify governance, social and environmental information supports a fundamental trend characterised by the growing requirement for asset management firms, including the HSBC Group, to consider the Principles for Responsible Investment, and the growing expectation of investors to include long-term issues when assessing companies' performance. HSBC France supports these expectations through various services and products.

In 2012, HSBC France's cash equity team pursued its monthly events on extra financial issues for their Socially Responsible Investment (SRI) asset manager clients, by presenting external experts who deal with subjects such as the valuation of intangible capital, carbon markets, auditors' interpretations of sustainability reports and measuring the impact of psychosocial risks on companies' financial performance.

In relation to products, 2012 was marked by the performance of Socially Responsible Investment (SRI) products, the continued growth of SRI employee savings and the issue of new SRI bonds.

The HSBC SRI range has been designed to meet the needs of all its customers: institutions, asset managers, multi-manager funds, companies, associations and retail customers. This range is integrated into the HSBC France core range of UCITS products and is also available through the life insurance contracts and employee savings plans offered by HSBC in France.

The HSBC *Actions Développement Durable* fund has seen its assets grow by 47.5 per cent, driven by the confidence of institutional and corporate clients (*via* employee savings plans), but also due to a reorganisation of the UCITS ranges with similar management objectives. The HSBC *Oblig Développement Durable* fund has increased its assets by 84.9 per cent thanks to the confidence of the multi-manager funds, but also through the open and dedicated range of employee savings plans. The HSBC EE *Diversifié Responsable et Solidaire* fund, reserved for employee savings plans, has risen every year since its

inception, moving from EUR 27.7 million to EUR 37.8 million. Although bond, equity and diversified funds recorded growth in 2012, SRI investments recorded an overall decline due to a reduction in money market rates, which resulted in a significant reduction in money market fund assets, to which the SRI Monetary Fund was no exception. Performance levels at the end of 2012 were very satisfactory especially for the HSBC *Oblig Développement Durable* fund, ranked in the Morningstar "EUR Diversified Bond" category 1<sup>st</sup> quartile over 3 months, 6 months, 1 year, 3 years, 5 years and this since its inception in March 2004.

For the fourth consecutive year, HSBC *Actions Développement Durable* fund and HSBC *Oblig Développement Durable* fund received in 2012 the SRI Novethic Label. This label is awarded to Socially Responsible Investment funds (SRI) whose management systematically takes into account environmental, social and governance criteria (ESG)<sup>1</sup>. The participation of HSBC France and HSBC Global Asset Management (France) at the third staging of Socially Responsible Investment Week (from 11 to 20 October 2012) also helped to raise the profile of the HSBC range. During the event, HSBC France offered to waive fees (subscription commissions) for any new subscription to HSBC *Actions Développement Durable* and HSBC *Oblig Développement Durable* funds for a month. The bank also continued its training activities at network level and assured that SRI funds will be promoted to targeted retail clients.

Concerning SRI employee savings plans, total assets in open-ended funds increased from EUR 85.9 million to EUR 150 million<sup>2</sup> as a result of the following promotional campaigns:

- since the merger of the CIPF HSBC EE *Actions Euro* with the HSBC EE *Actions Responsables* product in October 2012, the reference product for euro equities offered to all clients is now a product from the SRI range;
- [www.ere.hsbc.fr](http://www.ere.hsbc.fr) offers a dedicated space to SRI which is regularly updated, as is the documentation it contains;
- the Inter-Trade Union Committee on Employee Savings Plans (*Comité Intersyndical de l'Épargne Salariale* – CIES) has also renewed its label for the SRI savings plan product range which includes four sub-funds: HSBC EE *Actions Responsables*, HSBC EE *Diversifié Responsable et Solidaire*, HSBC EE *Obligations Responsables* and HSBC EE *Monétaire Etat*.

Concerning bond issues, HSBC France was lead arranger for a bond of EUR 43 million with a 10-year maturity based on socially responsible investments issued by a French region. Furthermore, HSBC's expertise in the field and its ESG rating enabled it to lead the first SRI corporate bond issue.

<sup>1</sup> More information at [www.novethic.fr](http://www.novethic.fr).

<sup>2</sup> The outstanding amount of the CIPF dedicated to a company or a group of companies is excluded.

### **Development of social entrepreneurship and of a social and solidarity-based economy**

The socially responsible company puts people and social impact at the heart of its business project. It finds itself at the crossroads of three main movements, namely the social and solidarity-based economy, the concept of the social business (understood to be a self-financing, non-loss and non-dividend company designed to address a social objective) and the commoditisation of social action (and, in particular, the transition from a mode of operation based on grants to a mode of operation by calls for projects). HSBC has a role to play in its development in the service of greater social equity.

At HSBC France 51 experts, associations, institutional and para-institutional entities are responsible for supporting existing and potential clients who are active in these areas. More mergers, understandings between organisations and the need for international services for a proportion of clients are anticipated in the future.

In terms of microfinance, HSBC France support for the Adie association (*Association pour le droit à l'initiative économique*), initiated in 2007, continues with an annual credit line of EUR 2 million, which has enabled 247 *microentrepreneurs* to launch their businesses and 346 people in a state of insecurity to return to work through personal microcredits.

To complete its commitment, HSBC France has had a stake, since 2008, in the *FinanCités* venture capital fund amounting to EUR 1 million and in *Business Angels des Cités*, since 2010, amounting to EUR 500,000. Late 2011, HSBC France made a new commitment with a participation of EUR 1 million in the independent venture capital fund Citizen Capital. This fund finances growing SMEs equity capital located or created by entrepreneurs from disadvantaged areas, and supports them in their projects.

Solidarity investments of the HSBC EE *Diversifié Responsable et Solidaire* fund were allocated as follows in 2012: EUR 308,700 to SIFA, EUR 350,000 to Adie and EUR 1,325,000 to *Habitat et Humanisme*, an increase of 9 per cent over 2011.

In 2012, Private Banking continued its approach initiated in 2011 of developing its range of philanthropic services. HSBC makes its partners and its contacts available to its Private Banking clients, alongside its banking network, expertise and the experience and knowledge of its employees to support its customers in their philanthropic initiatives and to help them to build or develop their projects. Within the context of this support, the bank offers its clients the possibility of participating in the *Rencontres des Philanthropes* sessions, an exclusive and discreet circle, during which they can exchange views and attend bi-monthly thematic meetings led by a philanthropist and an expert. In 2012, five meetings were held during a luncheon at the Group's head office in France.

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### **Operational environmental efficiency**

#### **2012-2020 Objectives**

In order to contribute to the commitment of the HSBC Group to reduce CO<sub>2</sub> emissions by 1 tonne per employee and per year by 2020, HSBC France focuses its attention around four objectives:

- improving its energy efficiency;
- reducing CO<sub>2</sub> emissions, notably those related to business travel;
- reducing paper consumption;
- reducing its production of non-recycled waste.

#### **Improving energy efficiency - sustainable use of resources**

In 2012, action focused on building renovations, floor space optimisation, promoting teleworking, an environmental schedule for all new leases or lease renewals, maintaining the *Attestation de Qualité Environnementale d'Utilisation* (environmental quality certification for building usage – high-performance level) for the *Cœur Défense* building, issued in April 2011 by Certivea. Through this initiative, HSBC France has signed a commitment with the owner and the manager of the building to participate in the effort to control its environmental footprint in these premises. HSBC France was one of the first of the occupant companies to obtain this distinction.

#### **Greenhouse gases and carbon footprint**

In France, Decree no. 2011-829 of 11 July 2011, relating to greenhouse gas emission footprints (BEGES) and the local climate energy plan, was issued. To meet these regulatory requirements, HSBC France brought its reporting standards into compliance.

The BEGES report determines the environmental footprint according to a recognised methodology and applies to companies with more than 500 employees. This exercise will enable HSBC France to make comparisons and will serve as a benchmark in its action plans. The main sources of CO<sub>2</sub> emissions of HSBC France are those related to energy consumption and transportation.

HSBC France's greenhouse gas emission footprint is available on its website<sup>1</sup>.

#### **Reducing CO<sub>2</sub> emissions related to business travel**

In 2012, the focus of action was the rationalisation of the fleet of vehicles with the reduction of their average carbon weight, the establishment of a new circular on business expense reimbursement and the participation of HSBC France in the *Défense Seine Arche* inter-business travel plan for three central sites (*Cœur Défense*, *Crystal* and *Ile-de-France*). The inter-business travel plan meets the legal obligations and affects 4,100 HSBC France employees.

<sup>1</sup> See [www.hsbc.fr](http://www.hsbc.fr) Corporate Sustainability section.

## Corporate, social and environmental responsibility (continued)

### Pollution and waste management

#### *Reducing production of non-recycled waste*

Individual garbage cans have been removed and collective selective sorting bins have been installed in the Cœur Défense and Crystal buildings. The rate of waste recycling has improved significantly.

#### *Reducing paper consumption and improving recycling*

Several major paperless office projects are underway across the HSBC Group. In addition, within the context of the Sustainable Development Pilot, action plans designed to reduce paper consumption at the branches have been examined.

### Protection of biodiversity

Through its environmental philanthropic programmes (see section “Employees’ commitment by awareness and philanthropy”), the implementation of the Equator Principles and environmental and social risk management procedures in its credit activities and project finance (see section “Integration of corporate sustainability in business lines”), the HSBC Group, including HSBC France, contributes to the protection of biodiversity.

### Resources allocated to the prevention of environmental and pollution risks – Measures of prevention, reduction or repair of emissions into the atmosphere, soil and water that may severely affect the environment – Taking into account of noise and any other form of pollution specific to a business – Land use

The activity conducted presents no risk of this type other than those associated with financial activities, which are undertaken in managing environmental impacts as stipulated in the section “Risk management related to the impact of climate change”.

Valeurs Mobilières Elysées (formerly known as Nobel), a wholly-owned subsidiary of HSBC France acquired in 1986, was initially a manufacturing company that ended its manufacturing activities in 1965. Pursuant to a prefectural order, Valeurs Mobilières Elysées has measured, for several years, the quality of groundwater in the area in which it conducted its manufacturing activities. The observations for 2012, carried out at the three remaining facilities under the control of a qualified technical expert, are in line with those for previous years and confirm that the quality of groundwater is satisfactory, with concentrations below the required amounts for all parameters concerned.

### Financial Risk

Given its business sector, HSBC France has no provision or guarantee regarding environmental risks.

## Employee Support

The data below is supplied in accordance with article R. 225-105-1 of the French Commercial Code for the application of article L. 225-102-1 paragraph 5 of the aforementioned Code.

### The workforce on 31 December 2012 and changes since 2011

#### Workforce enrolled

|  | 2012         | 2011 <sup>1</sup> | 2010 <sup>2</sup> | 2009 <sup>3</sup> | 2008 <sup>4</sup> |
|--|--------------|-------------------|-------------------|-------------------|-------------------|
| Total HSBC France group .....            | <b>9,851</b> | 10,335            | 10,479            | 10,677            | 11,227            |
| of which HSBC France .....               | <b>9,424</b> | 9,860             | 9,706             | 9,748             | 10,218            |
| of which subsidiaries and branches ..... | <b>427</b>   | 475               | 773               | 929               | 1,009             |

#### Personnel full-time equivalents

|  | 2012         | 2011 <sup>1</sup> | 2010 <sup>2</sup> | 2009 <sup>3</sup> | 2008 <sup>4</sup> |
|--|--------------|-------------------|-------------------|-------------------|-------------------|
| Total HSBC France group .....            | <b>9,570</b> | 10,030            | 10,121            | 10,350            | 10,886            |
| of which HSBC France .....               | <b>9,152</b> | 9,564             | 9,365             | 9,435             | 9,892             |
| of which subsidiaries and branches ..... | <b>418</b>   | 466               | 756               | 915               | 994               |

1 2011 was marked by the incorporation of HSBC Private Bank France within HSBC France (via a legal merger).

2 2010 was marked by the divestiture of its fund valuation activity (HSBC Securities Services (France)) to CACEIS.

3 2009 was marked by the integration of most of the employees of HSBC Financial Products (France) into HSBC Bank plc. Paris Branch, which is outside the perimeter mentioned above.

4 2008 was marked by two main events: the disposal by HSBC France of its seven regional banking subsidiaries and the legal merger of four banking subsidiaries (HSBC Herve, HSBC de Baecque Beau, HSBC UBP and HSBC Picardie) with HSBC France.

#### The HSBC France workforce contracted in 2012

This decrease is primarily a result of retirements and employee resignations.

548 new employees were hired in 2012 (including mobility within the Group), including 215 recruitments with permanent contracts, 333 fixed-term contracts, including 113 youth apprenticeships (fixed-term training contracts).

923 employees left the company, the end of their fixed-term contracts representing 40 per cent of this total, with 21 per cent resignations and 23 per cent retirements.

The structure of the workforce has stabilised. The proportion of management staff remains identical to that at the end of 2011 at 68 per cent; the percentage of women in this category remained stable at 48 per cent.

On 31 December 2012, 1,025 employees worked under the voluntary part-time work agreement or a little more than 11 per cent of the registered employees.

Finally, HSBC France employed 310 staff with disabilities at the end of 2012.

#### Remuneration and incentive schemes

##### Salaries and salary developments

In 2012 for the year 2013, in the absence of an agreement, management unilaterally decided to implement just one measure. This measure involved setting aside a financial package to enable individual increases in the following situations:

- to promote professional equality between men and women (pay and career equality), as well as fairness between full-time employees and part-time employees;

- for employees having benefited from long-term maternity leave, adoption leave or parental education leave;
- for the review and possible revision of remuneration of employees with disabilities;
- for the review and possible revision of the remuneration of employees over 50 years old not having benefited from a selective increase in salary over the last five years (from 2008 to 2012);
- for the review and possible revision of the remuneration of staff representatives, in application of the agreement of 30 October 2007 on the exercise of the right to organise within HSBC France.

In addition, a salary revision package and a variable package are made available to managers in order to review individual employee situations in application of the salary revision remuneration policy, and to grant bonuses based on individual performance both on a qualitative and quantitative basis.

##### Collective incentive schemes

A new compulsory and optional profit-sharing plan was the subject of negotiation in 2012 and agreements were signed on 27 June 2012. It now includes a profit-sharing agreement based on the legal formula and an incentive agreement for employees linked to the results of the company, with an overall ceiling. The agreements covering a period of three years apply to 2012, 2013 and 2014.

- Compulsory company profit-sharing agreement  
HSBC France's special compulsory profit-sharing reserve is calculated according to the statutory formula.

## Corporate, social and environmental responsibility (continued)

- Optional company profit-sharing agreement  
HSBC France's optional incentive plan is based on a financial indicator, pre-tax net income, with a distribution rate in increments of EUR 75 million, with three multiplier coefficients: improved equity yield, water consumption reduction and energy consumption reduction. These three factors can increase by up to 12 per cent the amount of incentive paid.

A global compulsory and optional profit-sharing ceiling has been set as follows: the sum of the special compulsory profit-sharing reserve is calculated according to the statutory formula and the optional incentive reserve is capped at 8.75 per cent of HSBC France's gross payroll, which will be the basis for social security contributions as defined in the annual declaration of wages, and not including any variable remuneration. The amount of the special compulsory profit-sharing reserve calculated according to the legal formula and as foreseen in the compulsory profit-sharing agreement cannot be reduced through this cap, and where applicable only the amount of the optional incentive can be decreased.

- Agreement on the exceptional measure for 2012  
HSBC France decided to take into account the special situation of employees on the lowest wages by proposing an agreement allowing for an exceptional bonus. The agreement was signed on 27 June 2012. A bonus of a gross amount of EUR 550 was paid in July 2012 to employees whose gross annual salary was strictly less than EUR 33,000 and with at least six months' employment in 2011 and still working for the company in July 2012. In total, nearly 2,500 employees benefited from this, at a total cost of EUR 1.4 million.

- Collective agreement on the HSBC France company savings plan

The agreement signed in 2008 offers all HSBC France employees a new employee savings plan, effective 1 January 2009.

Employee payments into the company savings plan and its long-term PERF (future retirement savings plan) receive a contribution of the following amounts:

- the contribution amount paid by the company into the company savings plan can reach EUR 1,800 per year;
- the contribution amount paid by the company in the future retirement savings plan can reach EUR 624 per year;
- accordingly, the company's contribution may reach a maximum of EUR 2,424 per year.

In addition, HSBC France wished to further diversify the choice of funds that are available to employees in the company savings plan. On this occasion, HSBC France also expanded the amount of funds related to socially responsible investments (SRIs). An agreement was therefore signed on 7 September 2012, to offer six new funds to employees, including two socially responsible funds, HSBC EE *Obligations Responsables* and HSBC EE *Actions Responsables*. These two SRI funds take into account governance, corporate, environmental and social

criteria, the pillars of corporate sustainability, in addition to the normal financial criteria.

- HSBC Holdings plc options and shares  
With effect from 2001 and following the merger of CCF (Credit Commercial de France) within the HSBC Group, CCF decided to no longer assign CCF options to its employees, insofar as they could participate in the stock-option and share purchase plan of HSBC Holdings Group (B shares) as part of a French sub-plan compliant with French legislation and tax rules.

Within this context, a number of HSBC France group employees benefited from the allocation of HSBC Holdings plc stock-options from 2001 to 2005.

In 2005, HSBC Group fundamentally revised its employee option and free share policy and implemented the HSBC Share Plan, approved by the General Assembly of May 2005. This regulation provides for the establishment of a French sub-plan (Schedule 5 of the general regulations), which complies with French legislation and tax rules.

This regulation was revised in 2011 in order to take into account amendments to regulations impacting the plan and to formalise the rules of the "Group Performance Share Plan" aimed at Executives of the Group. Within this context, the French sub-plan (Schedule 5 of the new regulations) was also the subject of a review to comply with local social and tax rules.

The objective of the HSBC Share Plan is to motivate executives to create shareholder value and to distinguish individual performance and potential. Allotments are also granted under this plan for the purposes of recruitment and retention of employees. From 2006 onwards, the general policy of the HSBC Group is to no longer grant stock options (except when required by a country's legal and tax rules) but to give priority to the allocation of free shares.

The Group now recognises two categories of free shares:

- the "Group Performance Shares" which have specific conditions defined below:
  - a five year vesting period,
  - a restricted period beyond the vesting period, which runs until retirement,
  - a condition of performance measured using eight indicators (four financial and four non-financial) from the performance scorecard of the manager concerned;
- the "Restricted Shares" that are not subject to specific performance conditions, but which are definitively owned by the employees remaining in the Group at the end of a period of one, two or three years.

### Capital increase reserved for HSBC France group employees (hereafter referred to as the "group")

In 2012, an HSBC Holdings plc share issue was proposed, reserved for employees, former employees still participating in the company savings plan, and employees of French subsidiaries in which HSBC Holdings plc owned more than 51 per cent.



HSBC France group employees with at least three months' service were entitled to subscribe to this new issue by investing:

- a tax-free payment, with an individual minimum of EUR 100 and an individual maximum of EUR 5,250, and in all circumstances within the limits of the legal ceiling (annual payments in the company savings plan may not exceed 25 per cent of gross annual remuneration);
- for HSBC France, the application of the calculation rules laid down by the profit-sharing agreements resulted to nil in 2012 in respect of the 2011 financial year, preventing subscriptions to this issue *via* either compulsory or optional profit-sharing;
- conversely, for subsidiaries, insofar as the agreements provide for compulsory or optional profit-sharing, employees of these entities had been able to subscribe to this transaction by investing the amount of the compulsory profit-sharing and any optional profit-sharing.

This transaction was conducted in the following manner:

- subscription period: between 4 October and 24 October 2012;
- subscription price in euros: the subscription price per share has been determined on the basis of the average price of HSBC Holdings plc shares over the twenty London Stock Exchange sessions that preceded 26 September 2012, the decision date of the Remuneration Committee of HSBC Holdings plc. The subscription price was EUR 5.6950;
- investment options: a single investment option was offered to employees to acquire HSBC Holdings plc shares with a 20 per cent discount, with a minimum of EUR 100 and a maximum investment of EUR 5,250 through a voluntary payment, and for the employees of subsidiaries only, through compulsory or optional profit-sharing, where applicable;
- cap: the total number of shares employees may subscribe could not exceed 4,000,000 HSBC Holdings plc shares. If this threshold is exceeded, a proportional reduction would apply starting with voluntary contributions.

This issue was subscribed for 2,274,523 HSBC Holdings plc shares, representing a total of EUR 12.9 million.

#### **Social Fund**

The consolidated amount of payments to the Works Committees and the Central Works Council, based on a percentage of the payroll, was EUR 3.5 million in 2012.

HSBC France pays into the HSBC France Employee Social Mutual Fund an amount equal to 0.05 per cent of the HSBC France base salaries. A Joint Committee to monitor the scheme defines the social fund's action policy and decides on the aid granted by this means to employees. The social fund may in particular provide financial support through the payment of healthcare costs for single-parent families weakened by their situation.

HSBC France also spent EUR 10.4 million in 2012 on socially-oriented payments (housing, back-to-school payments, transportation, childcare, parental allowances, long-service programmes and HSBC France employment medals).

#### **Work Organisation**

##### *Organisation of working hours*

Pursuant to the agreement on working hours, signed in October 2008, the annual employee work duration is 1,592 hours, excluding the paid solidarity day.

For employees whose working hours are recorded, working time shall be organised in two possible ways:

- on a weekly basis of 38 hours, or 7 hours 36 minutes daily, based on a 5-day working week. The number of RTT (reduction in working hours) days in 2012 was 17.5 days for a week worked Monday to Friday, and 18.5 days for a week worked from Tuesday to Saturday;
- on a weekly basis of 37 hours, or 7 hours 24 minutes daily, based on a 4.5-day working week. The number of RTT (reduction in working hours) days in 2012 was 12 days for a week worked Monday to Friday, and 12 days for a week worked from Tuesday to Saturday.

Management working on a total number of days basis are executives who hold a position involving a significant amount of autonomy in their time management, and whose foremost occupation is to coordinate and lead a team and/or whose mission requires a high level of expertise in their profession.

Rights to reduction in working hours (RTT) for employees working a fixed number of days annually vary, as for executives, according to their working pattern for the week.

##### *Overtime*

88,000 overtime hours were clocked by HSBC France employees in 2012, down 1 per cent from 2011. This percentage is in line with changes to the average workforce during 2012 compared with 2011.

Work performed in excess of the regulated hours relates mainly to the hours worked under the agreement relating to exceptional work, the volume of which increased by 5 per cent compared to 2011.

##### *Absenteeism*

In 2012, maternity leave was slightly higher than in 2011, after appointments made in recent years resulted in an increased number of women and younger people in the workforce. Absenteeism due to illness is slightly up compared to the previous year.

## Corporate, social and environmental responsibility (continued)

### Health and Safety

#### *Hygiene and Safety*

HSBC France has Health, Safety and Working Conditions Committees (CHSCTs) for all its activities in France.

These CHSCT committees have greater resources than those provided for by law, particularly in relation to visits to establishments and the number of representatives.

Pre-election agreements relating to the Works Committees/Employee representatives elections for 2013 strengthen the capacity of the CHSCTs, especially the number of representatives.

In 2012, the CHSCTs continued their involvement in the moves being implemented at central sites to bring together teams in the same business line, those concerning branch renovations and improvements as well as supporting reorganisations relating to employee working conditions.

#### *Stress Observatory*

Since 2004, HSBC France has suggested that employees in the Paris region answer the Stress Medical Observatory questionnaire during their periodic medical examination. In 2010, this provision was extended to employees in the provinces. The processing of the collected data using a scientific methodology has been entrusted to an independent firm with the IPRP (expert in occupational risk prevention) qualification covering the prevention of work-related risks.

2011 results showed the continuation of a slight decrease in stress levels already noted within the company in 2010. Groups expressing less favourable psychological experiences are identified among staff of 50 years of age and over, women, bank network employees, business line technicians processing banking transactions and people with more than 120 minutes of daily travel.

These surveys helped to identify factual elements and then to implement action plans to heighten awareness about stress factors and to reduce them through targeted action, particularly in terms of workload, work organisation, ergonomics, special support during organisational changes and suitable training that takes into account developments in the business.

#### *Psycho-social risk prevention framework*

A joint Steering Committee involving management, unions, CHSCT representatives, the Occupational Health Service and the Stress Medical Observatory entrusted the firm Technologia, an independent expert, to conduct a study into the working conditions of HSBC France group employees.

This approach has helped to map out psycho-social risk factors.

Among the factors felt as having the most impact on the quality of life at work were questions of requirements related to the sheer weight of processes and computer systems, those concerning the vision of the future or recognition in the workplace were also expressed. Conversely, the quality of local working arrangements was highly valued by a majority and emerges as a factor in reducing risks.

The Steering Committee is working on the basis of this study and in consultation with management and the CHSCT to create the necessary action plans to improve working conditions by prioritising the most affected occupations and the most significant risk factors.

#### *Work-related accidents, including their frequency and severity, as well as occupational diseases*

Occupational diseases concern only a very small percentage of employees, in any case, statistically insignificant. The frequency and severity rates of work-related accidents in 2012 are shown in the table of sustainability performance indicators of the HSBC Group in France.

#### *Professional/personal life balance*

In late 2010, HSBC France introduced a teleworking system which enables employees, if their functions allow it, to perform part of their activity from home. This arrangement is on a voluntary basis and uses the principle of alternating throughout the same week between one to three days of teleworking and a minimum of two consecutive days of work in the company.

As of 31 December 2012, 498 employees, primarily in support functions, have opted for this solution widely implemented within the HSBC Group, and their average level of satisfaction is high.

Teleworking significantly reduces weekly travel time, which helps to reduce the company's carbon footprint and allows employees to better combine work and personal life.

Furthermore, in October 2012, the bank's Senior Management sent a message to all executives in order to improve the spread of good managerial practices, especially with regards to patterns of work: except in exceptional circumstances or crisis situations, employees must not be contacted during their holidays, weekends or outside of working hours, and except in emergencies, meetings must not be scheduled before 9 a.m. or after 6 p.m.

### Training

Developing skills to provide a better service to clients is HSBC's strategy for a market that is becoming increasingly competitive, regulated and undergoing continuous change.

Beyond HSBC France's continued attachment to offering training courses in its main professions, 2012 was marked by a net rise in the volume of training courses to support company reorganisations within the context of the 2012-2014 Strategic Plan.

The 2012 training plan was structured according to this logic. By making courses available that are well suited to Retail Banking and Wealth Management personnel (sales representatives, Advance advisors, *Premier* advisors, *Premier Patrimoniaux* Advisors), the year 2012 presented itself as a turning point in the reorganisation of the retail banking business and has involved almost 800 employees in training courses leading to qualifications.

These courses constitute one of the fundamental strategic plan initiatives, namely to give everyone the opportunity to gain the level of competence and expertise necessary for their development. Some of these courses alternate theoretical training with practical training (field experience). The strong commitment of managers and employees in these training programmes produced very good results in terms of team qualifications.

At the same time, Commercial Banking is committed to developing expertise in association with the development of its international strategy (advanced training in Trade Finance, risk management, etc.) and to supporting the introduction of new remote banking services (Customer Transaction Services, Business Commercial Assistance Centre).

Finally, support functions and in particular HSBC Technology and Services (HTS) have developed training courses to develop both the expertise of their IT and organisation teams (project management, English) and courses with qualifications to enhance the versatility of the back office teams (banking transaction fundamentals).

Within the context of substantial changes to all skills and a strengthening of the global function lines, the role of manager is now even more critical. To this end, the training effort already commenced during 2011 has intensified with the continuation of the managerial training course (placing managers at the heart of the relationship) and with the introduction of new training courses covering change management, and finally with the establishment under the strategic plan of training dedicated to supporting employees in their professional development.

Within the context of these multiple changes, a catalogue of new “training courses for everyone” has been published to support these efforts and is aimed at all employees of HSBC France, covering the following topics: change management, communication, and personal, interpersonal and professional skills development.

Additional programmes have also been implemented in certain business lines such as Global Banking and Markets to provide roadmaps allowing employees to better identify their skill development opportunities and to ensure they receive appropriate training.

Regarding Performance Management, HSBC has introduced a global programme intended as much for managers as for staff and which includes six e-learning modules and four modules in face-to-face sessions to help employees develop their performance.

The organisation of these actions within the framework put in place over previous years enables employees to register independently (with the agreement of their managers for face-to-face training) for the desired modules and also receive invitations to key training sessions such as regulatory and mandatory training, new entrants’ integration programmes and key actions identified by the business lines (e.g.: training in new EDRAS sales methods for those in Wealth Management).

A particular effort has been made to assist employees increasingly exposed to international contexts, to enable them to quickly and sustainably develop their language skills. This support was extended in 2012 to new categories of employees and *via* more diversified systems such as intensive immersion.

All these training methods are aligned with Group values “Open, Connected and Reliable” and are intended to disseminate the behavioural practice “Acting with courageous integrity”.

To give more clarity to all of these training systems and to facilitate access to all students, an electronic catalogue is accessible on the HSBC France Intranet.

#### **Diversity and equality of treatment**

In 2012, HSBC France continued the implementation of its action plan focused on women’s careers, to promote women’s access to positions at the highest level of the company. This priority is shared by the HSBC Group, which has deployed it worldwide. Specific development paths for “talented women” were introduced in 2012. The objective is to promote the progress of female colleagues to the highest level. In addition, HSBC France has continued to place emphasis on better detection of women during talent reviews and when developing succession plans.

As of 31 December 2012, six women sat on the HSBC France Executive Committee, and women accounted for 48 per cent of executives and 34 per cent of point-of-sale Directors (Branches, Corporate Business Centres and Corporate Banking Centres).

The global corporate agreement on Diversity and Equity signed by unions and management in 2011 was implemented in 2012. The objectives of the bank are to promote equity between men and women with regard to career and remuneration, to improve paternity leave and the career of employees with disabilities, and to increase the proportion of women in classification levels where they are underrepresented. In this regard, the bank is committed to advancing the proportion of women in each level of the executive classification by four points in three years. And to better identify and combat gender discrimination in the development of careers and remuneration, two diagnostic approaches supported by both unions and management have been implemented. One concerns careers and is to monitor promotion indicators for men and women over several years. The other deals with remuneration, and reflects the attention given to wage equity. In fact, since 2004, the bank

## Corporate, social and environmental responsibility (continued)

has spent EUR 5.9 million in this area. Over the past four years, nearly 2,900 women have received a pay adjustment in respect of wage equality. The same wage equality diagnosis is made for social partners, people with disabilities and employees over 50 years of age.

### Seniors

Within the framework of the agreement signed in 2009 to promote the retention of senior employees over the age of 45, HSBC France offers these employees, notably those in their forty-fifth year, the benefits of a career review with their head of human resources. In 2012, 412 people received an invitation to this type of consultation.

### Fight against discrimination

HSBC values meritocracy. At the same level of competence and performance, everyone has the same chances of being hired and progressing throughout the company, regardless of their ethnic and social origins. In 2012, HSBC France launched an internal communication campaign about non-discrimination, through posters and totems placed at head office thoroughfares and in branches. At the same time, compulsory e-learning training for managers continued in 2012. In November 2012, a non-compulsory awareness training for all employees was launched. It aims to make them aware of the seriousness of stereotypes and prejudice with which we view others as well as within the context of individual actions and decisions. The awareness campaign and training programme focus on different possible causes of discrimination: ethnic origin, sex, family status, sexual orientation, age, disability, or one's way of working (teleworking or not).

At the same time, HSBC France conducted a "summer assistant" operation in connection with its partner associations working for equal opportunities: *IMS-Entreprendre pour la Cité*, *Mosaik-RH*, *Le relais-Sciences Po* and *Tremplin*. This approach aims to promote the diversity of origin of applicants for summer assistant posts, and to facilitate their access to students of universities in the Paris suburbs. The associations sent 115 candidate applications to the bank with five coming from students with disabilities. These candidates, all of whom were selected, were offered a summer job lasting between one and four months.

### Disability

As of 31 December 2012, HSBC France had 313 employees with disabilities. In 2012, 18 employees declared their disability to the company. HSBC France's disability policy is based on the renewal in July 2011 of the company agreement. It consists of three components:

- maintaining employment: each situation is handled on a case-by-case basis. In 2012, the bank made 30 work station improvements to make the working life of employees with disabilities easier, including the introduction of the TADEO service (telephony solution for the deaf) for seven employees. In addition, sign language courses have been intensified and four employees have benefited from financial support (hearing aids, wheelchair, etc.);
  - recruitment: HSBC France, which works with associations such as *Handiformabanque*, *Tremplin* and specialist firms, participated in two recruitment forums. In 2012, three people were recruited on permanent contracts and two on fixed-term contracts. In the previous agreement, the bank set the objective of hiring ten new staff members over the period (three years). This target was exceeded in 2011. In the new agreement, HSBC France is committed to hiring a minimum of ten new permanent-contract staff and ten apprenticeships;
  - daily life: in 2012, disabled employees or the family of a handicapped worker who received CESU Handicap tickets (cheques covering personal services: household tasks, childcare, sign language translation, etc.) financed by the bank numbered 325 people (+20 per cent). The CESU ticket was upgraded by EUR 25. In addition, extra days off are granted to employees with disabilities or those with a disabled close family member.
- To better inform people about disability, the bank held four awareness sessions for network managers on the theme "What is disability?", as well as an educational quiz on the subject offered to all employees. 600 staff members participated. Finally, 3,000 copies of a booklet "What is Disability" have been printed and distributed to the Occupational Health Service and to the regions.

### Fundamental conventions of the International Labour Organisation

HSBC France promotes and complies with the provisions of the fundamental conventions of the ILO concerning respect for freedom of association and the right to collective bargaining, and the elimination of discrimination in respect to employment and occupation. Furthermore, within the context of the Group's commitment to the United Nations Global Pact, HSBC France is fully compliant.

### Employees' commitment by awareness and philanthropy

In 2012, HSBC France committed nearly EUR 2.6 million to donations. The HSBC France group's employees completed 2,032 voluntary assignments, representing nearly 12,000 hours, including 75 per cent performed during working time.

The year 2012 was marked by:

- assistance given by the *Fondation HSBC pour l'Education*, which is continuing its work for the seventh consecutive year. In its 2012 call for projects, the Foundation again wished to support associations connected with schools. In total, 32 associations were supported, with seven new projects. Between June 2011 and June 2012, 8,900 children benefited from the support of the Foundation;
- the launch by the Group of the "HSBC Water Programme" (2012-2016) (see: "HSBC Group Corporate Sustainability strategy – Community investment".) To accompany the launch in France, a website entitled "*les défis Ecol'Eau*" was created

- calling on the imagination of employees to find ways of reducing their water consumption at home or at work. In 2013, employees in France will be invited to follow training sessions related to water issues and to participate in field activities;
- the continuation of environmental sponsorship activities launched in November 2010 by HSBC France centred around three objectives:
    - to educate the young about environmental protection through two programmes: Climate Initiative, with the *Fondation pour l'Education à l'Environnement en Europe* (FEEE), and the *Maud Fontenoy Fondation*,
    - to promote and organise on-site ecological activities involving employees and customers. In 2012, 26 teams participated in nature projects with the NFB, totalling more than 550 employees,
    - to support research into the impact of climate change on the financial industry: the Carbon Finance Chair and the SRI Chair;
  - the success of volunteering as a driving force behind team building, a managerial initiative launched in 2009. In 2012, 43 teams, more than 700 employees and at least 85 points of sale out of 385 (approximately 22 per cent) were involved in suggested activities or those that were custom-designed by the Sustainability Department.

## Corporate, social and environmental responsibility (continued)

### Methodological details on corporate, social and environmental information

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#### Introduction

In 2012, the HSBC France group had chosen KPMG to verify a selection of non-financial indicators identified by the symbol  in the tables shown on pages 70 and 71 of this Registration Document. The nature and conclusions of the tasks undertaken are shown in the examination report on pages 72 to 74.

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#### Scope of reporting

The scope of each indicator is shown in the table of sustainability performance indicators of the HSBC Group in France. The scope may vary depending on the availability of data or type of indicator.

Thus, corporate indicators concern the HSBC Group in France (excluding HSBC Assurances Vie (France) and HSBC Bank plc Paris Branch) or HSBC France, whereas environmental indicators concern the HSBC Group in France or HSBC France. The social indicators relating to “Company saving schemes: total assets of the SRI (Socially Responsible Investment) range” and to “Investment of the company savings fund HSBC EE *Diversifié Responsable et Solidaire* fund for the benefit of solidarity-based companies” are communicated within the scope of HSBC Global Asset Management (France).

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#### Change in scope

For environmental indicators, entities consolidated or deconsolidated during the year are accounted for in the data reported on the date they enter the Group and until the date they exit.

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#### Reporting period

The annual reporting period is the calendar year (from 1 January to 31 December).

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#### Reporting tools and processes

##### For environmental indicators

The reporting tool is that which is used by the HSBC Group, that is, Metrix, developed by Enablon. Its main functions include the collection of energy data (kWh) and CO<sub>2</sub> emissions, water (m<sup>3</sup>), paper (tonnes), waste (tonnes), km travelled and CO<sub>2</sub> emissions, collection of other data: comments, operational surface areas (m<sup>2</sup>), number of sites, workforce (FTE), initiatives, dual validation at country level, then at regional and global levels and, finally, dashboards.

##### For social indicators

The reporting tool is that which is used by the HSBC Group, that is, Peoplesoft.

##### For economic data

The reported data are monitored with the dedicated management software Apollo.

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#### Details on the definition of certain indicators

##### Environmental indicators

CO<sub>2</sub> emissions resulting from the consumption of electricity, gas, fuel oil, urban heating and air conditioning.

CO<sub>2</sub> emissions associated with transport correspond to journeys made by train and plane (which are purchased through travel agencies), by taxi, through car hire or group car fleet.

**Social indicators**

The total workforce comprises employees under permanent and fixed-term employment contracts. Internship, temporary and suspended contracts, employees taking early retirement, employees on long-term sick leave, permanently disabled employees and expatriates are included. Holiday auxiliary staff are excluded.

Hires and lay-offs include employees under permanent and fixed-term employment contracts. More than one hire will be recorded for a person hired more than once under a fixed-term contract during the reporting period. Likewise, an employee whose contract changes from a permanent to a fixed-term contract will be recorded as a hire.

The number of employees who work from home include those having signed an endorsement to their contract enabling them to work from home.

**Societal indicators**

Concerning the “Investment of the company savings fund HSBC EE *Diversifié Responsable et Solidaire* fund for the benefit of solidarity-based companies” indicator, the companies considered as solidarity-based are those having received “solidarity-based” approval from the prefecture or those with related solidarity-based status, *i.e.* those whose assets constitute at least 35 per cent of securities issued by solidarity-based companies.

Corporate, social and environmental responsibility (continued)

Table of sustainability performance indicators of the HSBC Group in France

| Indicator  | Change                    |                           |                         | Reference documents            |                                       |               |                           |
|--|---------------------------|---------------------------|-------------------------|--------------------------------|---------------------------------------|---------------|---------------------------|
|  | 2012                      | 2011                      | 2010                    | Scope*                         | GRI3                                  | ISO 26000     | Global Compact            |
| 1 Pre-tax earnings   | 559                       | 191                       | 628                     | EURm                           | HSBC in France                        |               |                           |
| Total shareholders' equity   | 5,213                     | 4,820                     | 4,832                   | EURm                           | HSBC France group                     |               |                           |
| Operating ratio  | 72                        | 85                        | 71                      | %                              | HSBC in France                        |               |                           |
| Core Tier 1 Ratio (Basel II)   | 12.6                      | 10.7                      | 12.1                    | %                              | HSBC France group                     |               |                           |
| <b>Sustainable Economy</b>   |                           |                           |                         |                                |                                       |               |                           |
| 2 Amount of loans granted to SMEs (European definition)  | 556.7                     | 714.3                     | 907                     | Total loans outstanding (EURm) | HSBC France                           | FS 6          |                           |
| <b>3 Equator principles – Category A</b>   |                           |                           |                         |                                |                                       |               |                           |
| - number of projects financed and their value  | 0 and 0                   | 0 and 0                   | 0 and 0                 | Total number of loans and EURm | HSBC in France                        | FS 3          | 6.3.5 ; 6.6.3 Principle 2 |
| <b>Equator principles – Category B</b>   |                           |                           |                         |                                |                                       |               |                           |
| - number of projects financed and their value  | 0 and 0                   | 1 and 100                 | 2 and 132               | Total number of loans and EURm | HSBC in France                        |               |                           |
| <b>Equator principles – Category C</b>   |                           |                           |                         |                                |                                       |               |                           |
| - number of projects financed and their value  | 1 and 128                 | 1 and 100                 | 3 and 215               | Total number of loans and EURm | HSBC in France                        |               |                           |
| Consultancy  | 3                         | 3                         | 4                       | Number                         | HSBC in France                        |               |                           |
| <b>4 Lines of credit allocated to Adie</b>   |                           |                           |                         |                                |                                       |               |                           |
|  | 2                         | 2                         | 3                       | EURm                           | HSBC France                           | FS 7          |                           |
|  |                           |                           |                         | Total loans outstanding (EURm) |                                       |               |                           |
| Amount of microfinance loans made via ADIE partnership   | 1,570                     | 0,590                     | 1,948                   | EURm                           | N/A                                   | FS 7          |                           |
| Number of microcredits disbursed (Adie)  | 593                       | 257                       | 770                     | Number                         | N/A                                   | FS 7          |                           |
| 5 SRI assets under management  | 825                       | 2,123                     | 1,846                   | EURm                           | HSBC Global Asset Management (France) | FS 10, 11, 12 |                           |
| Company saving schemes: total assets of the SRI range  | 150                       | 85.9                      | 79.5                    | EURm                           | HSBC Global Asset Management (France) |               |                           |
| <b>6 Investment of the company savings fund</b>  |                           |                           |                         |                                |                                       |               |                           |
| HSBC EE <i>Diversifié Responsable et Solidaire</i> fund for the benefit of solidarity-based companies  | 1,984                     | 1,829                     | 1,159                   | EURk                           | HSBC Global Asset Management (France) | FS 10, 11, 12 |                           |
|  | 350 Adie, 309 SIFA, 1,325 | 250 Adie, 309 SIFA, 1,270 | 250 Adie, 309 SIFA, 600 |                                |                                       |               |                           |
|  | Habitat et Humanisme      | Habitat et Humanisme      | Habitat et Humanisme    |                                |                                       |               |                           |
| Holdings in "societal" funds   | -                         | 1/ Citizen Capital        | 0.5/BAC                 | EURm                           | HSBC France                           | FS 7          |                           |
| <b>7 Number of customer complaints submitted to the Ombudsman</b>                                      |                           |                           |                         |                                |                                       |               |                           |
| Number of complaints processed and signed by the Ombudsman   | 548                       | 552                       | 502                     | Number                         | HSBC France                           | PR 8          | 6.7                       |
| <b>8 Level of satisfaction of our retail customers: customers claiming to be "very satisfied" (Q4)</b> |                           |                           |                         |                                |                                       |               |                           |
| Customer recommendations during the past two years (Q4)  | 50                        | 55                        | 52                      | %                              | HSBC France                           |               |                           |
|  | 40                        | 38                        | 35                      | %                              | HSBC France                           |               |                           |
| <b>Environmental Footprint</b>   |                           |                           |                         |                                |                                       |               |                           |
| 9 Energy Consumption   | 63                        | 66                        | 74                      | GWh                            | HSBC in France                        | EN 3, EN 4    | 6.5.5                     |
| Energy consumption in MWh/FTE  | 6.39                      | 6.69                      | 7.48                    | MWh/FTE                        | HSBC in France                        |               |                           |
| 10 Transportation  | 39.42                     | 40.3                      | 36.61                   | M per km                       | HSBC in France                        | EN 16         | 6.5.5 Principles 7 & 8    |



| Indicator  | Change                                    |                     |                     | Reference documents |                   |           |                  |
|--|---|---------------------|---------------------|---------------------|-------------------|-----------|------------------|
|  | 2012                                      | 2011                | 2010                | Scope*              | GRI 3             | ISO 26000 | Global Compact   |
| 11 Direct CO <sub>2</sub> emissions.....   | <input checked="" type="checkbox"/> 10.21 | 10.37               | 10.95               | HSBC in France      | GRI 16            | 6.5.5     | Principles 7 & 8 |
| - direct CO <sub>2</sub> emissions (Energy).....   | <input checked="" type="checkbox"/> 4.89  | 4.93                | 6.45                | HSBC in France      | EN 16             | 6.5.5     | Principles 7 & 8 |
| - direct CO <sub>2</sub> emissions (transportation).....   | <input checked="" type="checkbox"/> 5.32  | 5.44                | 4.5                 | HSBC in France      | EN 16             | 6.5.5     | Principles 7 & 8 |
| 12 Water Consumption.....  | 150                                       | 151                 | 160                 | HSBC in France      | EN 8              | 6.5.4     | Principles 7 & 8 |
| Water consumption per FTE.....   | 15.22                                     | 15.30               | 16.17               | HSBC in France      | EN 8              | 6.5.4     | Principles 7 & 8 |
| 13 Paper Consumption.....  | <input checked="" type="checkbox"/> 1,535 | 1,803               | 1,847               | HSBC in France      | EN 1, EN 2, EN 22 | 6.5.4     |                  |
| % of FSC paper.....  | <input checked="" type="checkbox"/> 91    | 90                  | 86                  | HSBC in France      | EN 1, EN 2, EN 22 | 6.5.4     |                  |
| 14 Waste production.....   | 1,729                                     | 1,926               | 2,224               | HSBC in France      | EN 1, EN 2, EN 22 | 6.5.4     | Principles 7 & 8 |
| Waste production per FTE <sup>1</sup> .....  | 175                                       | 194                 | 224                 | HSBC in France      | EN 1, EN 2, EN 22 | 6.5.4     | Principles 7 & 8 |
| % of recycled waste/total waste.....   | 72  | 77                  | 68                  | HSBC in France      | EN 1, EN 2, EN 22 | 6.5.4     | Principles 7 & 8 |
| <b>Human resources and security</b>  |   |                     |                     |                     |                   |           |                  |
| 15 Total workforce <sup>2</sup> .....  | 5,410 W/<br>4,014 M                       | 5,645 W/<br>4,215 M | 5,969 W/<br>4,510 M | HSBC France         | LA 14             | 6.3.7     | Principle 6      |
| Men (M) / Women (W).....   |   |                     |                     | HSBC France         |                   | 6.3.7     | Principles 7 & 8 |
| Recruitments.....  | <input checked="" type="checkbox"/> 548   | 1,188               | 1,133               | HSBC France         |                   |           |                  |
| Dismissals.....  | <input checked="" type="checkbox"/> 85    | 62                  | 99                  | HSBC France         |                   |           |                  |
| 16 Organisation of working hours   |   |                     |                     |                     |                   |           |                  |
| Absenteeism <sup>3</sup> .....   | 3.4                                       | -                   | -                   | HSBC France         |                   |           |                  |
| 17 Equal treatment:  |   |                     |                     |                     |                   |           |                  |
| - number of persons with disabilities.....   | 310                                       | 289                 | 250                 | HSBC France         |                   |           |                  |
| - number of recruitments via the IMS and Mozaik HR.....  | 88  | 25                  | 33                  | social results      |                   |           |                  |
| - % of employees less than 30 years old.....   | <input checked="" type="checkbox"/> 13.8  | 17                  | 18.1                | HSBC France group   |                   |           |                  |
| - % of employees over 50 years old.....  | <input checked="" type="checkbox"/> 29.6  | 29                  | 29.1                | HSBC France group   |                   |           |                  |
| - % of women in management.....  | <input checked="" type="checkbox"/> 17.5  | 18                  | 15                  | HSBC France group   |                   |           |                  |
| 18 % of non-executive directors (without function in the HSBC Group at 31.12).....   | 44  | 41                  | 39                  | HSBC France         |                   | 6.2       |                  |
| 19 Number of employees teleworking.....  | <input checked="" type="checkbox"/> 498   | 344                 | -                   | HSBC France         |                   |           |                  |
| 20 Health and Safety :   |   |                     |                     |                     |                   |           |                  |
| - number of fatal accidents at work.....   | 0   | 0                   | 0                   | HSBC France         | LA 7              | 6.4.6     |                  |
| - number of accidents resulting in more than 3 days of work incapacity.....  | 119                                       | 124                 | 52                  | HSBC France         | LA 7              | 6.4.6     |                  |
| - rate of work- and travel-related accidents <sup>4</sup> .....  | 9.3                                       | 11.4                | 11.9                | HSBC France         |                   |           |                  |
| - severity rate of work- and travel-related accidents <sup>5</sup> .....   | 0.2                                       | 0.2                 | 0.3                 | HSBC France         |                   |           |                  |
| 21 Training.....   | 284,297                                   | 202,509             | 235,505             | HSBC France         |                   |           | Principle 6      |
| <b>Commitment and patronage</b>  |   |                     |                     |                     |                   |           |                  |
| 22 Sponsorship Budget (EUR).....   | 2.6                                       | 2.3**               | 1.8                 | HSBC in France      |                   | 6.8       |                  |
| % of the sponsorship budget / pre-tax earnings.....  | 0.46                                      | 1.2                 | 0.37                | HSBC in France      |                   | 6.8       |                  |
| % approx. employees involved in volunteer SD activities.....   | 20  | 35                  | 40                  | HSBC in France      |                   | 6.8       |                  |
| Number of hours of volunteer work during work hours.....   | 8,621                                     | -                   | -                   | HSBC in France      |                   | 6.8       |                  |
| 1 Full-Time Equivalent.  |   |                     |                     |                     |                   |           |                  |
| 2 See also page 61.  |   |                     |                     |                     |                   |           |                  |
| 3 Number of working days of absences due to sickness / number of total theoretical working days.   |   |                     |                     |                     |                   |           |                  |
| 4 Rate of work- and travel-related accidents calculated using the following ratio: (number of accidents resulting in lost time/number of hours worked)*10 <sup>3</sup> .   |   |                     |                     |                     |                   |           |                  |
| 5 Severity rate of work- and travel-related accidents calculated using following ratio: (number of working days lost due to work- and travel-related accidents/number of hours worked)*10 <sup>3</sup> .   |   |                     |                     |                     |                   |           |                  |
| * HSBC France is a 99.9% subsidiary of the HSBC Group. The HSBC France group corresponds to the perimeter of the consolidated financial statements and HSBC France corresponds to the perimeter of the individual financial statements. HSBC in France's scope of operations comprises the operations of the HSBC Group in France, of HSBC Assurances Vie (France) and HSBC Assurances IARD (France) and of the Paris branch of HSBC Bank plc (excluding intra-group financing costs). |   |                     |                     |                     |                   |           |                  |
| ** An additional payment of EUR 1.8 million for the Fondation HSBC pour la Photographie were made to the Fondation de France under the aegis of which are placed these two programs. This amount will be consumed within 3 years from 2012, and will be included in this table as and when they are awarded to final beneficiaries.  |   |                     |                     |                     |                   |           |                  |
| <input checked="" type="checkbox"/> Selection of societal, social and environmental information having been verified with a level of moderate assurance by one of the Statutory Auditors.  |   |                     |                     |                     |                   |           |                  |

## Corporate, social and environmental responsibility (continued)

### Statement attesting to disclosure and limited assurance report of one of the Statutory Auditors on a selection of social, environmental and societal information

*This is a free translation into English of the original report issued in French and is provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

Year ended 31 December 2012

To the Chief Executive Officer of the company HSBC France:

As requested, and in our capacity as Statutory Auditors of the company HSBC France, we present you our report on the consolidated environmental, social and societal information presented in the management report for the financial year closed on 31 December 2012, in accordance with the provisions of article L. 511-35 of the French Monetary and Financial Code and article L. 225-102-1 of the French Commercial Code.

#### Management responsibility

The Board of Directors is responsible for establishing a management report including consolidated social, environmental and societal information required under article L. 511-35 of the French Monetary and Financial Code and article R. 225-105-1 of the French Commercial Code (hereafter “the Information”), established in accordance with the protocol used by the HSBC France group (“the Protocol”) and available at the company’s head office. A summary of the Protocol appears in the “Methodological details on corporate, social and environmental information” section of the management report.

#### Independence and quality control

Our independence is defined by the rules and regulations, ethical code of the profession and by the provisions of article L. 822-11 of the French Commercial Code. We have also implemented a quality control system which included documented policies and procedures aiming at ensuring compliance with the ethical rules, professional standards and applicable rules and regulations.

#### Statutory Auditors’ responsibility

It is our responsibility, based on the work performed to:

- attest that the required Information has been disclosed in the management report or that, in the event that any Information has been omitted, an explanation is provided in accordance with the third paragraph of article R. 225-105 of the French Commercial Code and French Decree no. 2012-557 of 24 April 2012 (Statement attesting to disclosure);
- express a limited assurance conclusion on the fact that the information selected by the HSBC France group, mentioned in the table below and identified by the  symbol (hereafter “Data”) was established, in all its material respects, in accordance with the above-mentioned Protocol (limited assurance report).

To assist us in conducting our work, we called on the sustainable development specialists of our firm.

#### I - Statement attesting to disclosure

We performed our work in accordance with the professional standards applicable in France.

- we compared the Information presented in the management report with the list provided by article R. 225-105 of the French Commercial Code;
- we verified that the Information covers the scope of consolidation, *i.e.*, the Company, its subsidiaries as defined by article L. 233-1 and the subsidiaries it controls as defined by article 233-3 of the French Commercial Code, within the methodological limitations set out in the “Methodological details on corporate, social and environmental information” section of the management report;
- for any consolidated Information that has been omitted, we verified that the explanations provided complied with the provisions of French Decree no. 2012-557 of 24 April 2012.

Based on our work, we attest that the required Information is presented in the management report.

## II - Statutory Auditors' report with limited assurance on a selection of Data

### Nature and scope of our work

We conducted our procedures in accordance with International Standards on Assurance Engagements (ISAE 3000) standard, in compliance with professional standards and best practice applicable in France.

We performed limited procedures in order to obtain a limited level of assurance that the Data selected by the group, mentioned in the table below and identified by the ☑ symbol did not contain any material misstatements. A reasonable level of assurance would have required more extensive work.

| Environmental indicators   | Scope  |
|--|--|
| CO <sub>2</sub> emissions regarding building energy consumption in 2012 (electricity, gas, fuel, urban heating and air conditioning) and transportation..... | HSBC in France (HSBC France and all its French subsidiaries, HSBC Bank plc Paris Branch, HSBC Assurances Vie (France) and HSBC Assurances IARD (France)) |
| Paper consumption and percentage of FSC paper among the total paper consumption.....   | (France)   |
| Social indicators  | Scope  |
| Percentage of employees under 30 years old.....  | HSBC Group in France   |
| Percentage of employees above 50 years old.....  | (except HSBC Assurances Vie (France) and HSBC Bank plc Paris Branch)   |
| Percentage of women among the executives.....  |  |
| Number of employees teleworking.....   | HSBC France  |
| Number of hires and redundancies.....  | HSBC France  |
| Societal indicators  | Scope  |
| Company saving schemes: total assets of the SRI (Socially Responsible Investment) range.....   | HSBC Global Asset Management (France)  |
| Investment of the HSBC EE <i>Diversifié Responsable et Solidaire</i> company savings fund for the benefit of solidarity-based companies.....                 | HSBC Global Asset Management (France)  |

We carried out the following reviews:

- we assessed the Protocol with respect to its relevance, completeness, objectivity, clarity and reliability, taking into account best practice in the sector where applicable;
- we verified the implementation in the group of a reporting, consolidation, handling and control process, aiming at the completeness and the consistency of the selected Data. We analysed the internal control and risk management process related to the Data production;
- we interviewed the people responsible for reporting Data related to the environment, social and societal activity, and carried out tests of details, on a sample basis, on the application of the Protocol on selected entities<sup>1</sup> (“the Entities”);
- we carried out consistency checks on the consolidation of the Data.

The contribution of the selected sites represents on average:

- between 74% and 100% of the environmental Data;
- 100% of the social Data;
- 100% of the societal (banking information) Data.

#### 1 Selected entities:

For environmental Data:

- CO<sub>2</sub> emissions regarding building energy consumption in 2012 (electricity, gas, fuel, urban heating and air conditioning) and transportation: HSBC in France, at the Real Estate Operations and Purchasing Departments.
- Paper consumption and percentage of FSC paper among the total paper consumption: HSBC France and HSBC Assurances Vie (France), at the Supply Services Department.

For social Data:

- Percentage of employees under 30 years old, percentage of employees over 50 years old, percentage of women among the executives: HSBC in France (except HSBC Assurances Vie (France) and HSBC Bank plc Paris Branch), at the Human Resources Department.
- Number of hires and redundancies, number of employees teleworking: HSBC France, at the Human Resources Department.

For societal Data: at the HSBC Global Asset Management (France) entity level.

## Corporate, social and environmental responsibility (continued)

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### Conclusion

On the basis of our work, nothing has come to our attention that causes us to believe that the selected Data, mentioned in the table above and identified by the  symbol, has not been prepared, in all material respects, in accordance with the Protocol.

Paris-La Défense, on 12 April 2013

KPMG Audit FS II

Philippe Arnaud

*Partner*

In charge of the Climate Change  
and Sustainability Services Department

Pascal Brouard

*Partner*

## Risk management

All the HSBC France group's activities involve analysis, evaluation, acceptance and management of some degree of risk or combination of different types of risks.

In compliance with the requirements of regulation 97-02 and the demands of the HSBC Group, the HSBC France group has established a permanent control and risk management system as set out in the Chairman's report on the internal control procedures and risk management procedure<sup>1</sup>.

This control and risk management framework is structured into ten risk function areas:

- financial risks:
  - credit,
  - markets,
  - structural interest rate/forex/liquidity risk;
- other operational risks:
  - legal,
  - tax,
  - information technologies,
  - security and fraud (which is enlarged since January 2012 to security, fraud, business continuity and information security),
  - human resources,
  - compliance (set out in the Chairman's report<sup>2</sup>),
  - accounting (set out in the Chairman's report<sup>3</sup>).

### FINANCIAL RISK

#### Credit risk

In the HSBC France group, credit risk management is overseen by three separate departments within risk functions:

- Wholesale Credit Risk Department: this combines the Credit teams (decision-making and Early Collection unit) allocated to Global Banking and Markets and Commercial Banking, recovery for Commercial Banking clients (excluding "Pôles Entrepreneurs" dedicated to very small companies) and monitoring and IEC teams (Commercial Information and Research), combined within a "Risk detection and monitoring" unit. The "Models" team is also part of the Wholesale Credit Risk Department;
- Retail Credit Risk Department: in addition to a management and statistical portfolio analysis function, this unit comprises the Credit (decision-making) teams dedicated to Retail Banking and Wealth Management and Private Banking clients, an enlarged Retail Early Collection unit covering both Early Collection (SRA) and Recovery units from Retail clients and "Pôles Entrepreneurs" cases, and also Decision-making Systems and Processes teams;

- Risk Business Management, including the Risk Strategy Department: this unit groups together support and control functions, *i.e.* Risk administration, Reporting, Credit review team and Remote monitoring, accounting and Internal Control for the Wholesale and Retail Credit teams. This entity also handles risk appetite, stress scenarios, emerging risks and regulatory oversight.

Independently of the business line it relates to, these departments report directly to the Deputy CEO in charge of risks, and report functionally to the HSBC Group Risk Department Europe.

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. It arises principally in the lending, trade finance, treasury and leasing businesses. The HSBC Group has standards, policies and procedures dedicated to monitoring and managing risk from all such activities.

#### Governance

HSBC Holdings plc is responsible for the credit risk management framework and provides centralised oversight and management of credit risk for its subsidiaries worldwide. In addition, each HSBC Group entity is accountable for:

- monitoring exposures to sovereign entities, banks and other financial institutions. HSBC's credit and settlement risk limits for counterparties in these sectors are approved and overseen by Group Credit Risk, to optimise the use of credit availability and avoid excessive risk concentration;
- monitoring intra-group exposures to ensure they are maintained within regulatory limits;
- controlling cross-border exposures, through the imposition of country limits with sub-limits by maturity and type of business. Country limits are determined by taking into account economic and political factors, and applying local business knowledge. Transactions with countries deemed to be at high risk are considered on a case-by-case basis.

The RMCs (Risk Management Committees), chaired by the Head of the Business line concerned or a delegate, attended by the Deputy CEO, provide the RMM with information and decision-making on regards credit risk.

Credit risk management for each of the main business lines (Global Banking and Markets, Commercial Banking, Retail Banking and Wealth Management) is supervised by the HSBC France Risk Management Meeting<sup>4</sup> (RMM), which meets monthly, chaired by the Deputy CEO. The committee's minutes along with a summary are then submitted to the monthly risk monitoring committee meetings organised by the "Europe" Risk Management Department.

<sup>1</sup> See Chairman's report pages 40 to 50.

<sup>2</sup> See Chairman's report pages 46 to 47.

<sup>3</sup> See Chairman's report pages 48 to 49.

<sup>4</sup> See Chairman's report page 43.

## Risk management (continued)

RMM is the main body responsible for lending policy and permanent control for the Credit function in the HSBC France group. Its responsibility is to monitor the Wholesale Credit Risk and Retail Credit Risk Departments and the Credit function's activities, and to define the strategic direction of the HSBC France group's policy as part of the HSBC Group's general directives. It is informed by the two departments of the main lending decisions, the state and development of the various lending portfolios, the efficiency of the Basel II framework it uses to define its lending policy, and the permanent control results reported.

RMM attendees are informed of any incidents in the Credit function and of the corrective measures taken. A summary of this information is presented to the quarterly session of the ORIC Committee (Operational Risk and Internal Control).

### The control framework

The Head of Wholesale Credit Risk and the Head of Retail Credit Risk are accountable for the permanent control in the HSBC France group's Credit function.

The two departments are the hub of the Credit function of the Global Banking and Markets. To ensure that information flows efficiently to all levels, controls are managed and adapted to the staff involved in the Credit Function according to pre-established intervention thresholds for monitoring, provisioning, level of credit authority, etc.

Controls are performed by dedicated internal controllers who carry out second-level independent controls on the Credit function (internal control teams BRCM (Business Risk and Control Management) of Risk Business Management, Global Banking and Markets and Commercial Banking, Retail Banking and Wealth Management and subsidiaries, the Credit review team and Monitoring), but also on agents also involved in operating activities (credit managers, credit analysts, branch managers and relationship managers and wholesale and retail supervisory departments).

The two Heads of permanent control for Credit activities are informed of any major issues relating to these activities within their respective scopes.

### Tools

In compliance with regulation 97-02, each entity in charge of credit risk has set up a system to cover all risks: generic risks inherent in lending activities have been listed in business line risk maps for each business line (Commercial Banking, Global Banking and Markets, Retail Banking and Wealth Management) covering the entire Credit function. These maps set out the required checks and reports required by the various participants and their frequency.

This structure is complemented by a permanent control framework for the central coordination of Basel II lending, involving:

- data quality (quality of the data used);
- Basel II monitoring (assessment of Use Test).

Internal control procedures are updated at least annually and validated by the Heads of permanent control for the Credit function by the review of risk maps presented at the ORIC Committee. They are also updated whenever a major change is made requiring the revision of controls or coverage of new risks.

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### Description of lending procedures

#### Lending powers

The power to grant loans is limited to those holding lending powers. Beneficiaries are notified in writing according to precise standards. Powers are allocated to individuals by name and not position. There is no lending committee: decisions are made individually.

HSBC France's CEO holds powers within the authority limits delegated by HSBC Bank plc. He has delegated his powers to the Deputy CEO, who in turn has sub-delegated them to each of the Credit departments. For amounts in excess of these limits, cases are sent to the HSBC Bank plc Credit Department for approval and, above a certain threshold, to the HSBC Group (HSBC Holdings plc) Risk Department for an absence-of-objection statement ("concurrence").

Working in concert with the Deputy CEO, the CEO has also delegated some of his powers in limited amounts:

- to the CEOs of banking subsidiaries;
- to the heads of commercial entities in the network and their employees.

A holder of lending powers is able to grant loans in compliance with the HSBC Group and HSBC France group lending directives.

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### The credit risk measurement and monitoring framework

The objectives of the monitoring and control of lending are:

- to anticipate adverse changes in our counterparties in order to enable us to take all steps to safeguard the interests of the HSBC France group;
- to pinpoint within the branch network the main areas of risks according to the main risk indicators;
- to conduct credit reviews in the branch network.

The identification, measurement, monitoring and control of credit risk are carried out in compliance with the HSBC Group directives (Group Standards Manual and Functional Instruction Manuals), local directives (Business Instruction Manuals) and the policy laid down by the RMC risk management committees (Global Banking and Markets, Commercial Banking and Retail Banking and Wealth Management).

Everyone involved in the lending process is part of credit risk control; everyone involved in the decision-making process is accountable. However, the responsibility for overseeing a loan falls mainly on the entity that granted the loan. Furthermore, the management structure in that entity must play its part in monitoring and managing credit risk.

Second-level controls are performed by dedicated credit risk monitoring teams.

The Credit Review France team takes a risk-based approach in order to select the entities to be audited and put together samples of credit cases to be reviewed. It also works according to the principle of an audit cycle of a maximum of three years for Global Banking, Leveraged Finance, HSBC Factoring (France) and Corporate Banking Centres (CBC) and a maximum of four years for the rest of its scope. At the request of the Deputy CEO, in charge of risks, the team can perform ad hoc audits of various issues relating to credit. Apart from follow-up audits, audits are carried out on-site.

On 1 October 2012, the Monitoring team – which performs remote credit reviews of Corporate Business Centres (*Centre d’Affaires Entreprises* – CAE) and Entrepreneurs divisions (*Pôles Entrepreneurs*) for the Commercial Banking network – was attached to the Credit Review team. The scope of intervention of this team, which conducts all of its reviews remotely, has been extended to the 23 Retail Banking and Wealth Management groups of branches. A specific method has been developed for Retail Banking and Wealth Management remote credit reviews, based on the method used during on-site credit reviews. At the same time, the method for Commercial Banking remote credit reviews has been overhauled in accordance with the standards of the HSBC Group.

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#### Credit quality<sup>1</sup>

The HSBC Group’s credit risk rating systems and processes differentiate exposures in order to highlight those with greater risk factors and higher potential severity of losses. For individually significant exposures, risk ratings are reviewed regularly and amendments are implemented promptly when necessary. Within the HSBC Group’s retail portfolios, risk is assessed and managed using a wide range of risk and pricing models.

This risk rating system is based on the probability of default and loss estimates, in accordance with the internal rating methods required by the Basel II framework for calculating regulatory capital.

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#### Guarantees received and other mitigating credit risk factors

The HSBC Group entities are required to implement guidelines on the acceptability of specific classes of guarantees received or credit risk mitigation and determine

valuation parameters. Such parameters are expected to be cautious, regularly reviewed and supported by empirical evidence. Security structures and legal covenants are subject to regular review to ensure that they continue to fulfil their intended purpose and remain in line with local market practice.

#### Loans and advances<sup>2</sup>

Securities received are an important factor in mitigating credit risk. It is however the HSBC Group’s policy to ensure that customers have the resources to repay their loans rather than to rely on securities. In certain cases, depending on the customer’s standing and the type of product, facilities may be unsecured.

The principal types of security are as follows:

- in the personal sector, mortgages over residential properties;
- in the commercial and industrial sector, pledges on the business assets being financed;
- in the commercial real estate sector, pledges on the properties being financed;
- in the financial sector, pledges on financial instruments such as debt securities and equities in support of financial transactions;
- in the credit sector, credit derivatives<sup>3</sup> including Credit Default Swaps (CDS) are also used to manage credit risk in the HSBC Group’s loan portfolio.

The HSBC France group does not disclose the fair value of collaterals held as security on unpaid but not depreciated loans and advances or depreciated debts, as it is not available.

#### Other securities<sup>4</sup>

Other securities held as guarantees for financial assets other than loans and advances are determined by the structure of the instrument. Debt securities, treasury and other eligible bills are generally unsecured with the exception of Asset-Backed Securities (ABS) and similar instruments, which are secured by portfolios of financial assets.

#### Derivatives<sup>5</sup>

The ISDA (International Swaps and Derivatives Association) master agreement or, in France, the FBF (*Fédération bancaire française*) contracts are the HSBC Group’s preferred agreement for documenting derivatives activity. They provide the contractual framework within which dealing activity across a full range of over-the-counter products is conducted, and contractually binds both parties to apply close-out netting across all outstanding transactions covered by an agreement if either party defaults or if other pre-agreed termination events occur. It is common, and the HSBC Group’s preferred practice, for the parties to execute a Credit Support Annex (CSA) in conjunction with the ISDA master agreement. Under a CSA, collateral is passed between the parties to mitigate the market-contingent counterparty risk inherent in the outstanding positions.

1 See the Consolidated financial statements, Note 33 Risk management page 166.

2 See the Consolidated financial statements, Note 30 Assets charged as security for liabilities and collateral accepted as security for assets page 161.

3 See the Consolidated financial statements, Note 13 Derivatives pages 135 to 139.

4 See the Consolidated financial statements, Note 33 Risk management pages 163 to 179.

5 See the Consolidated financial statements, Note 21 pages 114 to 116 and Note 13 pages 135 to 139.

## Risk management (continued)

### Deposit accounts

Settlement risk on multiple transactions, particularly those involving securities and equities, is substantially mitigated through assured payment systems or delivery *versus* payment mechanism.

### Concentration risk<sup>1</sup>

HSBC France puts the greatest emphasis on the quality and integrity of its risky assets base (including off-balance sheet commitments) and has introduced strict safeguards to avoid undue concentration of risk.

Risk diversification is a core principle within the HSBC Group. Risk concentration can come in a number of forms, including: a large concentration on a single counterparty, excessive commitment to geographical areas or business sectors, as well as from risk deriving from a lending portfolio that is too concentrated or that has correlated exposures.

The LCEP document (Large Credit Exposure Policy) sets out the policy of the HSBC France group on controlling Large Risks, and it also forms part of the policy of HSBC Bank plc, HSBC Holdings plc and meets the requirements of the French banking regulator, the *Autorité de contrôle prudentiel*.

The purpose of the LCEP is to ensure that:

- all HSBC France subsidiaries scrupulously adhere to both current policy and local regulatory requirements on large lending commitments in the jurisdictions in which they operate, and that they also apply the rules established by the local supervisory organisations;
- there is an appropriate framework procedure by which large commitments and concentrations of risk can be monitored and controlled;
- commitment to one individual borrower, or to a group of closely connected borrowers, should not become excessive in comparison to the capital base of HSBC France or HSBC Bank plc;
- excessive concentration and/or the combining of major exposures are excluded;
- commitments to geographical areas or business sectors should be strictly monitored to ensure that risky assets are diversified;
- reports to the Boards of Directors of HSBC France group subsidiaries, to HSBC France group Senior Management, and to the Boards of HSBC Bank plc and HSBC Holdings plc, and also to all supervisory bodies are compliant, consistent and in line with the HSBC Group policy.

To facilitate effective oversight and control, HSBC France, HSBC Bank plc and HSBC Holdings plc all hold centralised databases of information into which commitments are entered and by which they ensure that LCEP requirements are satisfied.

At the level of the Wholesale Credit Risk Department, the risk concentration is monitored using the supervision software programs, CARM and HUB (Vigirisk), which recover the authorisations and the balances outstanding from the operational systems and prepare monitoring reports.

### Concentration risk by counterparty

Risk exposure limits are classified into three categories:

- category A: all loans recognised on the balance sheet and trade facilities such as guarantees and standby letters of credit;
- category B: off-balance sheet treasury risks such as currency and interest rate swaps;
- payment: principally intraday risk on payment commitments and foreign exchange business with or in the name of our customers.

*Commitments to a single counterparty or group of counterparties, excluding financial institutions and central governments/central banks*

- Requirements of the HSBC Bank plc and the Financial Services Authority (FSA)

No exposure (total of categories A and B) may exceed 25 per cent of applicable capital, individual company or consolidated, of HSBC Bank plc without the prior agreement by the FSA.

To ensure that HSBC Bank plc complies with the FSA and LCEP requirements:

- authorisations (total of categories A and B), for HSBC France on the same counterparty or the same group of counterparties, in the normal course of its business may not exceed 25 per cent of HSBC France consolidated capital;
- HSBC France must obtain approval from HSBC Bank plc before taking additional authorisation exceeding 25 per cent of HSBC France consolidated capital.

There may be occasions or transactions exceeding this total (to a maximum of 50 per cent of HSBC France consolidated capital), which are possible on condition that:

- the risk relates to foreign exchange transactions or interest-rate products;
- the counterparty groups have an acceptable risk profile, have close relations with the HSBC Group, and are of significant importance to it;
- the risk is short-term.

Furthermore, settlement exposures within the normal course of operations should not exceed 25 per cent of HSBC France's consolidated capital. No settlement exposure should exceed 50 per cent of capital.

Any exposure representing more than 25 per cent of HSBC France's capital needs to be approved locally by the Deputy CEO for control of major risks, but also needs to follow the normal approval process from the usual

<sup>1</sup> See the Consolidated financial statements, Note 33 Risk management pages 163 to 179.



authorities. However, for any exposure representing more than 50 per cent of HSBC France's consolidated capital, an appropriate exemption request must be sent for approval to the Regional department. This exemption should be documented and reviewed annually.

For LCEP limits, directives are sent by the HSBC Group and are transposed at the HSBC France level, then approved by the Chief Credit Officers and the Deputy CEO in charge of risks.

A quarterly report on all risks (the total of categories A and B, and payment risk on an individual basis and settlement risk applicable to these counterparty groups) exceeding 10 per cent of HSBC France's capital must be submitted to HSBC France Senior Management, to HSBC France's RMM, to HSBC Bank plc's Wholesale and Market Risk RMC and to the Board of Directors of HSBC Bank plc and HSBC Holdings plc. This quarterly report must also be submitted to the HSBC France Audit and Risk Committee.

- *Autorité de contrôle prudentiel* (the French banking regulator) requirements

HSBC France group's net weighted risks (as defined by the *Autorité de contrôle prudentiel*) in the course of its ordinary business must not exceed 20 per cent of HSBC France group capital as based on external investment-grade ratings and internal counterparty ratings and 15 per cent for counterparties that do not have an external rating or (in the absence of an external rating) an internal rating of investment grade level.

In no case, even if the commitment is compliant with *Autorité de contrôle prudentiel* requirements, can any HSBC France group commitment be authorised if it would result in the requirements of either the HSBC Group or FSA being exceeded.

In addition to quarterly monitoring, a daily control procedure has been introduced at relationship manager level to ensure that no accounts for which they are responsible exceed the limits.

#### *Commitments to financial institutions*

Commitments (categories A and B) to financial institutions should not exceed 25 per cent of HSBC France's capital after deducting protection and risk deduction techniques eligible for the BIPRU (Prudential sourcebook for Banks, Building Societies and Investment Firms).

Within the framework of these global commitments to financial institutions, type A and B commitments to the following exposures should not exceed 10 per cent of HSBC France's capital within the normal course of operations:

- exposures with a maturity of more than one year;
- exposures to subsidiaries of financial institutions that are not financial institutions themselves.

Furthermore, settlement exposures within the normal course of operations should not exceed 25 per cent of HSBC France's consolidated capital.

Exemptions are nevertheless possible if it is necessary for HSBC France to maintain commitments above the aforementioned thresholds. However, each situation should be kept at the minimum and exemptions should be sent to the Regional department (HSBC Bank plc Risk) for approval and must be documented and reviewed each year.

These exemptions should not result in the failure to comply with the policy relating to control of major risks applicable to HSBC Bank plc.

As is the case for all Group entities, HSBC France has delegated responsibility to HSBC Holdings plc for approving all limits for banks and certain non-bank financial institutions, on the basis of the recommendations made by the Head of Wholesale Credit Risk and Relationship Managers in charge of banks.

All commitments to banks, building societies and non-bank financial institutions are controlled *via* the Carm for Banks application. HSBC Holdings plc's Risk Management Department sets the overall limit for each counterparty, and oversees and reviews these limits on a regular basis.

A quarterly statement of HSBC France's 50 largest commitments (both categories A and B) to financial institutions (excluding non-bank financial institutions) is given to HSBC France's Senior Management, the Board of Directors of HSBC France, HSBC France's RMM, HSBC Bank plc's Wholesale and Market Risk RMC, HSBC France's Audit and Risk Committee and the Board of Directors of HSBC Bank plc and HSBC Holdings plc.

#### **Sectorial concentration risk**

It is an HSBC France group principle to avoid excessive concentration in any business sector, and to take corrective measures if necessary. The Wholesale Credit Risk Department is responsible for supervising compliance with this principle.

Some business sectors are governed by their own Caps and business sector directives laid down by HSBC France and/or the HSBC Group.

The software application used for monitoring industry concentration risk is Vigirisk, which centralises the balances outstanding from the various information systems.

The Caps are monitored quarterly and notified to Risk Management Global Banking and Markets. Any modifications to Caps must be approved by RMC Global Banking and Markets.

#### **Geographical area concentration risk**

The overall risk limits for countries and central governments/central banks are determined by experience, current events and local knowledge as well as by the latest political, economic and market information. Consideration of the duration of the exposure is also very important in setting overall limits.

Commitments (categories A and B) should not exceed 25 per cent of HSBC France's capital apart from in the case of certain specific exposures:

- exposures to governments and central banks located in a country benefiting from a zero weighting according to the standardised methodology (S&P rating of AAA to AA-);

## Risk management (continued)

- exposures to multilateral development banks (as rated in the glossary of the FSA Handbook) and international organisations (as rated in the BIPRU) with a zero weighting;
- exposures to central governments and central banks of the European Union denominated in the local currency benefiting from a zero weighting (BIPRU 3.4.5).

However, it should be noted that regardless of how the country with zero weighting is qualified, all propositions are submitted for individual risk approval and authorisations are registered as normal.

The exposure risk on countries, central governments and central banks is monitored by the HSBC Group Risk Department, which establishes all overall limits. Overall limits for single countries are revised at least annually or at short intervals depending on circumstances. These limits are monitored continuously and adjustments may be made at any time.

A quarterly report on country cross-border risk exposure (categories A and B grouped) in excess of 10 per cent of HSBC France's capital is given to Senior Management, the Audit and Risk Committee and the Board of Directors of HSBC France, HSBC Bank plc and HSBC Holdings plc.

### Market risk

#### Market risk monitoring system

The risk management policy determined by HSBC France Senior Management oversees market risk by global limits, which it reviews, and also validates the proposals made by Market Risk Management in Market Risk Forum.

The HSBC Group assigns these global limits to HSBC France. These global limits are divided by business line and translated into operational limits within each entity by the Market Risk Managers.

These global limits are defined in terms of lists of authorised instruments, underlying assets, markets and maturities, Value at Risk (VaR) limits, sensitivity levels, maximum loss and stress tests. They are revised at least once a year by the Market Risk Forum. The committee can amend them as required.

The process for allocating market limits and the permanent market risk control system as a whole involve a number of people from the HSBC Group and HSBC France, as well as special committees, the roles of which are set out below.

#### Types of limits<sup>1</sup>

The maximum exposure and risk that HSBC France intends to bear are defined in a set of limits.

#### Local mandate limits, or Room Mandates

The HSBC Group annually allocates HSBC France and HSBC Bank plc Paris Branch a local room mandate per entity. It covers the most significant limits in terms of:

- Value at Risk, overall, total trading, sub-limits of VaR on interest rates, foreign exchange, equities;

- sensitivity to risk factors including option factors (interest rates, government curve, inflation, volatility, exchange rates), and various "spread" factors;
- Exposure At Default (EAD) by bond issuers;
- maximum daily and monthly losses, referred to as "max-loss";
- instruments authorised, by maximum maturity, market/currency and pay-off category.

A "one pager" summary version for each Entity Room Mandate (HSBC France and HSBC Bank plc Paris Branch) is submitted for approval by the Deputy CEO and reviewed annually at the HSBC France Market Risk Forum.

There is also a more detailed version of each Entity Room Mandate, with greater granularity.

#### The limits set by HSBC France Market Risk Forum

Annually, this Committee reviews and sets "one pager" entity mandate limits for HSBC France and HSBC Bank plc Paris Branch on the recommendation of the Head of MRMaC France (Market Risk Management and Control).

#### Operational limits

Market Risk Management and Control (MRMaC) issues the Room Mandate limits for HSBC France and HSBC Bank plc Paris Branch as detailed operational limits or "desk mandates". These limits are allocated to each Business Unit (Management Unit) and, if necessary, broken down by sub-business. They cover the following indicators:

- sensitivity to risk factors including option factors (interest rates, government curve, inflation, volatility, exchange rates), including various "spread" factors;
- instruments authorised:
  - by maximum maturity,
  - by pay-off category ;
- additional limits governing specific activities.

These limits are set to be consistent with the VaR limits allocated by the HSBC France Market Risk Forum and with those allocated overall to HSBC France.

### Governance at the HSBC Group level

#### Wholesale and Market Risk (WMR)

In the HSBC Group, market risk supervision is carried out within the Wholesale and Market Risk Department. Its Head reports to the HSBC Group Chief Risk Officer. This department is responsible, via the Market Risk Management and Control (MRMaC) entity, for allocating risk limits to the various HSBC Group entities by means of Site Entity Room Mandates once they have been approved by the HSBC Bank plc ALCO and RMM bodies. Similarly, this department is responsible for monitoring exposure at the HSBC Group level and for authorising temporary limits. The Wholesale and Market Risk has a European dimension.

<sup>1</sup> See the Consolidated financial statements, Note 13 Derivative instruments page 135 and Note 29 Maturity analysis of financial assets and liabilities page 159.

## **Europe Middle-East Africa Market Risk Management and Control: MRMaC EMEA**

The Head of MRMaC EMEA, who reports directly to Global Head MRMaC and to European Head Wholesale Credit and Market Risk, supervises the Room Mandates review process. He submits them for review by WMR. He is the functional superior of the Head of MRMaC France.

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### **HSBC France bodies and persons responsible for market risk monitoring**

#### **The HSBC France Market Risk Forum**

Its task is to supervise all market risks, to ensure that appropriate controls exist and to approve the main rules included in the supervision system.

The HSBC France Market Risk Forum is chaired by the Deputy CEO in charge of risks and meets monthly. It includes the heads of the business lines concerned by these risks and the main heads of the associated control functions: the Head of MRMaC France, the Head of Quantitative Risk and Valuation Group (QVRG) and the Global Banking and Markets Chief Operating Officer. The following are also members of the HSBC France Market Risk Forum: the Global Banking and Markets Finance Officer, and the Global Banking and Markets Product Control Officer.

MRMaC France acts as secretary of the committee.

The HSBC France Market Risk Forum reviews summary risk and results indicators, analyses any significant events observed during the previous month, including any breaches of “one-pager” mandate limits, (see page 80 “Types of limits”), instructs requests for permanent limits, and reviews temporary limits.

The committee also validates changes to calculation methods and risk measurement methods relating to secured funds.

All entities generating market risks must apply for renewal or extension of limits annually.

#### **The Risk Management Meeting (RMM)**

The minutes of the Market Risk Forum are attached to the monthly RMM file, during which the Head of the MRMaC team establishes the main points to be raised in terms of market risk.

#### **The Global Banking and Markets Chief Operating Officer**

With regard to his responsibility for Global Banking and Markets Risk, the Global Banking and Markets Chief Operating Officer reports on a functional basis to the Deputy CEO in charge of risks and permanent control. He is responsible in particular for QVRG, Product Control and ORIC. He and the head of MRMaC France are responsible for informing Senior Management of the content and development of market risk exposures. For this purpose, the Global Banking and Markets Chief Operating Officer, together with the MRMaC France Head of control functions,

organises regular information meetings for the Deputy CEO in charge of risks, which are attended by the Heads of QVRG and Product Control.

#### **Market Risk Management and Control**

Within Wholesale and Market Risk (WMR), MRMaC designs, develops and implements the market risk management policy. This in particular covers:

- permanent monitoring of market risks;
- the development and implementation of procedures complying with regulatory requirements and with best practices;
- allocation of market risk limits within the HSBC Group compatible with the HSBC Group’s strategy and risk appetite;
- approval of new products;
- consolidation of exposure at the HSBC Group level to market risks and Value at Risk (VaR) calculations.

The Head of MRMaC France reports on a hierarchical basis to the Deputy CEO in charge of risks and permanent control and functionally to the Head of MRMaC EMEA.

The Head of Traded Risk France is responsible for both MRMaC France and Traded Credit France. He is responsible for permanent control of market risk in accordance with regulation 97-02, and for ensuring the consistency and effectiveness of the market risk control framework. He will be referred to as Head of MRMaC France in this section on market risk.

In general, it is up to the Head of MRMaC France to provide Senior Management and HSBC France’s Market Risk Forum with comments and explanations concerning any significant breaches of max-loss and limitations (One pager Room Mandate), or any positions he deems useful for Senior Management to know about.

The Head of MRMaC France is a member of the HSBC France Market Risk Forum, the HSBC France Balance Sheet ALCO and the HSBC France Capital Management Forum. He takes part in the periodic Senior Management information meeting organised by the Chief Operating Officer of Global Banking and Markets and in the HSBC France Audit and Risk Committee.

MRMaC is made up of two teams: the Market Risk Management (MRM), a team of 8 people, and the Market Risk Control (MRC), a team of 14 people.

#### **Market Risk Management (MRM)**

Market Risk Management (MRM) defines market risk mandate limits, deals with breaches of limits and exceptional situations, analyses positions, monitors positions as a function of market movements, analyses the appropriateness of risk metrics (sensitivity, VaR, stress scenarios), defines and prepares a summary analysis of market risks for Senior Management, is involved in improving risk monitoring procedures and implements new indicators, as required by market developments.

## Risk management (continued)

The MRM team prepares the annual review of Room Mandates and, after in-depth analysis and approval from the HSBC France Market Risk Forum, submits it to WMR for approval *via* the Head of MRMaC EMEA.

Market Risk Management then defines “one-pager” and detailed Room Mandates, together with the desk mandates that apply to each business unit or management unit.

### Market Risk Control (MRC)

The Market Risk Control teams are responsible on a day-to-day basis for checking adherence to all of the various market risk limits, regardless of the level of the market risk mandate and the nature of the limit in question. They report any breaches of these limits and also any consumption in excess of a warning threshold set at 80 per cent of the limit. They are responsible for reporting on weekly stress tests. They also carry out the backtesting.

The backtesting compares the *ex ante* calculated VaR figures with *ex post* daily P&L (Profit & Loss) figures. This comparison tests the ability of VaR to control the expected P&L variations and therefore helps assess the quality of the internal model. Any shortcomings in the VaR model will particularly come to light if the day’s P&L figures exceed 99 per cent VaR or where VaR systematically and overwhelmingly exceeds daily P&L figures.

Backtesting is carried out both on profits and losses, using extreme quantiles (1 per cent and 99 per cent) of theoretical VaR distributions. The “backtesting violation” exceptions are reported and analysed.

The model is backtested by taking 99 per cent, one-day VaR figures and comparing them with daily results determined from changes in market prices assuming constant positions. Backtesting is done daily. Its results are reviewed monthly in a special HSBC Group committee and notified quarterly to the regulator.

The Market Risk Control structure is in line with that of the business lines.

A dedicated team produces and distributes HSBC France’s consolidated market risk reports for Senior Management Paris and the HSBC Group Consolidation. The team is also responsible for producing the various periodical summary statements required for both internal needs (RMM pack, annual reports, etc.) and external needs, such as supervisory authorities.

Market Risk Control reports hierarchically to the Head of MRMaC France and functionally to the Head of Global MRC.

### Quantitative Risk and Valuation Group (QRVG)<sup>1</sup>

Models developed by the front office research team are used in managing, valuing and assessing the risks of some derivative products. These models as well as VaR models are validated by an independent, specialist unit, the Quantitative Risk and Valuation Group (QRVG). Its manager reports on a local level to the Global Banking and Markets Chief Operating Officer and functionally to the Head of QRVG EMEA.

### Valuation Committee

Reporting to the Head of Product Control, it includes QRVG, Product Control and MRMaC members, and representatives of the financial functions of Global Banking and Markets and front office representatives. It meets within the first two weeks of the following month for discussion between all parties of the parameters of the models used by the front office. Also examined during these meetings are changes in the main calibration and price control indicators. A review is carried out of operations that are specifically modelled in front office/back office systems: “booking” by the custodian, specific features not modelled in the systems.

This committee also examines the methods for calculating provisions.

### Conclusion

HSBC France’s market risk mandate for 2012 was a continuation of that adopted in 2011, with a gradual reduction in risk metrics relating to the most volatile risk factors.

Throughout 2012, HSBC France continued to play a major role as a platform for the HSBC Group in eurozone government bonds and euro-denominated derivatives.

Particular attention was paid to monitoring positions on eurozone government bonds, which continued to be the main drivers of movements in capital markets earnings in 2012.

Usage of the main limits was relatively high throughout 2012, reflecting the substantial increase in risk-factor volatility.

Exposure to the debts of various eurozone countries, particularly those of peripheral countries, was maintained during the year 2012 within the allocated risk limits. Interest-rate movement sensitivity limits, which measure P&L volatility, were reduced significantly.

Throughout the first half of 2012, HSBC France operated with a multiplying factor close to the maximum level for calculating the regulatory capital requirement following the recording of a number of exceptions from VaR back-testing in 2011. This factor decreased during the second half of the year as exceptions from back-testing fell outside the regulatory window of one year rolling. At the end of the year, this factor was back at its minimum level.

Stressed VaR was introduced at 31 December 2011, in accordance with applicable regulations, resulting in an increase in the capital requirement. The reduction in market volatility accompanied by a reduction in risk nevertheless led to a reduction in VaR and stressed VaR in 2012.

<sup>1</sup> See the Consolidated financial statements, Note 13 Derivative instruments page 135 and Note 33 Risk management, page 159.

## Interest-rate risk

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Structural interest-rate risk is managed in accordance with HSBC Group standards and centrally by the ALM Department (DGFB) which is part of the Finance Department.

This structural interest rate risk affects banking operations and structural components of the balance sheet and does not affect market operations. The main objective of HSBC France structural rate risk management is to suppress the sensitivity of net income to interest rates by managing the fixed interest rate gap (imbalance between expected fixed interest inflows and outflows by maturity ranges).

Structural interest rate risk arises mainly from the changes in disparities between future returns on assets and future costs of liabilities stemming from variations in interest rates. Analysis of this risk is complicated, as a result of the need to make assumptions, partly due to the options available to borrowers on some products, for instance early repayment of property loans, but also because of the behaviour of depositors with regard to balances that by contract are withdrawable on demand, such as current accounts. When necessary, behavioural features, which are different from contractual features, are assessed to determine the actual underlying interest rate risk.

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### Governance

The body responsible for monitoring structural interest rates, liquidity and forex risks is the Balance Sheet ALCO which is headed up by the DGFB which reports to the Risk Management Meeting. The Balance Sheet ALCO, which meets every month, brings together the main heads of business lines and support functions concerned by ALM. It examines risk indicators prepared by the Finance Department and analyses all significant changes in the financial and regulatory environment relating to these risks.

Its duty is to supervise balance sheet risks in a systematic manner, to ensure that appropriate controls exist, to approve on an annual basis the main management rules and limits included in the supervision framework and to regularly monitor each behaviour assumption and the interest rate liquidity and foreign exchange risk positions.

Any incidents observed during structural interest rate, liquidity and forex risk management processes and the corrective measures taken are presented to the Balance Sheet ALCO on a quarterly basis.

HSBC France analyses a number of indicators each month on a consolidated basis, allowing for effective monitoring of interest rate risk (including static gaps, calculating the sensitivity of results, stress scenarios etc.). The DGFB coordinates the work of the TALCO Committee which meets monthly to supervise structural interest-rate risk management in the Commercial Banking retail businesses. The TALCO meeting minutes and all the above mentioned interest-rate risk indicators are submitted monthly to Balance Sheet ALCO for approval.

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### Interest-rate risk measurement and supervision system (and methods)

The interest-rate risk assessment process is performed monthly and is based on Commercial Banking businesses interest rate gap analysis. Each month, a gap is calculated reflecting assumptions on changes in assets and liabilities, based on which hedges are set up.

Indeed, on the basis of information produced indirectly by the central systems and/or reports provided by the entities, DGFB measures monthly and supervises structural interest-rate risk on an individual entity basis, where the risk is significant and on a consolidated basis for the other entities. Centralising the process enables DGFB to manage risk in the best way possible and to lay down rules for transferring this risk to the department responsible for markets activities (Global Markets).

The net interest rate risk exposure is transferred to dedicated trading books managed by the trading room through a series of internal deals (cash or swap) between the business units and the trading room. Net exposure is managed through the use of derivatives to close the market positions. The breakdown of derivative instruments by types of contract used is set out in Note 13 of the Consolidated financial statements<sup>1</sup>.

The structural interest-rate risk management model sets out a framework of operational limits to be adhered to in deciding upon new hedging transactions. As such, the new gap after hedging must ensure that the staggered residual exposure is kept to within the limits.

A principal management tool for the structural interest-rate risk is the control of the interest-rate sensitivity of the projected net margin under varying interest rate scenarios. In addition, following simulation work carried out to comply with Basel II Pillar 2 requirements on the Economic Value of Equity, each month, HSBC France also measures the impact on equity of an across-the-board rise or fall of 200 basis points.

Risk is measured and hedging transactions are carried out centrally by the DGFB: these activities rely on a set of formalised controls that are certified on a monthly basis. The process for the execution and accounting justification of hedging transactions has been documented, key controls have been identified and certificates drawn up according to the HSBC Group standards, in accordance with the Sarbanes-Oxley Act.

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### Liquidity risk

Liquidity risk is defined as the risk that HSBC France does not have sufficient financial resources to meet its obligations as they fall due, or will access to such resources only at an excessive cost. This risk arises from mismatches in the timing of cash flows. Funding risk (a form of liquidity risk) arises when the liquidity needed to fund illiquid asset positions cannot be obtained on the expected terms and when required.

1 See page 135. The principal accounting policies relating to derivatives are presented in Note 21 of the Consolidated financial statements page 114.

## Risk management (continued)

The objective of the HSBC France's liquidity and funding management framework is to ensure that all foreseeable funding commitments can be met when due, and that access to the wholesale markets is co-ordinated and cost-effective. To this end, HSBC France maintains a diversified funding base comprising core retail and corporate customer deposits and institutional balances. This is augmented with wholesale funding and portfolios of highly liquid assets diversified by maturity which are held to enable HSBC France to respond quickly and smoothly to unforeseen liquidity requirements.

HSBC France maintains strong liquidity positions and manages the liquidity profiles of its assets, liabilities and commitments with the objective of ensuring that its cash flows are balanced appropriately and that all its anticipated obligations can be met when due.

HSBC France adapts its liquidity and funding risk management framework in response to changes in the mix of business that it undertakes, and to changes in the nature of the markets in which it operates. It also seeks to continuously evolve and strengthen its liquidity and funding risk management framework.

HSBC France's liquidity risk is managed centrally by the ALM Department (DGFB) which is part of the Finance Department. The liquidity steering committee, chaired by the DGFB, closely monitors the liquidity risk measuring systems and coordinates short-term management. This committee, which is a sub-committee of the Balance Sheet ALCO, is attended monthly by those responsible for carrying out operations (Balance Sheet Management), preparing reports and monitoring (Finance Department). This committee is tasked with managing liquidity ratios, preparing the funding plan, looking into alternative sources of funding and handling any matters relating to liquidity.

### Policies and procedures

The management of liquidity and funding is primarily undertaken locally in HSBC France in compliance with practices and limits set by the Balance sheet ALCO. It is the HSBC Group's general policy that each banking entity should be self-sufficient when funding its own operations.

Liquidity risk is monitored by tracking a number of indicators which are updated monthly for the liquidity steering committee and for Balance Sheet ALCO. These indicators are as follows:

- monitoring the French liquidity ratio, as required by French regulations;
- producing FSA regulatory reports;
- projecting cash flows per various stress scenarios and considering the level of liquid assets necessary in relation thereto;
- monitoring balance sheet liquidity and advances to core funding ratios against internal and regulatory requirements;
- maintaining a diverse range of funding sources;

- managing the concentration and profile of debt maturities;
- managing contingent liquidity commitment exposures within pre-determined caps;
- maintaining debt financing plans;
- monitoring depositor concentration in order to avoid undue reliance on large individual depositors and ensure a satisfactory overall funding mix; and
- maintaining liquidity and funding contingency plans. These plans identify early indicators of stress conditions and describe actions to be taken in the event of difficulties arising from systemic or other crises, while minimising adverse long-term implications for the business.

### Primary sources of funding<sup>1</sup>

Current accounts and savings deposits payable on demand or at short notice form a significant part of HSBC France's funding, and the HSBC Group places considerable importance on maintaining their stability. For deposits, stability depends upon preserving depositor confidence in the group's capital strength and liquidity, and on competitive and transparent pricing.

HSBC France's participation in the European Central Bank's three-year Long-Term Refinancing Operation (LTRO) falls within the framework of the conservative and cautious financing policy of HSBC France, which prior to the operation respected all of its regulatory and internal ratios. HSBC France subscribed to EUR 5 billion out of a total of EUR 1,012 billion.

Given HSBC France's subscription to the LTRO in the amount of EUR 5 billion, the amount of senior EMTN issues by HSBC France in 2012 was limited to EUR 1.9 billion and was zero until December, when HSBC France issued EUR 0.7 billion in the form of two-year FRNs. At the same time, deposits decreased by EUR 0.7 billion to EUR 23.6 billion at 31 December 2012 compared with EUR 24.3 billion at 31 December 2011.

Pursuant to the objective of diversifying its sources of funding, HSBC France had led in 2011 the transformation of its French Covered Bonds structured programme into HSBC SFH (France), a "Société de Financement de l'Habitat" fully regulated by the ACP. The outstanding amount of "Obligations de Financement de l'Habitat" issued by the structure as of 31 December 2012 stands at EUR 1.9 billion.

### The management of liquidity risk

HSBC France uses a number of major measures to manage liquidity risk, as described below:

#### French regulatory ratio

HSBC France monitors the one month French regulatory ratio, as required by French regulators. Banks are required to maintain this ratio greater than 100 per cent at all times, to make sure that their liquid assets are sufficient to cover their liabilities as they fall due. It is calculated for HSBC France

<sup>1</sup> See the Consolidated financial statements, Note 29 Maturity analysis of financial assets and liabilities page 159.

on a stand alone basis and each subsidiary subject to it makes its own calculation. In 2012, the average liquidity ratio of HSBC France on a stand alone basis was 131 per cent, compared with 122 per cent in 2011.

#### **Advances to core Funding ratio**

HSBC France emphasises the importance of core customer deposits as a source of funds to finance lending to customers, and discourages reliance on short-term professional funding. This is achieved by placing limits on banking entities which restrict their ability to increase loans and advances to customers without corresponding growth in core customer deposits or long term debt funding. This measure is referred to as the “advances to core funding” ratio. Advances to core funding ratio limits are set by the Balance sheet ALCO. The ratio expresses loans and advances to customers as a percentage of the total of core customer deposits and term funding with a remaining term to maturity in excess of one year. HSBC France would meet any unexpected net cash outflows by selling securities and accessing additional funding sources such as interbank or collateralised lending markets. In 2012, the average advances to core funding ratio was 88 per cent, compared with 101 per cent in 2011.

The HSBC Group also uses measures other than the advances to core funding ratio to manage liquidity risk, including projected cash flow scenario analyses.

#### **Stressed one month coverage ratio**

The stressed one month coverage ratio is derived from these scenario analyses, and expresses the stressed cash inflows as a percentage of stressed cash outflows over a one month time horizon. HSBC France is required to target a ratio of 100 per cent or greater. In 2012, the average “stressed one month coverage ratio” was 112 per cent, compared with 107 per cent in 2011.

#### **Projected cash flow scenario analyses**

HSBC France uses a number of standard projected cash flow scenarios designated to model both group-specific and market-wide liquidity crises, in which the rate and timing of deposit withdrawals and drawdowns on committed lending facilities are varied and the ability to access interbank funding and term debt markets and generate funds from assets portfolios is restricted. The appropriateness of the assumptions under each scenario is regularly reviewed. In addition to the HSBC Group’s standard projected cash flow scenarios, HSBC France designed its own scenarios tailored to reflect specific local market conditions, products and funding bases. Limits for cumulative net cash flows under stress scenarios are set for each banking entity.

Both ratio and cash flow limits reflect the local market place, the diversity of funding sources available and the concentration risk from large depositors. Compliance with entity level limits is monitored and reported regularly to the RMM.

#### **Contingent liquidity risk**

In the normal course of business, HSBC France provides customers with committed facilities, including committed backstop lines to conduit vehicles sponsored by the group

and standby facilities to corporate customers. These facilities increase the funding requirements of HSBC France when customers choose to raise drawdown levels over and above their normal utilisation rates. The liquidity risk consequences of increasing levels of drawdown are analysed in the form of projected cash flows under different stress scenarios.

#### **Foreign exchange risk**

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As HSBC France is part of the HSBC Group, its exchange rate positions are limited. Foreign exchange trading positions arising from banking operations are systematically transferred to the trading room which manages exchange rate risk according to the limits set by the Market Risk Forum.

There is also an exchange rate risk on equity due to investments in foreign currency that are not hedged by financing in foreign currency. This exposure, termed as “structural”, corresponds to net investments in subsidiaries, branches or associated companies for which the euro is not the functional currency.

HSBC France’s investments in foreign subsidiaries are small in amount. The structural foreign exchange exposure is mainly linked to these subsidiaries’ profits retained in reserves. This exposure and the sensitivity of capital ratios to variation in exchange rates are monitored by the Balance Sheet ALCO.

HSBC Holdings plc terms this risk as “structural”, and monitors it through exposure and capital adequacy sensitivity indicators calculated by the Finance Department. The analysis of these ratios is presented to the Balance Sheet ALCO on a quarterly basis.

#### **Capital management<sup>1</sup> (audited information except where stated)**

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In compliance with the European Union’s Banking directive, the *Autorité de contrôle prudentiel* (ACP – French banking regulator) requires each bank and banking group to maintain a specific ratio of total capital to risk-weighted assets. Data on capital adequacy are sent to the ACP that lays down the minimum capital adequacy requirements for the HSBC France group.

#### **Governance**

The Board of Directors has the ultimate responsibility of managing HSBC France group’s capital base. A number of committees help the Board of Directors in this role. These are the Executive Committee, the Risk Management Meeting (RMM), the Balance Sheet ALCO, the Capital Management Committee (CMC). The governance and supervision of resilience tests committee (SOC) was merged with the CMC in 2012. The Finance Department co-ordinates the various aspects of capital management. These are regulatory reporting, capital adequacy planning, assessment of resilience to stresses and management of sources of capital.

1 See the Consolidated financial statements, Note 33 Risk cover and regulatory ratios page 178, and Note 28 Fair value of financial instruments page 153.

## Risk management (continued)

### Methods

The HSBC France group's capital resources policy is to conserve its capital base through the diversification of its sources of capital and an efficient allocation of capital. The HSBC Group ensures that at all times it maintains a prudent relationship between its total capital, as measured according to the criteria used by the ACP for supervisory purposes, and the varied risks of its business.

### Regulatory capital

The HSBC France group capital is divided into two tiers. Tier 1 capital comprises only common equity as no hybrid securities eligible for inclusion in additional Tier 1 capital have been issued by the HSBC France group. Core Tier 1 capital is comprised of shareholders' funds attributable to the group and minority interests, after adjusting for items reflected in shareholders' funds which are treated differently for the purposes of capital adequacy (mainly cash flow hedge reserves, reserves arising from revaluation of property, unrealised gains arising on the fair valuation of instruments held as available-for-sale and the credit spread on HSBC France's own debt). The book values of goodwill and intangible assets are deducted from Tier 1 capital.

Tier 2 capital, in addition to qualifying subordinated loans, is comprised of part of the property revaluation reserves and part of the unrealised gains on the fair valuation of instruments held as available-for-sale. To calculate the total amount of regulatory capital, the carrying value of financial investments in banks is deducted from these two categories of capital, plus any items specified by regulations.

### Regulatory capital requirements

#### *Pillar 1*

Basel II provides three approaches for the calculation of Pillar 1 credit risk capital requirements. The standardised approach requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties, and groups other counterparties into broad categories to which it applies risk type weightings. The Internal Ratings-Based ("IRB") foundation approach, allows banks to calculate their credit risk regulatory capital requirement on the basis of their internal assessment of the probability that a counterparty will default (Probability of Default, "PD"), with quantification of Exposure At Default ("EAD") and an estimate of loss in the event of default (Loss Given Default, "LGD"), the two latter being subject to standard supervisory parameters. Lastly, the advanced IRB approach allows banks to use their own internal assessment of not only PD, but also the quantification of EAD and LGD. Expected losses are calculated by multiplying EAD by PD and LGD. The capital requirement under the IRB approach is intended to cover unexpected losses and is derived from a formula specified in the regulatory rules, which incorporates these factors and other variables such as maturity and correlation.

To measure its credit risk, with the approval of the ACP, the HSBC France group has used the advanced IRB approach for sovereign risk in relation to banks and retail clients since late 2007. As of 2009, HSBC France received approval from the ACP to use the advanced IRB approach for Commercial

Banking clients (LGD in 2009, EAD in 2012). Only some residual exposures are still measured using the foundation or standard approach as an exception.

Market risks are measured, with ACP approval, using Value at Risk (VaR) models or standard rules laid down by the ACP. As regards the counterparty risk, four calculation approaches are defined by Basel II to determine exposure values: the standardised method, mark to market, initial risk and internal model methods.

The HSBC France group uses internal models based on VaR to calculate capital requirements for market risk, and the mark to market approach for counterparty credit risk.

Basel II also introduced capital requirements for operational risk which, again, contains three levels of sophistication. The capital required under the foundation approach is a simple percentage of income, whereas under the standardised approach banks apply three different percentages of income according to each of eight business lines defined by the regulations. Lastly, the advanced approach uses the banks' own statistical analysis and operational risk data modelling to determine capital adequacy requirements. The HSBC France group has adopted the standardised approach.

#### *Pillar 2*

The second pillar of Basel II (Supervisory Review and Evaluation Process) involves both banks and regulators taking a view on whether a bank should hold additional capital against risks not covered in Pillar 1. Part of the Pillar 2 process is the Internal Capital Adequacy Assessment Process (ICAAP), which is the bank's self assessment of risks not captured by Pillar 1. A report on this assessment, regularly updated, is made to the ACP.

#### *Pillar 3*

Pillar 3 of Basel II is related to market discipline and aims to make banks more transparent by requiring them to publish more details on their risks, capital and risk management. The HSBC Group does not publish its own set of Pillar 3 disclosures in France but these are included in the disclosures that HSBC Holdings plc makes available on the investor relations section of its website.

### Regulatory changes

Regulations moved into a new phase in late 2011 with the introduction of "stressed value at risk" for the calculation of market risks under CRD3 (Basel 2.5). The HSBC France group took into account the impact of this change at end-2011.

### Resilience testing

The resilience testing exercises required by the supervisory authorities assess the impact on capital and liquidity of very adverse but plausible scenarios, and so come up with measures to mitigate these effects. They are also a tool that the bank's management can use in its task of managing capital and liquidity, to enable it to consider corrective measures if the early signs of such scenarios emerge. The testing programme carried out by HSBC France in 2012 includes certain specific scenarios required by Senior Management, the HSBC Group or its supervisory authority (Financial Services Authority).



## Regulatory capital position

The table below sets out the analysis of regulatory capital:

### Composition of regulatory capital

(in millions of euros)

|   | 2012   | 2011   |
|---|--------|--------|
| <b>Tier 1:</b>  |        |        |
| Shareholders' funds of the parent company   | 5,213  | 4,820  |
| Non-controlling interests   | 48     | 48     |
| Less: dividends to be paid to the parent company  | (240)  | –      |
| Less: items treated differently for the purposes of capital adequacy                                | (153)  | (192)  |
| Less: goodwill capitalised and intangible assets  | (363)  | (364)  |
| Less: deductions in respect of expected losses  | (64)   | (75)   |
| Less: investments in credit institutions exceeding 10% of capital                                   | (309)  | (305)  |
| Total qualifying Tier 1 capital   | 4,133  | 3,932  |
| <b>Tier 2:</b>  |        |        |
| Reserves arising from revaluation of property and unrealised gains on available-for-sale securities | 44     | 54     |
| Perpetual subordinated loan and term subordinated loan  | 55     | 88     |
| Less: deductions in respect of expected losses  | (64)   | (75)   |
| Less: investments in credit institutions exceeding 10% of capital                                   | (35)   | (67)   |
| Total qualifying Tier 2 capital   | –      | –      |
| Total qualifying Tier 3 capital   | –      | –      |
| Investments in other banks and other financial institutions   | (5)    | (4)    |
| Other deductions  | –      | –      |
| Total capital   | 4,128  | 3,928  |
| Total risk-weighted assets (unaudited)  | 32,673 | 36,889 |
| Total risk-weighted assets before the additional requirement due to the floor (unaudited)           | 30,501 | 36,889 |
| <b>Capital ratios: (unaudited)</b>  |        |        |
| Total capital   | 12.6%  | 10.7%  |
| Tier 1 capital  | 12.6%  | 10.7%  |
| Tier 1 capital before the additional requirement due to the floor                                   | 13.5%  | 10.7%  |

The above figures were computed in accordance with the EU banking consolidation directive and the ACP prudential standards. The group complied with the ACP's capital adequacy requirements throughout 2012 and 2011.

In 2008, HSBC France granted a EUR 650 million subordinated loan to HSBC Bank plc and as a result, the 10 per cent of capital limit for such investments was exceeded; at 31 December 2012, EUR 309 million was deducted from Tier 1 capital (EUR 305 million at 31 December 2011) and EUR 35 million from Tier 2 capital (EUR 67 million at 31 December 2011).

#### Tier 1

Taking into account the impact of the deduction of Expected Loss under Basel II and the deduction of investments in banks in excess of 10 per cent of capital, the net variation results mainly from the profit of the year redeemed by the variation of the credit spread on own debt that is EUR 242 million less interim dividends of EUR 240 million.

#### Tier 2

Taking into account the impact of the deduction of Expected Loss under Basel II and the deduction of investments in banks in excess of 10 per cent of capital, Tier 2 capital decreased mainly due to the discount to the subordinated debt equalling EUR 33 million.

#### Risk-weighted assets

The fall in risk-weighted assets is mainly due to the decrease of market risk.

In 2012, the floor led to an additional requirement of EUR 2.2 billion of risk weighted assets.

## Risk management (continued)

### OPERATIONAL RISKS

Operational risk is the risk of losses arising from shortcomings or failings attributable to internal processes, employees, IT systems or external events including those that are unlikely to occur but which present a significant risk of loss, including the risks of internal and external fraud.

#### Identification and management of operational risks

##### Governance

The operational risk management framework is the responsibility of a Central team: the Operational Risk and Internal Control Department (DCIRO).

This department, which reports to the Deputy CEO in charge of risks and permanent control, centralises work relating to the operational risk management and supervision of permanent control framework.

The operational risk management and control framework is structured into ten risk functions. The supervision of the main risk functions is set out above and below. The management of the risk of non-compliance and the accounting risk control framework are described in the Chairman's report on pages 46 to 49.

Within this framework, a specific Operational Risk and Internal Control (ORIC) Committee conducts, for the entire HSBC France group, regular reviews of business lines and risk functions, operational risks, the results of controls carried out, and progress made in action plans implemented to mitigate identified risks and operational losses.

ORIC or BRCM (Business Risk and Control Management) Committees within the business lines and risk functions are responsible for overseeing management of the operational risks and permanent controls of each entity.

The HSBC France group has procedures covering the process for the identification, reporting, management, control and prevention of operational risks, specifying in particular that:

- operational risk management is first and foremost the responsibility of managers through how they run their operations;
- IT systems are used to identify and report operational risks and generate regular and appropriate reports;
- identification and assessment of risks and controls across the entire scope are updated at least once a year in order to identify any significant changes;
- operational losses are collated and reported.

The HSBC Group uses the standardised approach for calculating the regulatory capital needed to cover operational risks. To estimate economic capital, the HSBC Group uses the same concept, but as applied to certain specific businesses in the HSBC Group's structure instead of the eight business lines of the regulatory approach.

The HSBC Group has, however, started work centrally on developing an economic capital model. The HSBC Group is planning in the medium term to make an eventual transition to the advanced method (AMA) for calculating the regulatory capital required to cover operational risks.

#### Identification and risk measurement through risk and controls mapping

HSBC France and its businesses are exposed to all the types of operational risks that banks face, particularly:

- risk of mistakes in processing transactions, particularly market transactions;
- risk of fraud, internal and external (in particular Internet fraud, fraudulent transfers, bank card fraud, etc.);
- risk related to information security;
- risk related to customer relations.

Business-line internal control and operational risk management teams (Business Risk and Control Management) coordinate work, within their entities, to identify operational risks liable to affect their business. In conjunction with the business head concerned, they analyse and quantify those risks. This risk map covers the whole operational risks exposure of the business including the first and second level of key controls required to monitor these risks. Action plans are drawn up for all risks identified as significant according to its grading, and progress made is monitored by business-line internal control and operational risk management teams.

Each risk function also lists the risks for which it is responsible and to which it is exposed in its day-to-day operations.

To prepare risk maps, internal control and operational risk management teams in the businesses and functions comply in particular with the provisions of the Operations FIM Group manual using, where appropriate, a process-based approach.

Operational risk and incident analyses and reports DCIRO prepares monthly reports for the HSBC France and HSBC Group Senior Management, and presents summary reports to the relevant bodies (the HSBC France ORIC Committee, Risk Management Meeting, and the Audit and Risk Committee).

These reports in particular cover:

- an executive summary explaining movements on losses over the past period and the principles of the operational risks management framework;
- a “heat map” covering indicators of exposure to each type of operational risk (i.e. excluding credit and market risk) accompanied by a description of the main problems and associated action plans for the main types of risk (Top Existing Risks);
- the main incidents in the past period and the associated action plans.

Reporting statements are prepared on the basis of declarations made in the HSBC Group's incident management system, Orion, which should ultimately constitute an Enterprise Risk Management (ERM) tool. This application allows for decentralised management of the risk identification and updating process, declarations of operating losses and the monitoring of action plans decided with a view to mitigating the criticality of risks deemed to be major.

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## Legal risks and potential litigation

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The HSBC France Legal Department (DAJ) is responsible for the HSBC France group's legal function, and has analysed and mapped this function's major risks.

This department helps the various HSBC France group businesses to prevent and control legal risk and is in charge of litigation follow-up.

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### Prevention of legal risks

The DAJ is responsible for running the Legal and Tax Risks Committee. This meets quarterly to examine situations likely to give rise to specific and significant legal or tax risks. It also runs the Complex and Structured Transactions Committee, which examines the legal, accounting, tax and financial, and reputational risks arising from complex structured transactions. The DAJ is also involved in the Products Examination and ORIC (Operational Risk and Internal Control) Committees, in the RMM (Risk Management Meeting) of the HSBC France group, and in due diligence procedures for market operations, structured transactions and any new acquisition (or disposal) of an entity by the HSBC France group.

The DAJ is responsible for managing risks, directly or indirectly, connected with all contentious matters. It is involved in dealing with credit files requiring special management or in default. It also monitors other risks that might have a legal impact.

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### Control framework of legal risk

The Legal and Tax Risks Committee, chaired by the Deputy CEO in charge of risks, meets quarterly to ensure that the risks framework for legal and tax risks remains adequate in the face of changes in laws, regulations and organisations. The committee also examines the monitoring of incidents raised previously, the results of controls, along with any new incidents and measures taken. It reports on its activities to the HSBC France group ORIC Committee.

Each HSBC France subsidiary that is directly affected by regulation 97-02 draws up a half-yearly legal permanent control report, signed by a lawyer and the Head of permanent control of the subsidiary for itself and the companies it controls. These reports highlight any significant matters revealed by controls, or any control deficiencies and proposed action plans to resolve any incidents observed during controls.

At the HSBC France level, the corporate lawyers responsible for legal risk in the various business lines prepare continuous legal control certifications which, taken as a whole, cover all major legal risks identified for all HSBC France entities in their entirety.

On the basis of these reports, HSBC France's Head of Legal prepares a half-yearly general certification on the Legal Function's permanent control.

The whole of this framework is effective and a detailed description of it is given in a regularly updated circular.

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### Litigation monitoring<sup>1</sup>

The situation of the risks arising from significant litigation in progress against the HSBC France group is examined quarterly. It is examined by a committee chaired by the Deputy CEO in charge of risks and is made up of representatives of the Finance Department, the Credit Department and the DAJ. This committee gives a considered opinion on the basis of which Senior Management decides upon the amount of the provision to be charged or written back.

Cases in progress at 31 December 2012 involving legal risks likely to have an adverse influence on the HSBC France group net assets are set out below.

### Interbank fees relating to electronic cheque processing ("CEIC")

In 2002, a number of banks with retail networks, including HSBC France, forming part of an inter-branch committee sponsored by the French Banking Federation, introduced a system of interbank fees applying to the new electronic cheque processing termed the "*Echange d'Images Chèques*" (EIC), the cheque image exchange system.

In March 2008, the French Competition Authority sent notification of a complaint to the twelve members of the committee – including HSBC France – for the introduction of interbank fees when the EIC was set up.

On 20 September 2010, the French Competition Authority took an unfavourable decision as regards the scheme introduced in 2002. In substance, it found that the CEIC constituted an illegal scheme, the purpose of which included effects on the cost of processing cheques causing an increase in costs charged on "major remitter" customers. The banks involved in setting up this charging system were fined a total of EUR 384.9 million. HSBC France was ordered to pay a fine of EUR 9.05 million. HSBC France, together with the other banks that were fined, except the Bank of France, decided to appeal this unfavourable decision.

The banks actually contest as much the purpose as the anticompetitive effect of the CEIC and argue that it has no significant effect on the costs of banking services. The banks and HSBC France in particular further question the method used in calculating the fines imposed upon them.

<sup>1</sup> See the Consolidated financial statements, Note 36 Litigation page 180.

## Risk management (continued)

On 23 February 2012, the Paris Court of Appeal overturned the decision of the French Competition Authority, finding that the authority had failed to demonstrate a restriction by subject. The Paris Court of Appeal cleared the banks of wrongdoing and ordered the repayment of fines paid by the banks. The French Competition Authority is appealing to the Court of Cassation against the decision.

### Enquiry by the French Competition Authorities on the interbank fees relating to all means of payment other than cheques

On 16 April 2009 and 22 September 2010, HSBC France along with some ten other banks and the GIE Cartes Bancaires received questionnaires from the French Competition Authority on the interbank fees applied to means of payments used in France. This followed a complaint made by the *Fédération des Entreprises du Commerce et de la Distribution* (FCD) due to the existence, or due to levels considered excessive, of multilateral or bilateral interbank commissions related to the usage of means of payment. The French Competition Authority decided to conduct research into the practices of the largest French banks and bank card networks operating in France (Visa Europe, Mastercard Europe SPRL, Mastercard France, Mastercard International Inc., the GIE Cartes Bancaires CB and the GIE Carte Bleue Visa) on interbank fees paid and received for all means of payment used in France (direct debits, transfers, debit and credit cards) between 2000 and 2008.

The French Competition Authority, having expressed, “competition concerns,” with regard to the GIE Cartes Bancaires, in light of the replies to the questionnaires as much from the GIE as from the banks, accepted the opening of commitment proceedings.

On 7 July 2011, the Competition Authority announced its decision to make the commitments proposed by the GIE Cartes Bancaires CB under this procedure mandatory. To our knowledge, no appeal has been made against this decision.

As regards interbank fees applied to payment methods other than cheques and cards, the French Competition Authority agreed to an undertakings procedure.

On 14 March 2012, it set out its competition concerns and in response to those concerns, the banks have drawn up a draft set of undertakings.

### The Apollonia case

As about twenty banks, HSBC was led to work during a limited period of time (from early 2006 to April 2007) and mainly in one branch, with a financial adviser and estate agent, Apollonia. The latter offered its clients (mainly independent professionals) “turnkey” tax efficient products of the “*Loueur Meublé Professionnel* (LMP)” (professional lessor of furnished accommodations) type and for a small number of investors “*Loi Robien*” type tax efficient products.

Between April 2006 and April 2007, 184 property loan applications were approved, for a total of EUR 29 million, bearing in mind that different media have said the total amount of operations by Apollonia with all banks would be around EUR 2 billion.

At the end of September 2008, HSBC France became aware of the use of reprehensible marketing methods by Apollonia. Moreover, it appeared that most of the borrowers took out several loans through Apollonia from various banks without notifying HSBC France.

Five notaries have been indicted for conspiracy to commit organised fraud, forgery and use of forgeries. HSBC France is involved as a civil law party, giving it access to the criminal file. From this, it has become apparent that a very large proportion of the official agency authorisations, signed by the buyers giving authority to sign purchase and sales deeds, were not properly prepared.

HSBC France systematically brings proceedings against those investors with loan repayments due but the hearings are in abeyance because of the criminal procedure underway. However, in order to settle the financial aspects of the matter, without waiting for the outcome of criminal proceedings, out-of-court settlements have already been reached with some borrowers and talks are continuing with other borrowers. Proceedings have also been commenced against the notaries involved and their insurer MMA. These proceedings have also been adjourned.

Adequate provisions have been recorded for the Apollonia case in the light of information available to Senior Management.

### Euribor enquiry

In October 2011, the European Commission carried out unannounced on-site inspections of several banks, including HSBC France, operating in Euribor (Euro Interbank Offered Rate) derivatives. The European Commission suspects that employees of the banks in question may have infringed European laws prohibiting anti-competitive collusion and commercial practices that restrict competition, through the possible co-ordination of daily information used to calculate Euribor. On the same matter, HSBC France has received requests for information from the *Autorité des Marchés Financiers* and the US Commodities and Futures Trading Commission (CFTC). HSBC France is providing all appropriate co-operation, and is not currently able to foresee the potential outcome of these enquiries given the current state of information.

To date, as far as HSBC France is aware, it is not threatened by any other regulatory, civil law or arbitration proceedings that are in progress or in suspense against it that might have, or over the last 12 months have had, any significant effect on the financial situation or the profitability of the company and/or of the group.

### Tax risk

The HSBC France Tax Department (DAF), which is responsible for the HSBC France group tax risk function, was set up at the beginning of 2010 by splitting the former Legal and Tax Department. It reports directly to the Deputy CEO in charge of risks.

This department assists HSBC France’s various business lines, along with its subsidiaries, to prevent and control tax risks. The department has analysed the major risks in the function and has mapped them.

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### Prevention of tax risks

The DAF attends to the Legal and Tax Risks Committee, which is run by the DAJ, and also to the HSBC France group Complex and Structured Transactions Committee, the Product Examination Committee, and the ORIC (Operational Risk and Internal Control) and RMM (Risk Management Meeting) Committees.

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### Tax risk monitoring system

Each of HSBC France's subsidiaries, directly covered by regulation 97-02, prepares tax certificates half-yearly for itself and for the companies that it controls.

On the basis of these certifications, HSBC France's Head of Tax Affairs confirms HSBC France's tax compliance to the HSBC Group twice a year.

The whole of this framework is operational and a detailed description of it is given in a circular.

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### IT Systems Risk

#### IT risk management

IT risk has consequences on three levels:

- operational: even if the activity is not directly based on an IT process, closure of the IT service generally results in a shutoff or slowdown in the bank's production;
- financial: IT expenditure (hardware, software, know-how) constitutes a significant proportion of the bank's assets;
- legal: regulations require oversight of the security of the IT system (*Loi Informatique et Libertés*, LCEN, SOX Act, LSF, etc.).

IT risks are assessed using the HSBC Group's RCA methodology. Control of these risks is based on a governance and organisational structure meeting Group standards and best practice guidelines (CMM, ITIL, COBIT).

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### Missions and coverage

HSBC France's IT Department forms part of the global function HSBC Technology and Services (HTS). It relies on the following teams to support the IT services provided by HTS to the business lines, central departments and other HTS departments:

- Risk and Control Administration (RCA), responsible for management of operating risk within the tolerated thresholds;
- Change Delivery (CD), responsible for management of major organisational change programmes;
- IT Operations (ITO), responsible for the implementation and maintenance of infrastructures;
- Software Delivery (SwD), responsible for the development and maintenance of software solutions.

The missions of the IT function are covered by the following HSBC Group manuals:

- Group Standard Manual (GSM): 10.6 Information Technology;

- Functional Instruction Manual (FIM IT).

The IT risk function aims to implement an IT risk reduction strategy that is consistent with the information system strategy. This strategy also aims to meet the information system's confidentiality, integrity and availability requirements with respect to the bank's business lines. IT risk management often involves standard arrangements such as the IT Recovery Plan (IRP), data back-up and the Business Recovery Plan (BRP). However, it is also more extensive, since it requires implementation of the HSBC Group's risk assessment methodology, which is handled in France by the Internal Control and Operational Risks Department (DCIRO), and the preparation of a risk management plan commensurate with the potential financial damage.

Some risks are managed through the Business Recovery Plan and the IT Recovery Plan, but the issues involved in any IT organisation mean that other risks need to be managed, such as:

- failure to comply with legal obligations;
- human and programming errors;
- loss of expertise relating to projects and/or technologies;
- unavailability of the information system when new developments or new third-party solutions are implemented;
- system and/or code vulnerabilities;
- outsourcing of sensitive functions and processes;
- loss of or damage to audit trails;
- failure of key suppliers in the regulatory sense;
- internal or external fraud.

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### The IT function's permanent control system

The IT function's permanent control unit is part of Internal Control, which itself reports to the General Secretariat of HSBC Technology and Services (HTS).

The identification of all potential risks and control objectives in the IT Function complies with the COBIT method. To reflect the Group's organisational structure, IT risks are identified around three mapped departments, namely CD, ITO and SwD.

The assessment of IT risk is revised annually. As part of this organisation, the IT Function's permanent control unit lists IT risks and co-ordinates the key controls required to manage each risk, with the support of department managers, who remain responsible for first-level controls on operational processes and who must apply the key controls identified.

The IT Function's permanent control information (results of control reviews, progress with the control plan, change in risk reviews and control assessments, any failures and remedial actions taken) are communicated monthly to HTS' governance body (Comex) and quarterly to the IT risk function's governance body (HTS BRCM IT Committee). Permanent control work and results are also reported monthly in the Risk Management Meeting (RMM) and quarterly in central ORIC Committee meetings.

## Risk management (continued)

In addition to comply with the US Sarbanes-Oxley Act, the HSBC Group has set up a permanent control documentation and assessment framework, co-ordinated by the Finance Department, relating to the IT processes involved in preparing financial statements.

### Risk monitoring

The IT risk function prepares a control plan on an annual basis. This plan sets out the key control monitoring activities that are performed annually. To ensure that it remains relevant, it is reviewed and updated on an ongoing basis depending on changes in the IT Function.

The results of risk assessments and controls form the basis of the annual control plan. It is approved annually through an appropriate governance procedure, validated by the HTS RCA owner.

Any major IT problem identified through control monitoring is reported to HTS' permanent control management and HSBC France's permanent control supervision department (DCIRO).

### Information security policy

The information security policy includes information both in electronic and paper format, and must cover technological, organisational and human risks.

Risks relating to information security are a central concern of the HSBC Group and HSBC in France. To reduce risks in this area, numerous directives have been adopted over the last few years and all HSBC France employees are reminded of them on a regular basis.

The security measures applicable within the HSBC Group are laid out in a set of standards, made up of various documents such as the Functional Instruction Manuals (FIM) and the Security Secondary Standards. These standards apply to all HSBC France employees and are based on industry best practice, unless they are more restrictive. Each entity, business or department is responsible for applying the standards and incorporating them into the everyday work of its employees.

Monitoring and governance of IT systems security risk are the responsibility of the Information Security Risk team (ISR). This team reports to the Security and Fraud Risk department (SFR), under the responsibility of the Chief Risk Officer.

ISR's objectives are particularly:

- to monitor the data security risks borne by the bank;
- to reduce security risks to an acceptable and/or accepted level by the Senior Management (notion of risk appetite);
- to safeguard the HSBC brand and its reputation;
- to minimise losses arising from the security incidents;
- to ensure that security measures are consistent throughout all entities.

To achieve these objectives, it is necessary to:

- lay down the data security requirements in local policies and procedures;
- to ensure that everyone knows the data security requirements and that the business lines incorporate the data security requirements in their day-to-day work;
- to co-ordinate the activities of Business Information Risk Officers (BIRO), who are the business-line representatives of ISR and are tasked with implementing security policies within business lines;
- deploy secondary lines of defences for ensuring that the bank is compliant with the HSBC Group's safety standards;
- to provide "expert" assistance on ISR matters to all entities.

The various ISR activities are intended to ensure the integrity and confidentiality of information belonging to HSBC and its clients:

- checks of management of user access to the bank's applications and operating systems, and the password management policy;
- application security, to ensure that applications used within the company have been developed in accordance with the rules and comply with the bank's security policies;
- business-line controls, to ensure that business lines comply with Group policy regarding the treatment of sensitive data, supported by BIROs;
- infrastructure security, involving penetration tests and work to ensure the security level of the bank's technical infrastructure;
- risks relating to service providers, involving checks that the services HSBC entrusts to certain partners are performed with the required level of safety;
- incidents and threats, involving work to manage threats within HSBC France and any security incidents, including the preparation and monitoring of remedial action plans;
- communication and training, involving the preparation of annual communication and training plans and their implementation.

### Fraud prevention

Within the Security and Fraud Risk (SFR), the anti-fraud unit's main task is to ensure that the measures for protecting the group against internal and external fraud are comprehensive, efficient and appropriate.

This involves:

- preventative action, incorporating special anti-fraud controls into procedures identified as sensitive to the risk of fraud;
- detection work, using software or reports for detecting fraud;
- investigation or enquiry work where internal or external fraud is identified.

In terms of governance, fraud prevention requires coordination between all parties involved: businesses, internal control and operational risk management teams, Compliance, Credit and Human Resources. For this purpose, a SFR representative sits in on business-line BRCM Committee meetings. As regards frauds designated as major, there is a fraud response group that meets in exceptional circumstances, such as in the event of internal fraud or targeted attacks on HSBC France client Internet platforms.

Amongst the activities carried out regularly within the unit are:

- involvement at an early stage in installing systems and designing processes to cut down vulnerability to fraud;
- making employees and clients more aware of fraud;
- analysing trends in fraud and the ways in which it is carried out, as well as gathering information;
- investigations on the basis of reports received, alerts generated by systems or other detection methods;
- funds recovery actions;
- support in instigating legal proceedings;
- monitoring corrective actions taken on detecting a fraud.

Amongst the priority areas covered within this unit are systems, procedures and controls relating to:

- recruitment of permanent or temporary employees, including service providers;
- client identification and authentication, whatever the service channel: Internet, branches, call centres, mobiles;
- the collection and update of sensitive customer information in databases;
- instructions in connection with means of payment;
- opening accounts by means of any of the service channels, in cooperation with Compliance and Credit Risk Departments;
- the existence of the segregation of duties principle and of traceability of transactions to deter internal frauds by whatever process.

Following on from the measures taken in 2011, the focus in 2012 was on the prevention and detection of Internet frauds (viruses or remote account access), with the monitoring of suspicious client connections with software allowing high-level surveillance of the behaviour of client connections.

Rogue trading and counterparty fraud are covered by the Global Banking and Markets control units and therefore do not fall directly within the anti-fraud unit remit. Instead, it becomes involved at the stage of investigation when an internal fraud has been detected or is suspected in connection with counterparty risk.

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### 2012 cost of fraud report

The total for internal and external frauds (excluding bank cards) represents around 25 per cent of the total of typical operational losses, *i.e.* EUR 4.9 million. This total has risen as a result of client frauds such as credit frauds, which are better identified and clearly marked out from credit risk itself. The number of cases in the year remained more or less constant at around 1,000, of which 250 were frauds and 750 attempted frauds.

### Frauds carried out by customers

Frauds carried out by customers are defined as the customer's deliberate intention to deceive the bank by any means, such as false discounted bills, drawings made after the depositing of dishonoured cheques or bills, and loans obtained on the basis of false documents.

In 2012, these frauds represented around EUR 3.1 million.

### External frauds

These are frauds committed by third parties against customers' accounts or against the bank: opening an account with identity dissimulation, identity theft, presenting falsified or fake cheques, fake payment transfers.

In 2012, these frauds represented around 15 per cent by amount. Losses attributable to fake transfers decreased significantly thanks to observance of the call back procedure.

Losses caused by an Internet virus increased in terms of both the number of cases and the amount. Furthermore, as the Internet and online banking present a high risk of fraud, the anti-fraud unit is closely involved in the implementation of new customer authentication systems and management of Internet fraud.

### Internal frauds

These are frauds committed by employees with or without outside complicity, including frauds committed by HSBC service providers and HSBC temporary staff.

In 2012, these frauds represented around 2 per cent of typical operational losses with a significant fraud at the beginning of the year.

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## Business continuity

### The Recovery Plan

The purpose of the Business Recovery Plan (BRP) is to ensure that business can carry on or continue to run at the minimum level considered necessary to safeguard the interests of the business, its employees and its customers, in the event of a major disaster or disruption likely to have a significant impact on the business of HSBC France and/or of its subsidiaries, or to produce a significant deterioration in the image of the business.

## Risk management (continued)

The HSBC Group's Operations FIM (Functional Instruction Manual) specifies that: "Each department or business unit should devise a business recovery plan that takes account of the risks for their business activities, analysis of the impact, requirements in terms of resources etc., resulting in the creation of a business continuity management plan that needs to be updated, tested and approved by management at least once a year (and more frequently if major changes occur). This plan must describe how ordinary activity can resume after an adverse event or an interruption to business activity".

A list of four types of business interruption is proposed in the FIM:

- loss of premises (e.g. fire, flooding, blocked access, etc.);
- loss of personnel (e.g. contagious disease, etc.);
- loss of systems (e.g. IT virus, shutdown of central systems, etc.);
- loss of supplier and critical internal dependence.

These various kinds of interruption have been used in analysing the impact prior to the implementation of HSBC France's Business Recovery Plans.

These four types of business interruption can be used to cover the following FBF scenarios:

- centennial floods (under review);
- accidents, nuclear, radio, biological, and chemical attacks;
- health risks (under review);
- multiple bomb attacks;
- widespread electricity breakdown;
- general transport strike;
- service provider failure;
- cyber attack consequences.

The HSBC Group standards (GSM section 10.5 and Operations FIM) provide that each department or entity must have at the minimum a business recovery plan which is kept updated and which is tested at least annually (more frequently in the event of major changes). The plan must describe how normal activity is to be resumed after a major incident.

Regulation 97-02 requires that each main establishment should lay down a business recovery plan which should be updated and should be tested at least once a year.

Because of the size of HSBC in France and the large number of its geographical locations and businesses to be covered, each business, department, subsidiary and central function has prepared a Business Recovery Plan appropriate to its business according to its assessment of the risk of the unavailability of a property and also of the absence of all or some of its employees, an IT system or an internal or external service provider.

Within each unit and depending on their size, a BRP correspondent (coordinator) – who may be dedicated or not – is appointed by name. The correspondent reports to a

named manager (RPCA, Champion or Sponsor) and is in charge of the general coordination of the framework within the entity. He organises and supervises the implementation of technical resources and annual tests. He also manages the preparation of or prepares reports on tests and initiates appropriate procedures to make corrections or changes if necessary. He is in charge of communications and methodological support within the entity, keeping the plans and various deliverables, saving them on the space made available by the central team and declaring any measures taken within his entity.

A BRP Editor for each business line has been appointed by name since the end of 2012, reporting on a hierarchical basis to the head of the activity concerned and on a functional basis to the business entity's coordinator. He is in charge of conducting impact analysis (use of group tools) and writing up and revising BRPs.

A central structure for organising and managing these plans (RPCA), located within the Security Department, ensures that the exercise is comprehensive, that the plans are held centrally so as to be accessible by the various departments involved in implementing them, and that the system is consistent throughout.

This central structure is responsible for organising business recovery co-ordination committee meetings and for communicating about organisational, technical and testing strategies.

All important documents, the detailed Business Recovery Plans for departments and subsidiaries, and the necessary technical documents are held in a central "documents database", which can be accessed by authorised employees from all the company's locations. There must nevertheless be a copy of these documents on the secured dedicated space of these entities.

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### The Major Incident Group

Activation of the implementation of BRPs is based on a multi-tiered management system:

- the business line crisis committee if the trigger incident is restricted to just the entity or of limited seriousness;
- a committee at the level of HSBC France's Senior Management called MIG (Major Incident Group).

The MIG can be activated in two ways, depending on the seriousness of the incident and the risk to be covered:

- The level 2 MIG consists of a dozen or so deputies to business line heads or heads of functions covering the cross-functional activities needed to manage a major incident or crisis (Communications – Human Resources – Real Estate – IT – Markets – Operations – Security – Logistics). This committee is chaired by the Chief Risk Officer or Chief Operating Officer (acting), seconded by four dedicated working parties (Communications – Human Resources – Real Estate and IT – Business Continuity). This committee, activated by a cascade warning process initiated by a security post (technical control post (TCP): active 24/7), triggers all or part of the BRP if necessary after analysis.



- The level 3 MIG is made up of business line or function heads and chaired by the CEO of HSBC France and benefits from the same supports.

The detailed structure of MIG and its workgroups, the principles and structure established, the description of the contacts and the escalation process, the contact details of those involved, and the “reflex” files to be implemented in case of activation are contained in a reference document called MIM (Major Incident Manual) which is continuously updated by the HSBC France group SFR/BCM manager. This manual together with a reference card (major incident card) are provided regularly to the members of the crisis system.

Emergency measures are planned to manage incidents as soon as they occur in order to ensure the protection of people, communications, safeguarding and rebuilding of assets.

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#### The resources and fallback site

The HSBC France Management has approved an internal-fallback site solution and authorised the resources for implementing it.

The main special fallback site, located in a Parisian suburb, is fitted with shared, general-use workstations, as well as trading stations.

This secure site is open and accessible to personnel on the decision of MIG at the request of business lines during scheduled tests, validated by the RPCA in the event of a transport strike or during programmed tests. It resembles a normal group operations site and is made up of a number of open plan office areas together with the necessary technical resources (computer terminals, telephones, printers, faxes and special equipment – scanners, specialist readers) to continue carrying out the business activities decided upon in the appendices of the Business Recovery Plans.

In the event of a crisis, priority will be given to Markets, Asset Management, bank transactions processing and non-production IT facilities

All essential activities are covered by Business Recovery Plans.

### Human Resources

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#### Risks relating to Human Resources management and control system

HSBC France’s Human Resources Department is responsible for the permanent control of the Human Resources (HR) risk of the HSBC France group. For this purpose, it has mapped the function’s risks to serve as a basis for the businesses and other risk functions in preparing their own risk maps in terms of risks arising from Human Resources.

In addition, mapping of the risks to which the Department itself is exposed, whether they relate directly to human resources or not, has also been carried out. The document is updated at least once a year and is used in support of the annual control plan.

The internal controller also relies on risk indicators (Operational Risk and People Risk Heat Map), which are distributed monthly at the Risk Management Meeting.

The People Risk Committee was set up in 2009. It meets quarterly to review the continuing appropriateness of the permanent control system of the Human Resources risk function. The members of this committee, other than the main Heads of HSBC France’s Human Resources Department, are the Heads of HSBC France’s subsidiaries’ Human Resources Departments and the Head of the HR Operations Department, which has formed part of HTS Service Delivery and the HR DCIRO correspondent.

The Committee reviews progress on points previously put forward for improvement and unresolved audit points and the results of controls and new plans of action arising from them. It approves the due diligence and results of post-implementation reviews of new processes or products. It ensures that service providers are listed and that the risks relating to the services provided have been assessed. It reports on its work to the HSBC France group’s ORIC Committee.

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#### The committees

##### Role of the HSBC France People Committee

The purpose of the People Committee is to enable the main HSBC France Senior Managers (CEO, Deputy CEO in charge of Global Banking and Markets, Deputy CEO in charge of risks, and the Head of Human Resources), on a monthly basis, to tackle all Human Resources issues of strategic importance, in accordance with the HSBC Group HR policy and developments in it.

On the subject of compensation, the People Committee carries out various roles both on the overall and individual aspects.

##### Compensation policy

It examines the main thrust of the compensation policy put forward by HR for France and approves it.

It ensures that this policy fits in with the general principles of the compensation policy set out by the HSBC Group for all of its subsidiaries, in accordance with the specific directives set by the businesses.

It gives its opinion on whether this policy complies with local industry standards and the recommendations of the French bank supervisory authorities (*Autorité de contrôle prudentiel, Autorité des Marchés Financiers, Fédération Bancaire Française*).

##### Variable compensation arrangements

It checks that all variable compensation arrangements in place in the bank’s various businesses are in line with the general principles set out in the compensation policy for France, the HSBC Group and the global businesses and comply with the requirements of the supervisory authorities.

## Risk management (continued)

It reviews the variable compensation packages awarded either locally or by global businesses to French staff on the basis of the performance of each business line, while taking risk and compliance into account.

It approves the structure of these packages, *i.e.* the split between fixed and variable salary, between immediate compensation and deferred compensation in application of the HSBC Group rules, particularly in connection with deferred compensation and local industry standards on the subject.

### *Individual awards*

It reviews and approves the consistency of remuneration of population covered by the order of 13 December 2010 (except for the members of the People Committee) before submitting them to the appropriate HSBC Group decision-making bodies.

It reviews the business' 20 highest earners (except the members of the People Committee) and also the compensation of the CEOs of the Private Bank and the Asset Management subsidiaries in conjunction with the HSBC Group's decision-making bodies and the global businesses.

It ensures that proposed individual compensation packages take account of any individual failures to meet the bank's credit risk, compliance and reputation criteria.

At the end of the meeting, the Committee prepares a summary of the decisions taken on compensation. This summary is presented at the Nomination and Remuneration Committee of the Board of Directors that follows the "People Committee".

### **Role of the Nomination and Remuneration Committee**

On the basis of a summary produced by the People Committee, the Nomination and Remuneration Committee gives its opinion on the bank's compensation policies and practices, ensuring they are consistent with the HSBC Group policy and that they comply with applicable local standards. It also ensures that risk management and compliance issues are taken into account.

Its scope of responsibility covers all compensation policies and practices in place within the company, with a more in-depth review of market professionals and Executive Directors.

It also reviews the remuneration paid to Executive Directors and submits its recommendations to the Board of Directors.

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### **Role of the Risk and Compliance Functions as regards remuneration policies**

The Risk and Compliance Functions are, in accordance with the HSBC Group rules (Functional Instruction Manual – FIM and Group Standards Manual – GSM) referred to for advice on laying down compensation policies and introducing new variable compensation systems.

Since 2009, situations of failure of compliance and infringements of internal rules of procedure, identified by the Risk and Compliance Functions, have been taken into account when awarding variable compensation.

To strengthen the Risk and Compliance Functions, throughout the year and especially during the annual salary review process when individual variable compensation is decided, certain changes were made in 2010.

On a practical level, these functions are responsible, in their respective fields of operation, for:

- listing, throughout the year, all instances of non-adherence to compliance rules and/or rules of internal procedure and/or rules concerning risk;
- notifying the cases listed to the manager of the business involved or to his deputy and to HSBC France's Head of Compliance;
- advising the HR managers involved of cases observed that are likely to lead to disciplinary proceedings;
- listing and summarising all problems of breaches of compliance regulations and/or internal procedures and/or risk procedures and notifying them to the Head of the Risk Function;
- keeping a record of each of the breaches and any resolution of them;
- if necessary, providing feedback to management for possibly making changes to the "balanced scorecard" of the employees involved in the breaches.

Especially during the salary review process, the Head of Compliance must take part in meetings organised by the HR Department in the presence of the managers concerned and the Deputy CEO in charge of risks, in order to assess the severity of cases on the basis of information reported by risk functions and the business line's summary of that information.

As regards the most significant cases of non-compliance with rules and/or internal procedures, and/or risks as identified during the year, managers and the Deputy CEO in charge of risks must make decisions about:

- the impact (significant, marginal or nil) on the variable compensation of the employees concerned;
- whether the "clawback" rule needs to be applied, cancelling some or all previously awarded shares, depending on the severity of the event.

After these decisions, the HR Department must certify that the managers concerned and HR have made any required adjustments to the variable compensation of the employee concerned.

If the proposed variable compensation requires it (above a certain threshold), risk and compliance functions may be asked to contribute to the preparation of a business case setting out the compliance breach and/or internal rule breach and its impact on variable compensation.

The Head of Human Resources notifies the People Committee of the list of decisions giving a summary of the individual and/or group behaviour that breached internal rules in terms of risk or compliance.

## **Dependency**

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HSBC France is not dependent on any patents, licences or industrial, commercial and financial supply contracts.

## **Insurance and risk coverage**

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The HSBC Group in France is covered by the main global insurance programmes taken out by HSBC Holdings plc in London regarding the coverage of the major risks (fraud, professional liability, directors' and officers' liability).

As regards the specific insurance requirements of its operations and in compliance with French regulations, HSBC France organises local insurance programmes centrally, *via* its Insurance Department, on behalf of the HSBC Group in France. In particular, insurance is used to cover professional liability relating to regulated activities, public liability, banking risks and the fleet of cars, etc.

Generally, the levels of coverage, retentions and excesses are:

- in line with insurance market conditions, business areas, practice and legislation;
- appropriate to the value of the assets and the potential impact on the balance sheets of HSBC France and HSBC Holdings plc.

The total amount of insurance premiums paid in 2012 represented 0.26 per cent of the net operating income of the HSBC France group.

Most of the programmes, notably international, involve the participation of an HSBC Group captive reinsurance subsidiary.

Broker, insurance and expert partners are chosen in accordance with a strict selection and solvency supervision policy, established and controlled by HSBC Insurance Holdings plc.

## Financial highlights\*

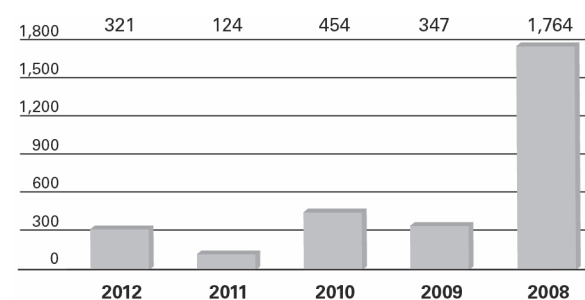
### HSBC France group

| (in millions of euros)   | 2012           | 2011    | 2010    | 2009    | 2008    |
|--|----------------|---------|---------|---------|---------|
| Profit before tax .....  | <b>388</b>     | 59      | 512     | 406     | 1,744   |
| Profit attributable to shareholders.....                                       | <b>321</b>     | 124     | 454     | 347     | 1,764   |
| Profit before tax for the HSBC Group's operations in France <sup>1</sup> ..... | <b>559</b>     | 191     | 628     | 548     | 1,853   |
| At 31 December   |                |         |         |         |         |
| Shareholders' funds.....   | <b>5,213</b>   | 4,820   | 4,832   | 5,060   | 5,228   |
| Loans and advances to customers and banks .....                                | <b>76,486</b>  | 82,984  | 95,291  | 80,485  | 78,556  |
| Customers' accounts and deposits by banks .....                                | <b>75,356</b>  | 75,234  | 86,055  | 90,373  | 95,927  |
| Total assets.....  | <b>225,208</b> | 221,390 | 210,836 | 213,444 | 266,025 |
| Number of employees (full-time equivalents) .....                              | <b>9,570</b>   | 10,030  | 10,121  | 10,350  | 10,886  |
| Capital ratios   |                |         |         |         |         |
| Total capital <sup>2</sup> .....   | <b>12.6%</b>   | 10.7%   | 12.0%   | 12.2%   | 9.6%    |
| Core Tier One capital <sup>2</sup> .....                                       | <b>12.6%</b>   | 10.7%   | 12.1%   | 12.2%   | 9.5%    |
| Cost efficiency ratio .....  | <b>75.9%</b>   | 90.6%   | 73.0%   | 73.9%   | 48.5%   |

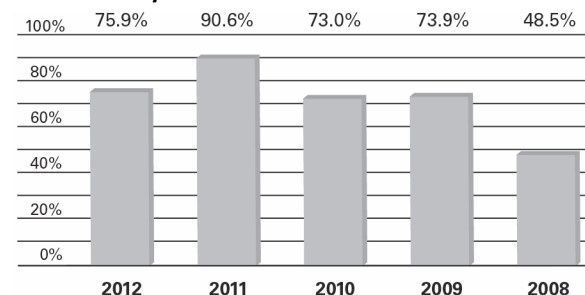
The financial highlights are influenced by changes in the group structure over the five years. The most significant changes are as follows:

- in 2008: disposal by HSBC France of its seven regional banking subsidiaries;
- in 2009: disposal by HSBC France of its equity derivatives business to HSBC Bank plc Paris Branch;
- in 2010: disposal by HSBC France of HSBC Securities Services (France) to CACEIS;
- in 2011: disposal by Sinopia Asset Management of Sinopia Asset Management (Asia Pacific) Limited to HSBC Global Asset Management (Hong Kong) Limited and Sinopia Asset Management (UK) Limited to HSBC Global Asset Management (UK) Limited. Disposal by HSBC Private Bank France of LGI to HSBC Private Bank (Luxembourg) SA.

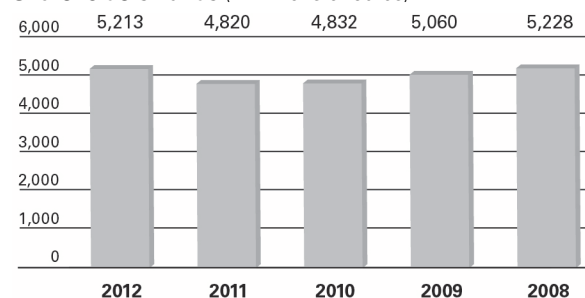
#### Profit attributable to Shareholders (in millions of euros)



#### Cost efficiency ratio



#### Shareholders' funds (in millions of euros)



\* Published consolidated financial information – HSBC France legal perimeter. In accordance with IFRS as endorsed by the EU.

<sup>1</sup> The contribution of France to the results of the HSBC Bank plc operations includes the HSBC France group, i.e. the results of entities legally owned by HSBC France but located outside France, i.e. the legal scope in its entirety, and also the Paris branch of HSBC Bank plc, which is engaged in equity derivative activities, as well as HSBC Assurances Vie (France) and HSBC Assurances IARD (France), to the exclusion of the costs of funding and the debt on acquisition recognised by HSBC Bank plc Paris Branch.

<sup>2</sup> Capital ratios under Basel II from 2008, with an additional requirement due to the Basel I floor in 2012, which increased the risk-weighted assets by EUR 2.2 billion and decreased the Core Tier One capital ratio by 0.9 basis point.

## Ratings

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HSBC France is rated by three main agencies: Standard & Poor's, Moody's and Fitch.

|                            | Standard & Poor's | Moody's         | Fitch            |
|----------------------------|-------------------|-----------------|------------------|
| Long-term rating.....      | AA -              | A1              | AA -             |
| Rating revised on .....    | -                 | -               | 10 December 2012 |
| Rating confirmed on.....   | 23 August 2012    | 1 February 2013 | -                |
| Outlook.....               | Negative          | Stable          | Stable           |
| Outlook revised on.....    | 23 August 2012    | -               | -                |
| Outlook confirmed on ..... | -                 | 1 February 2013 | 10 December 2012 |
| Short-term rating.....     | A-1+              | P-1             | F1+              |

During the year 2012, HSBC France's ratings have been affected by the persistence of a poor macroeconomic environment along with its consequences on the whole financial sector. Moreover, the rating agencies have given more emphasis to regulatory developments and risk concentration. In this context, HSBC France's ratings evolved coherently with those of its parent company HSBC Bank plc.

## Consolidated financial statements

### Consolidated income statement for the year ended 31 December 2012

| <i>(in millions of euros)</i>   | <i>Notes</i> | <b>31.12.2012</b> | 31.12.2011 |
|---|--------------|-------------------|------------|
| Interest income .....   |              | <b>1,663</b>      | 2,052      |
| Interest expense .....  |              | <b>(650)</b>      | (1,184)    |
| Net interest income .....   |              | <b>1,013</b>      | 868        |
| Fee income .....  |              | <b>960</b>        | 1,014      |
| Fee expense .....   |              | <b>(224)</b>      | (245)      |
| Net fee income .....  |              | <b>736</b>        | 769        |
| Trading income .....  |              | <b>352</b>        | (61)       |
| Net income from financial instruments designated at fair value .....  |              | <b>(108)</b>      | 120        |
| Gains less losses from financial investments .....  |              | <b>58</b>         | 52         |
| Dividend income .....   |              | <b>7</b>          | 6          |
| Other operating income .....  |              | <b>38</b>         | 27         |
| <b>Total operating income before loan impairment (charges)/release and other credit risk provisions</b> ..... |              | <b>2,096</b>      | 1,781      |
| Loan impairment charges and other credit risk provisions .....  |              | <b>(117)</b>      | (109)      |
| <b>Net operating income</b> .....   | 4            | <b>1,979</b>      | 1,672      |
| Employee compensation and benefits .....  | 5            | <b>(993)</b>      | (998)      |
| General and administrative expenses .....   |              | <b>(543)</b>      | (558)      |
| Depreciation of property, plant and equipment .....   | 18           | <b>(47)</b>       | (49)       |
| Amortisation of intangible assets and impairment of goodwill .....  | 17           | <b>(8)</b>        | (8)        |
| <b>Total operating expenses</b> .....   |              | <b>(1,591)</b>    | (1,613)    |
| <b>Operating profit</b> .....   |              | <b>388</b>        | 59         |
| Share of profit in associates and joint ventures .....  |              | -                 | -          |
| <b>Profit before tax</b> .....  |              | <b>388</b>        | 59         |
| Tax expense .....   | 7            | <b>(67)</b>       | 65         |
| Net profit of discontinued operations .....   |              | -                 | -          |
| <b>Profit for the period</b> .....  |              | <b>321</b>        | 124        |
| Profit attributable to shareholders of the parent company .....   |              | <b>320</b>        | 123        |
| Profit attributable to non-controlling interests .....  |              | <b>1</b>          | 1          |
| <i>(in euros)</i>   |              |                   |            |
| Basic earnings per ordinary share .....   | 9            | 4.75              | 1.83       |
| Diluted earnings per ordinary share .....   | 9            | 4.75              | 1.83       |
| Dividend per ordinary share .....   | 9            | 3.56              | 1.75       |

## Consolidated statement of comprehensive income for the year ended 31 December 2012

| <i>(in millions of euros)</i>   | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Profit for the period .....   | <b>321</b>        | 124        |
| <b>Other comprehensive income</b>   |                   |            |
| Available-for-sale investments:   |                   |            |
| – fair value gains/(losses) taken to equity .....   | <b>200</b>        | (52)       |
| – fair value gains/(losses) transferred to the income statement on disposal .....             | <b>(58)</b>       | (64)       |
| – amounts transferred to/(from) the income statement<br>in respect of impairment losses ..... | <b>2</b>          | 5          |
| – income taxes .....  | <b>(52)</b>       | 41         |
| Cash flow hedges:   |                   |            |
| – fair value gains/(losses) taken to equity .....   | <b>80</b>         | 92         |
| – fair value (gains)/losses transferred to income statement on disposal .....                 | <b>(57)</b>       | (25)       |
| – income taxes .....  | <b>(8)</b>        | (26)       |
| Actuarial gains/(losses) on defined benefit plans .....                                       | <b>(23)</b>       | (5)        |
| Exchange differences .....  | <b>–</b>          | –          |
| <b>Other comprehensive income for the period, net of tax</b> .....                            | <b>84</b>         | (34)       |
| <b>Total comprehensive income for the period</b> .....  | <b>405</b>        | 90         |
| <b>Total comprehensive income for the year attributable to:</b>                               |                   |            |
| – shareholders of the parent company .....  | <b>404</b>        | 89         |
| – non-controlling interests .....   | <b>1</b>          | 1          |
|   | <b>405</b>        | 90         |

## Consolidated financial statements (continued)

### Consolidated balance sheet at 31 December 2012

#### ASSETS

| <i>(in millions of euros)</i>                                | <i>Notes</i> | <b>31.12.2012</b> | 31.12.2011 |
|--|--------------|-------------------|------------|
| Cash and balances at central banks . . . . .                 | 32           | <b>6,770</b>      | 4,805      |
| Items in the course of collection from other banks . . . . . | 32           | <b>815</b>        | 806        |
| Trading assets . . . . .                                     | 12           | <b>40,577</b>     | 39,013     |
| Financial assets designated at fair value . . . . .          |              | <b>5</b>          | 598        |
| Derivatives . . . . .  | 13           | <b>90,258</b>     | 82,738     |
| Loans and advances to banks . . . . .                        | 28           | <b>28,132</b>     | 29,705     |
| Loans and advances to customers . . . . .                    | 28           | <b>48,354</b>     | 53,279     |
| Financial investments . . . . .                              | 14           | <b>8,258</b>      | 7,518      |
| Interests in associates and joint ventures . . . . .         | 16           | <b>6</b>          | 6          |
| Goodwill and intangible assets . . . . .                     | 17           | <b>377</b>        | 378        |
| Property, plant and equipment . . . . .                      | 18           | <b>295</b>        | 265        |
| Other assets . . . . .                                       | 20           | <b>296</b>        | 1,117      |
| Deferred tax assets . . . . .                                | 23           | <b>200</b>        | 211        |
| Prepayments and accrued income . . . . .                     |              | <b>865</b>        | 946        |
| Assets classified as held for sale . . . . .                 | 20           | <b>-</b>          | 5          |
| <b>TOTAL ASSETS</b> . . . . .                                |              | <b>225,208</b>    | 221,390    |

#### LIABILITIES AND EQUITY

| <i>(in millions of euros)</i>                                | <i>Notes</i> | <b>31.12.2012</b> | 31.12.2011 |
|--|--------------|-------------------|------------|
| <b>Liabilities</b>   |              |                   |            |
| Deposits by banks . . . . .                                  | 28           | <b>32,992</b>     | 32,338     |
| Customer accounts . . . . .                                  | 28           | <b>42,364</b>     | 42,896     |
| Items in the course of transmission to other banks . . . . . | 32           | <b>771</b>        | 757        |
| Trading liabilities . . . . .                                | 27           | <b>36,271</b>     | 38,258     |
| Financial liabilities designated at fair value . . . . .     | 21           | <b>5,654</b>      | 5,527      |
| Derivatives . . . . .  | 13           | <b>89,114</b>     | 81,681     |
| Debt securities in issue . . . . .                           | 28           | <b>10,655</b>     | 12,605     |
| Retirement benefit liabilities . . . . .                     | 5            | <b>152</b>        | 117        |
| Other liabilities . . . . .                                  | 22           | <b>539</b>        | 837        |
| Current taxation . . . . .                                   |              | <b>27</b>         | 25         |
| Accruals and deferred income . . . . .                       |              | <b>1,143</b>      | 1,215      |
| Provisions for liabilities and charges . . . . .             | 24           | <b>97</b>         | 97         |
| Deferred tax liabilities . . . . .                           | 23           | <b>2</b>          | 2          |
| Subordinated liabilities . . . . .                           | 26           | <b>166</b>        | 166        |
| <b>TOTAL LIABILITIES</b> . . . . .                           |              | <b>219,947</b>    | 216,521    |
| <b>Equity</b>  |              |                   |            |
| Called up share capital . . . . .                            | 31           | <b>337</b>        | 337        |
| Share premium account . . . . .                              |              | <b>16</b>         | 16         |
| Other reserves and retained earnings . . . . .               |              | <b>4,860</b>      | 4,468      |
| <b>TOTAL SHAREHOLDERS' EQUITY</b> . . . . .                  |              | <b>5,213</b>      | 4,821      |
| Non-controlling interests . . . . .                          |              | <b>48</b>         | 48         |
| <b>TOTAL EQUITY</b> . . . . .                                |              | <b>5,261</b>      | 4,869      |
| Liabilities classified as held for sale . . . . .            | 22           | <b>-</b>          | -          |
| <b>TOTAL EQUITY AND LIABILITIES</b> . . . . .                |              | <b>225,208</b>    | 221,390    |



## Consolidated statement of changes in equity for the year ended 31 December 2012

|   | 31.12.2012              |               |                   |                                       |                           |                          |                             |                               |                            |                           |              |
|---|-------------------------|---------------|-------------------|---------------------------------------|---------------------------|--------------------------|-----------------------------|-------------------------------|----------------------------|---------------------------|--------------|
|   | Called up share capital | Share premium | Retained earnings | Available-for-sale fair value reserve | Cash flow hedging reserve | Foreign exchange reserve | Share-based payment reserve | Associates and joint ventures | Total shareholders' equity | Non-controlling interests | Total equity |
| <i>(in millions of euros)</i>                     |                         |               |                   |                                       |                           |                          |                             |                               |                            |                           |              |
| <b>At 1 January 2012</b>                          | <b>337</b>              | <b>16</b>     | <b>4,334</b>      | <b>(24)</b>                           | <b>63</b>                 | <b>2</b>                 | <b>89</b>                   | <b>4</b>                      | <b>4,821</b>               | <b>48</b>                 | <b>4,869</b> |
| Share capital issued, net of costs                | -                       | -             | -                 | -                                     | -                         | -                        | -                           | -                             | -                          | -                         | -            |
| Dividends to shareholders                         | -                       | -             | -                 | -                                     | -                         | -                        | -                           | -                             | -                          | -                         | -            |
| Net impact of equity-settled share-based payments | -                       | -             | -                 | -                                     | -                         | -                        | (13)                        | -                             | (13)                       | -                         | (13)         |
| Dividends to non-controlling interests            | -                       | -             | -                 | -                                     | -                         | -                        | -                           | -                             | -                          | -                         | -            |
| Other movements                                   | -                       | -             | 8                 | -                                     | -                         | -                        | (7)                         | -                             | 1                          | (1)                       | -            |
| Total comprehensive income for the period         | -                       | -             | 297               | 92                                    | 15                        | -                        | -                           | -                             | 404                        | 1                         | 405          |
| <b>At 31 December 2012</b>                        | <b>337</b>              | <b>16</b>     | <b>4,639</b>      | <b>68</b>                             | <b>78</b>                 | <b>2</b>                 | <b>69</b>                   | <b>4</b>                      | <b>5,213</b>               | <b>48</b>                 | <b>5,261</b> |

|   | 31.12.2011              |               |                   |                                       |                           |                          |                             |                               |                            |                           |              |
|---|-------------------------|---------------|-------------------|---------------------------------------|---------------------------|--------------------------|-----------------------------|-------------------------------|----------------------------|---------------------------|--------------|
|   | Called up share capital | Share premium | Retained earnings | Available-for-sale fair value reserve | Cash flow hedging reserve | Foreign exchange reserve | Share-based payment reserve | Associates and joint ventures | Total shareholders' equity | Non-controlling interests | Total equity |
| <i>(in millions of euros)</i>                     |                         |               |                   |                                       |                           |                          |                             |                               |                            |                           |              |
| <b>At 1 January 2011</b>                          | <b>337</b>              | <b>16</b>     | <b>4,341</b>      | <b>46</b>                             | <b>22</b>                 | <b>(1)</b>               | <b>67</b>                   | <b>4</b>                      | <b>4,832</b>               | <b>48</b>                 | <b>4,880</b> |
| Share capital issued, net of costs                | -                       | -             | -                 | -                                     | -                         | -                        | -                           | -                             | -                          | -                         | -            |
| Dividends to shareholders                         | -                       | -             | (118)             | -                                     | -                         | -                        | -                           | -                             | (118)                      | -                         | (118)        |
| Net impact of equity-settled share-based payments | -                       | -             | -                 | -                                     | -                         | -                        | 24                          | -                             | 24                         | -                         | 24           |
| Dividends to non-controlling interests            | -                       | -             | -                 | -                                     | -                         | -                        | -                           | -                             | -                          | -                         | -            |
| Other movements                                   | -                       | -             | (7)               | -                                     | -                         | 3                        | (2)                         | -                             | (6)                        | (1)                       | (7)          |
| Total comprehensive income for the period         | -                       | -             | 118               | (70)                                  | 41                        | -                        | -                           | -                             | 89                         | 1                         | 90           |
| <b>At 31 December 2011</b>                        | <b>337</b>              | <b>16</b>     | <b>4,334</b>      | <b>(24)</b>                           | <b>63</b>                 | <b>2</b>                 | <b>89</b>                   | <b>4</b>                      | <b>4,821</b>               | <b>48</b>                 | <b>4,869</b> |

**Consolidated financial statements** (continued)**Consolidated cash flow statement for the year ended 31 December 2012**

| <i>(in millions of euros)</i>   | <i>Notes</i> | <b>31.12.2012</b> | 31.12.2011 |
|---|--------------|-------------------|------------|
| <b>Cash flows from operating activities</b>                                       |              |                   |            |
| Profit before tax   |              | <b>388</b>        | 59         |
| Net profit on discontinued operations   |              | –                 | –          |
| – non-cash items included in net profit   | 32           | <b>59</b>         | 114        |
| – change in operating assets  | 32           | <b>3,322</b>      | 17,215     |
| – change in operating liabilities   | 32           | <b>(2,219)</b>    | (13,207)   |
| – change in assets/liabilities classified as held for sale (including cash flows) |              | –                 | –          |
| – elimination of exchange differences   |              | <b>(60)</b>       | (278)      |
| – net (gain)/loss from investing activities                                       |              | <b>(63)</b>       | (64)       |
| – share of profits in associates and joint ventures                               |              | –                 | –          |
| – dividends received from associates  |              | –                 | –          |
| – tax paid  |              | <b>(12)</b>       | 56         |
| Net cash flows from operating activities  |              | <b>1,415</b>      | 3,895      |
| <b>Cash flows (used in)/from investing activities</b>                             |              |                   |            |
| Purchase of financial investments   |              | <b>(3,738)</b>    | (7,396)    |
| Proceeds from the sale of financial investments                                   |              | <b>3,170</b>      | 2,515      |
| Purchase of property, plant and equipment   |              | <b>(79)</b>       | (87)       |
| Proceeds from the sale of property, plant and equipment                           |              | <b>11</b>         | (1)        |
| Purchase of goodwill and intangible assets  |              | <b>(7)</b>        | (9)        |
| Net cash outflow from acquisition of and increase in stake of subsidiaries        |              | –                 | –          |
| Net cash inflow from disposal of subsidiaries                                     |              | –                 | 13         |
| Net cash outflow from acquisition of and increase in stake of associates          |              | –                 | –          |
| Proceeds from disposal of associates  |              | –                 | –          |
| Net cash flows (used in)/from investing activities                                |              | <b>(643)</b>      | (4,965)    |
| <b>Cash flows (used in)/from financing activities</b>                             |              |                   |            |
| Issue of ordinary share capital   |              | –                 | –          |
| Net purchases of own shares   |              | –                 | –          |
| Increase in non-equity non-controlling interests                                  |              | –                 | –          |
| Subordinated loan capital issued  |              | –                 | –          |
| Subordinated loan capital repaid  |              | –                 | –          |
| Dividends paid to shareholders  |              | –                 | (118)      |
| Dividends paid to non-controlling interests                                       |              | –                 | –          |
| Net cash flows (used in)/from financing activities                                |              | –                 | (118)      |
| <b>Net increase in cash and cash equivalents</b>                                  |              | <b>772</b>        | (1,187)    |
| Cash and cash equivalents at 1 January  |              | <b>29,033</b>     | 30,091     |
| Effect of exchange rate changes on cash and cash equivalents                      |              | <b>15</b>         | 129        |
| <b>Cash and cash equivalents at 31 December</b>                                   |              | <b>29,820</b>     | 29,033     |

## Notes to the consolidated financial statements

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## Consolidated financial statements (continued)

### 1 Basis of preparation

- a** HSBC France has prepared its consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as endorsed by the European Union (EU). 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. EU-endorsed IFRSs may differ from IFRSs as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. At 31 December 2012, there were no unendorsed standards effective for the year ended 31 December 2012 affecting the consolidated financial statements at that date, and there was no difference between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to HSBC France.

The consolidated financial statements of HSBC France are available upon request from the HSBC France registered office at 103, avenue des Champs-Élysées – 75419 Paris Cedex 08 or on the website [www.hsbc.fr](http://www.hsbc.fr).

These consolidated financial statements were approved by the Board of Directors on 27 February 2013.

At 31 December 2012, HSBC France revised its methodology for determining “Credit Valuation Adjustment” (CVA) for derivatives. Historically, the probability of default used in the CVA calculation has been based on HSBC France group’s internal credit rating for the counterparty taking into account how credit ratings may deteriorate over the duration of the exposure based on historical rating transition matrices. As a result of evolving market practice, HSBC France has decided to revise the methodology for determining the probability of default to one derived from current market levels for certain transaction types such as credit default swaps without an adjusting factor where the credit default swap or other market data relates to the counterparty. Where relevant information for a particular counterparty is not available in the market, adjustments are made as necessary on other appropriate market information to determine the appropriate probability of default. Such adjustments are driven by considerations of the credit rating of the counterparty. In addition, as a result of the evolving market practices and in conjunction with the revised methodology for determining CVA, the HSBC France group aligned its methodology for determining the “Debit Valuation Adjustment” (DVA). Historically, the group had adopted a zero DVA. At 31 December 2012, the effect of the changes in fair value estimate as a result of the revisions to methodology was to reduce derivative assets by EUR 98 million resulting in a net trading loss of EUR 98 million. It is impracticable to estimate the effect of the changes in fair value estimate on future periods. See Note 28 for further information on credit valuation adjustment and debit valuation adjustment methodologies.

During 2012, in addition to the above, the HSBC France group adopted a number of standards and interpretations, and amendments, as a result of the evolving market practices which impacted the accounts as detailed below.

- b** The HSBC France group’s (the “group”) consolidated financial statements consist of the financial statements of HSBC France, its subsidiaries, HSBC France’s interests in jointly controlled entities and associates as at 31 December.

#### *Acquisitions*

Acquired subsidiaries are consolidated from the date at which control passes to HSBC France until the date on which this control ends. As allowed under IFRS 1, HSBC France has opted not to restate business combinations that took place before 1 January 2004, the date at which it adopted IFRS.

HSBC France’s acquisitions of subsidiaries are accounted for using the purchase method. The cost of an acquisition is recognised at fair value at the date on which HSBC France takes control, taking into account the costs directly attributable to the acquisition. Identifiable assets, liabilities and contingent liabilities are recognised at fair value at the acquisition date. The difference between the acquisition cost and fair value of the portion of identifiable net assets attributable to HSBC France is recognised as goodwill if positive and immediately taken to income if negative.

#### *Consolidation methods*

Companies controlled by the group are fully consolidated. Exclusive control over a subsidiary is determined by the ability to govern the subsidiary’s financial and operating policies in order to benefit from its activities. Control results from:

- the direct or indirect ownership of a majority of the subsidiary’s voting rights;
- the power to appoint, remove or gather a majority of members of the subsidiary’s Board of Directors or equivalent governing bodies;
- the power to govern the financial and operating policies of the entity under a statute or an agreement.

## 1 Basis of preparation (continued)

The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether an entity has the power to govern the financial and operating policies of another entity.

Jointly controlled companies are reported using the equity method. HSBC France has joint control over a company when, as part of a contractual agreement, strategic financial and operating decisions relating to the company's activity require the unanimous consent of all the venturers sharing control.

Companies over which HSBC France has significant influence are accounted for as associates. Significant influence is the power to participate in the financial and operating decisions of an entity without controlling it. Significant influence is assumed if 20 per cent or more of an entity's voting rights are held.

Lastly, HSBC France consolidates distinct legal entities created specifically to manage a transaction or a group of similar transactions ("special purpose entities"), even if there is no capital link, provided that HSBC France controls the entities in substance, based on the following criteria:

- the entity's activities are being conducted on behalf of HSBC France, such that HSBC France benefits from these activities;
- HSBC France has decision-making and managing powers to obtain the majority of benefits arising from the entity's ordinary activities. These powers include the ability to dissolve the entity, to change its charter or Articles of Association and to veto proposed changes of the Special Purpose Entities' (SPE) charter or Articles of Association. These powers may have been delegated through an autopilot mechanism;
- HSBC France is able to obtain the majority of the benefits from the entity and may therefore be exposed to risks arising from the entity's activities;
- HSBC France retains the majority of the risks related to the entity in order to obtain benefits from its activity.

### *Elimination of internal transactions*

All transactions internal to the HSBC France group are eliminated on consolidation.

### *Share of the results and reserves of joint ventures and associates*

The consolidated financial statements include the attributable share of the results and reserves of joint ventures and associates owed to HSBC France, based on financial statements updated not earlier than three months prior to 31 December.

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- c** 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 those reported.

Management believes that HSBC France's critical accounting policies where judgement is necessarily applied are those which relate to impairment of loans and advances, goodwill impairment, the valuation of financial instruments, the impairment of available-for-sale financial assets and deferred tax assets.

In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of HSBC France's net income, financial position and cash flows have been made.

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## **d** *Future accounting developments*

### *Standards and Interpretations issued by the IASB and endorsed by the European Union (EU)*

At 31 December 2012, a number of standards and interpretations, and amendments thereto, had been issued by the IASB, which had no effect on HSBC France's consolidated financial statements. In addition to the projects to complete financial instrument accounting, the IASB is continuing to work on projects on revenue recognition and lease accounting, which together with the standards described below, will represent widespread and significant changes to accounting requirements from 2013.

## Consolidated financial statements (continued)

### 1 Basis of preparation (continued)

*Standards and Interpretations issued by the IASB but not endorsed by the European Union (EU)*

- Standards applicable in 2013

In May 2011, the IASB issued IFRS 10 “Consolidated Financial Statements” (“IFRS 10”), IFRS 11 “Joint Arrangements” (“IFRS 11”) and IFRS 12 “Disclosure of Interests in Other Entities” (“IFRS 12”). The standards are effective for annual periods beginning on/or after 1 January 2013 with early adoption permitted. IFRSs 10 and 11 are to be applied retrospectively.

Under IFRS 10, there will be one approach for determining consolidation for all entities, based on the concept of power, variability of returns and their linkage. This will replace the current approach which emphasises legal control or exposure to risks and rewards, depending on the nature of the entity. IFRS 11 places more focus on the investors’ rights and obligations than on structure of the arrangement, and introduces the concept of a joint operation. IFRS 12 includes the disclosure requirements for subsidiaries, joint arrangements and associates and introduces new requirements for unconsolidated structured entities. Based on HSBC France’s assessment to date, IFRSs 10, 11 and 12 are not expected to have a material impact on the group’s financial statements.

In May 2011, the IASB also issued IFRS 13 “Fair Value Measurement” (“IFRS 13”). This standard is effective for annual periods beginning on/or after 1 January 2013 with early adoption permitted. IFRS 13 is required to be applied prospectively from the beginning of the first annual period in which it is applied. The disclosure requirements of IFRS 13 do not require comparative information to be provided for periods prior to initial application.

IFRS 13 establishes a single source of guidance for all fair value measurements required or permitted by IFRSs. The standard clarifies the definition of fair value as an exit price, which is defined as a price at which an orderly transaction to sell the asset or to transfer the liability would take place between market participants at the measurement date under current market conditions, and enhances disclosures about fair value measurement.

Based on HSBC France assessment to date and as a result of the changes to the DVA and CVA methodology set out on page 106, the impact of IFRS 13 is not expected to be material to HSBC France.

In June 2011, the IASB issued amendments to IAS 19 “Employee Benefits” (IAS 19 revised). The revised standard is effective for annual periods beginning on/or after 1 January 2013 with early adoption permitted. IAS 19 revised must be applied retrospectively.

The most significant amendment for HSBC France is the replacement of interest cost and expected return on plan assets by a finance cost component comprising the net interest on the net defined benefit liability or asset. This finance cost component is determined by applying the same discount rate used to measure the defined benefit obligation to the net defined benefit liability or asset. The difference between the actual return on plan assets and the return included in the finance cost component in the income statement will be presented in other comprehensive income. The effect of this change is to increase the pension expense by the difference between the current expected return on plan assets and the return calculated by applying the relevant discount rate.

Based on HSBC France’s estimate of the impact of this particular amendment on the 2012 consolidated financial statements, the change would decrease pre-tax profit, with no effect on the pension liability. The effect on total operating expenses and pre-tax profit is not material. The effect at the date of adoption on 1 January 2013 was not material to HSBC France.

In December 2011, the IASB issued amendments to IFRS 7 “Disclosures – Offsetting Financial Assets and Financial Liabilities”, which requires the disclosures about the effect or potential effects of offsetting financial assets and financial liabilities and related arrangements on an entity’s financial position. The amendments are effective for annual periods beginning on/or after 1 January 2013. The amendments are required to be applied retrospectively.

- Standards applicable in 2014

In December 2011, the IASB issued amendments to IAS 32 “Offsetting Financial Assets and Financial Liabilities”, which clarified the requirements for offsetting financial instruments and addressed inconsistencies in current practice when applying the offsetting criteria in IAS 32 “Financial Instruments: Presentation”. The amendments are effective for annual periods beginning on/or after 1 January 2014 with early adoption permitted and are required to be applied retrospectively.

## 1 Basis of preparation *(continued)*

The group is currently assessing the impact of the amendments to IAS 32 but it is impracticable to quantify their effect as at the date of publication of these financial statements.

In October 2012, the IASB issued amendments to IFRS 10, IFRS 12 and IAS 27 “Investment Entities”, which introduced an exception to the principle that all subsidiaries shall be consolidated. The amendments require a parent company, that is an investment entity, to measure its investments, in particular subsidiaries, at fair value through profit or loss instead of consolidating all subsidiaries in its consolidated and separate financial statements. The amendments are effective from 1 January 2014 with early adoption permitted. Based on HSBC France initial assessment, these amendments are not expected to have a material impact on the group’s consolidated financial statements.

- Standards applicable in 2015

In November 2009, the IASB issued IFRS 9 “Financial Instruments” (IFRS 9), which introduced new requirements for the classification and measurement of financial assets. In October 2010, the IASB issued additions to IFRS 9 relating to financial liabilities. Together, these changes represent the first phase in the IASB’s planned replacement of IAS 39 “Financial Instruments: Recognition and Measurement” (IAS 39) with a less complex and improved standard for financial instruments.

Following the IASB’s decision, in December 2011, to defer the effective date, the standard is effective for annual periods beginning on/or after 1 January 2015 with early adoption permitted. IFRS 9 is required to be applied retrospectively but prior periods need not be restated.

The second and third phases in the IASB’s project to replace IAS 39 will address the impairment of financial assets measured at amortised cost and hedge accounting.

The IASB is in the process of amending the requirements for classification and measurement in IFRS 9 to address practice and other issues.

As a result of uncertainties with regard to the final IFRS 9 requirements for classification and measurement and impairment, the HSBC France group remains unable to provide a date by which it will apply IFRS 9 as a whole and it remains impracticable to quantify the effect of IFRS 9 as at the date of the publication of these financial statements.

- EU Endorsement

All the standards applicable in 2013 and 2014 have been endorsed for use in the EU, except for the amendments to IFRS 10, IFRS 11 and IFRS 12 “Transition Guidance” and the amendments to IFRS 10, IFRS 12 and IAS 27 “Investment Entities”. Until these amendments are endorsed, the relief they provide for comparatives disclosures in accordance with IFRS 12 will not be available.

## 2 Principal accounting policies

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### a *Interest income and expense*

Interest income and expense for all interest-bearing financial instruments except those classified as held-for-trading or designated at fair value (other than debt issued by HSBC France and related derivatives) are recognised in “Interest income” and “Interest expense” in the 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 at inception 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, HSBC France 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 HSBC France 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 at the original effective interest rate of the financial asset applied to the carrying amount as reduced by any allowance for impairment.

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

#### b Non-interest income

##### *Fee income*

HSBC France earns fee income from a diverse range of services it provides to its customers. Fee income is accounted for as follows:

- if the income is earned on the execution of a significant act, it is recognised when the significant act has been 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);
- if the income is earned as services are provided, it is recognised as the services are provided (for example, asset management, portfolio and other management advisory and service fees);
- if the income is an integral part of the effective interest rate of a financial instrument, it is recognised as an adjustment to the effective interest rate (for example, loan commitment fees) and recorded in “Interest income” (see Note 2 a).

##### *Dividend income*

Dividend income is recognised when the right to receive payment is established. This is the ex-dividend date for equity securities.

##### *Net income from financial instruments designated at fair value*

Net income from financial instruments designated at fair value comprises all gains and losses from changes in the fair value of financial assets and financial liabilities designated at fair value through profit and loss. Interest income and expense and dividend income arising on those financial instruments are also included, except for debt securities in issue and derivatives managed in conjunction with debt securities in issue. Interest on these instruments is shown in “Net interest income”.

##### *Trading income*

Trading income comprises all gains and losses from changes in the fair value of financial assets and financial liabilities held-for-trading, together with related interest income, expense and dividends.

#### c Segment reporting

HSBC France mainly operates in France and manages its business through the following customer groups: Retail Banking and Wealth Management (including Insurance and Asset Management), Commercial Banking, Global Banking and Markets and Private Banking.

HSBC France’s operations include a number of support services and head office functions. The costs of these functions are allocated to business lines, where it is appropriate, on a systematic and consistent basis.

The reporting of financial information by segment required by IFRS 8 is disclosed in Note 10.

#### d Determination of fair value

All financial instruments are recognised initially at fair value. The fair value of a financial instrument on initial recognition is normally the transaction price, *i.e.* the fair value of the consideration given or received. In certain circumstances, however, the initial fair value may be based on current market transactions in the same instrument, or on valuation techniques including only data from observable markets.

Subsequent to initial recognition, the fair values of financial instruments measured at fair value that are quoted in active markets are based on bid prices for assets held or liabilities to be issued and offer prices for assets to be acquired or liabilities held at the time. When independent prices are not available, fair values are determined by using valuation techniques which refer to observable market data. These include comparison with similar instruments where market observable prices exist, discounted cash flow analysis, option-pricing models and other valuation techniques commonly used by market participants.

For certain derivatives, fair values 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.



## 2 Principal accounting policies (continued)

A number of factors such as bid-offer spread, credit profile and model uncertainty are taken into account, as appropriate, when values are calculated using valuation techniques.

If the fair value of a financial asset measured at fair value becomes negative, it is recorded as a financial liability until its fair value becomes positive, at which time it is recorded as a financial asset, or it is extinguished.

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### e *Reclassification of financial assets*

Non-derivative financial assets (other than those designated at fair value through profit or loss upon initial recognition) may be reclassified out of the fair value through profit or loss category in particular circumstances:

- financial assets that would have met the definition of loans and receivables at initial recognition (if the financial asset had not been required to be classified as held for trading) may be reclassified out of the fair value through profit or loss category if there is the intention and ability to hold the financial asset for the foreseeable future or until maturity;
- financial assets (except financial assets that would have met the definition of loans and receivables) may be reclassified out of the fair value through profit or loss category and into another category in rare circumstances.

When a financial asset is reclassified as described in the above circumstances, the financial asset is reclassified at its fair value on the date of reclassification. Any gain or loss already recognised in the income statement is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortised cost, as applicable.

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### f *Loans and advances to banks and customers*

Loans and advances to banks and customers include loans and advances originated by HSBC France, 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. Loans and advances are recognised when cash is advanced to borrowers and are derecognised when either borrowers repay their obligations, or the loans are sold or written off or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment losses.

For certain leveraged finance and syndicated lending activities, the group may commit to underwrite loans on fixed contractual terms for specified periods of time, where the drawdown of the loan is contingent upon certain future events outside the control of the group. Where the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a trading derivative and measured at fair value through profit and loss. On drawdown, the loan is classified as held for trading and measured at fair value through profit and loss. Where it is not the group's intention to trade the loan, a provision on the loan commitment is only recorded where it is probable that the group will incur a loss. This may occur, for example, where a loss of principal is probable or the interest rate charged on the loan is lower than the cost of funding. On inception of the loan, the hold portion is recorded at its fair value and subsequently measured at amortised cost using the effective interest method. However, where the initial fair value is lower than the cash amount advanced, the write down is charged to the income statement. The write down will be recovered over the life of the loan, through the recognition of interest income using the effective interest rate method, unless the loan becomes impaired. The write down is recorded as a reduction to other operating income.

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### g *Loan impairment*

Losses for impaired loans are recognised promptly when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Impairment losses are calculated on individual loans and on loans assessed collectively. Losses expected from future events, no matter how likely, are not recognised.

#### *Individually assessed loans*

Impairment losses on individually assessed accounts are determined by an evaluation of the exposures on a case-by-case basis. HSBC France assesses at each balance-sheet date whether there is any objective evidence that a loan is impaired.

In determining such impairment losses on individually assessed accounts, the following factors are considered:

- HSBC France'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 their debt obligations;
- the likely dividend available on liquidation or bankruptcy;

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

- the extent of other creditors' commitments ranking ahead of, or *pari passu* with, HSBC France and the likelihood of other creditors continuing to support the company;
- 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 amount and timing of expected receipts and recoveries;
- the realisable value of security (or other credit mitigants) 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 foreign currency if loans are not in local currency; and,
- where available, the secondary market price for the debt.

Impairment loss is calculated by comparing the present value of the expected future cash flows, discounted at the original effective interest rate of the loan, with its current carrying value, and the amount of any loss is charged in the income statement. The carrying amount of impaired loans is reduced through the use of an allowance account.

#### *Collectively assessed loans*

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 covers loans that are impaired at the balance sheet date but which will not be individually identified as such until some time in the future.

The collective impairment loss is determined after taking into account:

- historical loss experience in portfolios of similar risk characteristics (for example, by industry sector, loan grade or product, etc.);
- the estimated period between a loss occurring and that loss being identified and evidenced by the establishment of an allowance against the loss on an individual loan; and,
- management's experienced judgement as to whether the current economic and credit conditions are such that the actual level of inherent losses 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 portfolio.

#### *Loan write-offs*

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery of these amounts and, for collateralised loans, when the proceeds from realising the security have been received.

#### *Reversals of impairment*

If, in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed to the extent it is now excessive by reducing the loan impairment allowance account. The amount of any reversal is recognised in the income statement.

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#### **h** *Trading assets and trading liabilities*

Treasury bills, debt securities, equity shares and short positions in securities, which have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, are classified as held for trading. Such financial assets or financial liabilities are recognised at trade date when HSBC France enters into contractual arrangements with counterparties to purchase or sell securities, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the income statement. Subsequently, their fair values are remeasured; all subsequent gains and losses from changes in the fair value of these assets and liabilities, together with related interest income and expense and dividends, are recognised in the income statement within "Trading income" as they arise.

## 2 Principal accounting policies (continued)

### i *Financial instruments designated at fair value*

A financial instrument, other than one held for trading, is classified in this category if it meets one or more criteria set out below, and is so designated by management. HSBC France may designate financial instruments at fair value where the designation:

- eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring financial assets or financial liabilities or recognising the gains and losses on them on different bases;
- applies to a group of financial assets, financial liabilities or both that is managed and its performance evaluated on a fair value basis and where information about that group of financial instruments is provided internally on that basis to key management staff; or,
- relates to financial instruments containing one or more embedded derivatives that significantly modify the cash flows resulting from those financial instruments.

The fair value designation, once made, is irrevocable. Designated financial assets and financial liabilities are recognised at trade date when HSBC France enters into contractual arrangements with counterparties to purchase or sell securities, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the income statement. Subsequently, the fair values are remeasured and, except for interest payable on debt securities in issue designated at fair value, gains and losses from changes therein are recognised in “Net income from financial instruments designated at fair value”.

Gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are also included in “Net income from financial instruments designated at fair value”. Interest on these derivatives is also included in this line, except for interest on derivatives managed with debt securities in issue designated at fair value, which is included in net interest income. The amount of change during the period, and cumulatively, in the fair value of designated financial liabilities and loans and receivables that is attributable to changes in their credit risk, is determined as the amount of change in fair value that is not attributable to changes in market conditions.

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### j *Financial investments*

Treasury bills, debt securities and equity shares intended to be held on a continuing basis are classified as available-for-sale securities unless designated at fair value (see Note 2 i) or classified as “held-to-maturity”. Financial investments are recognised at trade date, when the Group enters into contractual arrangements with counterparties to purchase securities, and are normally derecognised when either the transactions are sold or the borrowers repay their obligations.

HSBC France did not hold any “held-to-maturity” investments in 2011 or 2012.

Available-for-sale securities are initially measured at fair value plus direct and incremental transaction costs. They are subsequently remeasured at fair value. Changes in fair value are recognised in equity in the “Available-for-sale reserve” until the securities are either sold or impaired. On the sale of available-for-sale securities, gains or losses held within equity are recycled through the income statement and classified as “Gains less losses from financial investments”.

Interest income is recognised on such securities using the effective interest method, calculated over the asset’s expected life. Where dated investment securities have been purchased at a premium or discount, these premiums and discounts are recognised as an adjustment to the effective interest rate. Dividends are recognised in the income statement when the right to receive payment has been established.

An assessment is made at each balance sheet date as to whether there is any objective evidence of impairment where an adverse impact on estimated future cash flows of the financial asset or group of assets can be reliably estimated.

If an available-for-sale financial asset is determined to be impaired, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement) is removed from equity and recognised in the income statement within “Loan impairment charges and other credit risk provisions” for debt instruments and within “Gains less losses from financial investments” for equity instruments.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement until the sale of this instrument.

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

Management is required to exercise judgement in determining whether there is objective evidence that an impairment loss has occurred. Once an impairment has been identified, the amount of impairment is measured in relation to the fair value of the asset.

The objective evidence required to determine whether an available-for-sale debt security is impaired comprises evidence of the occurrence of a loss event, and evidence that the loss event results in a decrease in estimated future cash flows. Where cash flows are readily determinable, a low level of judgement may be involved. Where determination of estimated future cash flows requires consideration of a number of variables, some of which may be unobservable in current market conditions, more significant judgement is required.

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#### k Sale and repurchase agreements (including stock lending and borrowing)

When securities are sold subject to a commitment to repurchase them at a predetermined price (“repos”) or are the subject of a stock lending agreement, they remain on the balance sheet and a liability is recorded in respect of the consideration received. Conversely, securities purchased under analogous commitments to resell (“reverse repos”) are not recognised on the balance sheet and the consideration paid is recorded in “Loans and advances to banks” or “Loans and advances to customers” as appropriate. The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement using the effective interest method.

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

Securities borrowed are not recognised on the balance sheet, unless control of the contractual rights that comprise these securities is obtained and the securities are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in “Trading income”, and the obligation to return them is recorded as a trading liability and measured at fair value.

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#### l Derivatives and hedge accounting

Derivatives are recognised initially, and are subsequently remeasured, at fair value. Fair values are obtained from quoted market prices in active markets, or by using valuation techniques, including recent market transactions, where an active market does not exist. Valuation techniques include discounted cash flow models and option pricing models as appropriate. In the normal course of business, the fair value of a derivative at initial recognition is considered to be the transaction price (*i.e.* the fair value of the consideration given or received). However, in certain circumstances the fair value of an instrument will be evidenced by comparison with other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, including interest rate yield curves, option volatilities and currency rates. When such evidence exists, HSBC France recognises a trading profit or loss on inception of the derivative. If observable market data are not available, the initial increase in fair value indicated by the valuation model, but based on unobservable inputs, is not recognised immediately in the income statement but is recognised over the life of the transaction on an appropriate basis, or recognised in the income statement when the inputs become observable, or when the transaction matures or is closed out.

Certain derivatives embedded in other financial instruments, such as the conversion option in a convertible bond, are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract, when the terms of the embedded derivative are the same as those of a stand-alone derivative, and the combined contract is not designated at fair value. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement. Derivatives embedded in home purchase savings products (*Plan Epargne Logement/Compte Epargne Logement*) are some of the main embedded derivatives identified by HSBC France, and have therefore been valued using an HSBC France specific model (see Note 13).

All derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. Derivative assets and liabilities on different transactions are only netted if the transactions are with the same counterparty, a legal right of set-off exists, and the cash flows are to be settled on the same date and on a net basis.

## 2 Principal accounting policies (continued)

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 income statement. Where derivatives are designated as hedges, HSBC France classifies them as derivatives as either: (i) hedges of the change in fair value of recognised assets or liabilities or firm commitments (“fair value hedge”); (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”); or (iii) hedges of net investments in a foreign operation (“net investment hedge”). Hedge accounting is applied to derivatives designated as hedging instruments in a fair value, cash flow or net investment hedge provided certain criteria are met.

### *Hedge accounting*

Following the HSBC Group policy, HSBC France does not use the “carve out” arrangements contained in the European regulation no. 2086/2004 in relation to the accounting for macro-hedging operations.

As required in IAS 39, HSBC France documents, at the inception of a hedging relationship, the relationship between the hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking the hedge. Therefore it is also required to measure, both at hedge inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective. Interest on designated qualifying hedges is included in “Net interest income”.

### *Fair value hedge*

Changes in the fair value of derivatives that are designated and qualify as fair value hedging instruments are recorded in the income statement, together with any changes in the fair value of the asset or liability or group thereof that are attributable to the hedged risk.

If the hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to the income statement over the residual period to maturity. Where the adjustment relates to the carrying amount of a hedged equity security, this remains in retained earnings until the disposal of the equity security.

### *Cash flow hedge*

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. Any gain or loss relating to an ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled to the income statement in the periods in which the hedged item will affect profit or loss. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity until the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

### *Net investment hedge*

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in equity; the gain or loss relating to the ineffective portion is recognised immediately in the income statement. Gains and losses accumulated in equity are included in the income statement when the foreign operation is disposed.

### *Hedge effectiveness testing*

To qualify for hedge accounting, IAS 39 requires the hedge to be highly effective. At the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness). Actual effectiveness (retrospective effectiveness) must also be demonstrated on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method an HSBC France entity adopts for assessing hedge effectiveness will depend on its risk management strategy.

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

In assessing effectiveness, the changes in the fair value or the cash flows of the hedged item and the hedging instrument must be expected to, or must almost fully, offset each other. For prospective effectiveness, the changes in fair value or cash flows must be expected to offset each other in the range of 90 per cent to 110 per cent. For actual effectiveness, the changes in fair value or cash flows must offset each other in the range of 80 per cent to 125 per cent for the hedge to be deemed effective.

#### *Derivatives that do not qualify for hedge accounting*

All gains and losses from changes in the fair value of any derivative that does not qualify for hedge accounting are recognised immediately in the income statement. These gains and losses are reported in “Trading income”, except where derivatives are managed in conjunction with financial instruments designated at fair value, in which case gains and losses are reported in “Net income from financial instruments designated at fair value”.

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#### **m** *Derecognition of financial assets and liabilities*

Financial assets are derecognised when the rights to receive cash flows from the assets have expired; or where HSBC France has transferred its contractual rights to receive the cash flows of the financial assets and has transferred substantially all the risks and rewards of ownership; or where control is not retained. Financial liabilities are derecognised when they are extinguished, *i.e.* when the obligation is discharged or cancelled or expired.

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#### **n** *Offsetting financial assets and financial liabilities*

Financial assets and financial liabilities are offset and the net amount reported in the 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.

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#### **o** *Associates and joint ventures*

Investments in associates and interests in joint ventures are initially stated at cost, including attributable goodwill, and adjusted thereafter for the post-acquisition change in HSBC France’s share of net assets.

Unrealised gains on transactions between HSBC France and its associates and jointly controlled entities are eliminated to the extent of HSBC France’s interest in the associate or joint venture. Unrealised losses are also eliminated to the extent of HSBC France’s interest in the associate or joint venture unless the transaction provides evidence of an impairment of the asset transferred.

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#### **p** *Goodwill and intangible assets*

Goodwill arises on business combinations, including the acquisition of subsidiaries, joint ventures or associates when the cost of acquisition exceeds the fair value of HSBC France’s share of the identifiable net assets, liabilities and contingent liabilities acquired. By contrast, if HSBC France’s interest in the fair value of the identifiable assets, liabilities and contingent liabilities of an acquired business is greater than the cost to acquire, the excess is recognised immediately in the income statement.

Intangible assets are recognised separately from goodwill when they are separable or arise from contractual or other legal rights, and their fair value can be measured reliably.

Goodwill is allocated to cash-generating units for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. Impairment testing is performed annually by comparing the present value of the expected future cash flows from a business with the carrying value of its net assets, including attributable goodwill. Goodwill is stated at cost less accumulated impairment losses, which are charged to the income statement.

Goodwill on acquisitions of joint ventures or associates is included in “Interests in associates and joint ventures”.

At the date of disposal of a business, attributable goodwill is included in HSBC France’s share of net assets in the calculation of the gain or loss on disposal.

Intangible assets include computer software, trade names, customer lists, core deposit relationships and merchant or other loan relationships. Intangible assets are subject to impairment review if there are events or changes in circumstances that indicate that the carrying amount may not be recoverable.

## 2 Principal accounting policies (continued)

Intangible assets that have an indefinite useful life, or are not yet ready for use, are tested for impairment annually. This impairment test may be performed at any time during an annual period, provided it is performed at the same time every year. An intangible asset recognised during the current period is tested before the end of the current annual period.

Intangible assets that have a finite useful life (between 3 and 5 years) are stated at cost less amortisation and accumulated impairment losses and are amortised over their useful lives. Estimated useful life is the lower of legal duration and expected economic life.

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### q *Property, plant and equipment*

Land and buildings are stated at historical cost, or fair value at the date of transition to IFRS (“deemed cost”), less any impairment losses and depreciation calculated to write off the assets as follows:

- land is not depreciated;
- acquisition-related expenses on buildings are expensed in the year in which they occur, as are preliminary costs;
- depreciation of buildings is calculated on a straight-line basis over their estimated useful lives, which are generally between 25 and 75 years.

Equipment, fixtures and fittings (including equipment on operating leases where HSBC France is the lessor) are stated at cost less any impairment losses and depreciation is calculated on a straight-line basis to write off the assets over their estimated useful lives, which are generally between 5 and 10 years. HSBC France holds certain properties as investments to earn rentals or for capital appreciation, or both. Investment properties are included in the balance sheet at fair value with changes in fair value recognised in the income statement in the period of change. Fair values are determined by independent professional valuers who apply recognised valuation techniques.

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

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### r *Finance and operating leases*

Assets leased to customers under agreements which transfer substantially all the risks and rewards associated with ownership, other than legal title, are classified as finance leases. Where HSBC France is a lessor under finance leases, the amounts due under the leases, after deduction of unearned charges, are included in “Loans and advances to banks” or “Loans and advances to customers” as appropriate. Finance income receivable is recognised over the periods of the leases so as to give a constant rate of return on the net investment in the leases.

Where HSBC France 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”. The finance lease and corresponding liability are recognised initially at the fair value of the asset or, if lower, the present value of the minimum lease payments. Finance charges payable are recognised over the periods of the leases based on the interest rates implicit in the leases so as to give a constant rate of interest on the remaining balance of the liability.

All other leases are classified as operating leases. Where HSBC France is the lessor, the assets subject to the operating leases are included in “Property, plant and equipment” and accounted for accordingly. Impairment losses are recognised to the extent that the carrying value of equipment is impaired through residual values not being fully recoverable. Where HSBC France is the lessee, the leased assets are not recognised on the 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.

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### s *Income tax*

Income tax on the profit or loss for the year comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in shareholders’ equity, in which case it is recognised in shareholders’ equity.

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 HSBC France intends to settle on a net basis and the legal right to set off exists.

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the 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 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 set off exists in the entity.

Deferred tax relating to actuarial gains and losses on post-employment benefits is recognised directly in equity. From 1 January 2005, deferred tax relating to fair value remeasurement of available-for-sale investments and cash flow hedges, which are charged or credited directly to equity, is also credited or charged directly to equity and is subsequently recognised in the income statement when the deferred fair value gain or loss is recognised in the income statement.

In 2010, the French Tax “*taxe professionnelle*” was replaced by a new tax “*contribution économique territoriale*” (CET) composed of the “*cotisation foncière des entreprises*” (CFE) based on the rental value of taxable property, and the “*cotisation sur la valeur ajoutée des entreprises*” (CVAE) corresponding to 1.6 per cent of added-value of the year.

The HSBC France group has treated the CVAE as income tax, in application of IAS 12. Deferred CVAE contributions are accounted for on the basis of temporary differences between the book value of assets and liabilities and their tax value from a CVAE standpoint.

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#### t Pension and other post-retirement benefits

HSBC France operates a number of pension and other post-retirement benefit plans. These plans include both defined benefit and defined contribution plans and various other retirement benefits such as post-retirement health-care benefits.

The costs recognised for funding these defined benefit plans are determined using the Projected Unit Credit Method, with annual actuarial valuations performed on each plan. Following the HSBC Group policy, HSBC France uses the option offered by IAS 19 not to defer actuarial gains and losses on the balance sheet and to recognise them directly in reserves, without being recognised in income. 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 period until the benefits are vested. The current service costs and any past service costs, together with the expected return on scheme assets less the unwinding of the discount on the scheme liabilities, are charged to operating expenses.

The net defined benefit liability recognised in the 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. All cumulative actuarial gains and losses on defined benefit plans have been recognised in equity at the date of transition to IFRS.

The cost of providing other post-retirement benefits such as health-care benefits are accounted for on the same basis as defined benefit plans.

Payments to defined contribution plans and state-managed retirement benefit plans, where HSBC France’s obligations under the plans are equivalent to a defined contribution plan, are charged as an expense as they fall due.

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#### u Equity compensation plans

Share-based payments are payments based on shares issued by HSBC Holdings plc. HSBC France employees benefit from the following advantages:

- until 2005, HSBC Holdings plc awarded share options on HSBC Holdings plc shares;
- from 2006, HSBC Holdings plc implemented share plans on HSBC Holdings plc shares;
- employees can subscribe to HSBC Holdings plc shares within the employee share ownership plan.

##### *Share option plans*

The compensation expense to be spread on a straight-line basis over the vesting period is determined by reference to the fair value of the options at grant date, and the impact of any non-market vesting conditions such as option lapses. An option may lapse if, for example, an employee ceases to be employed by HSBC France before the end of the vesting period. Estimates of such future employee departures are taken into account when accruing the cost during the service period.



## 2 Principal accounting policies (continued)

### *Share plans*

This expense is spread on a straight-line basis over the vesting period with a balancing entry in a reserve account. The expense value takes into account hypotheses regarding employee departures and performance conditions for the part of the shares subject to such conditions.

### *Employee share ownership plan*

Employees can subscribe to HSBC Holdings plc shares with a discount and without any vesting period. This advantage is expensed immediately as employee compensation and benefits. The five-year lock-in period is not taken into account in the consideration of the expense.

As permitted by IFRS 1, HSBC France has undertaken full retrospective application of IFRS 2 “Share-based payment”.

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### v *Foreign currencies*

Items included in the financial statements of each of HSBC France’s entities are measured using the currency of the primary economic environment in which the entity operates (“the functional currency”). The consolidated financial statements of HSBC France are presented in euros. 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 income statement. Non-monetary assets and liabilities that are measured in terms of 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.

The results of branches, subsidiaries, joint ventures and associates not reporting in euros are translated into euros at the average rates of exchange for the reporting period. Exchange differences arising from the retranslation of opening foreign currency net investments and the related cost of hedging and exchange differences arising from retranslation of the result for the reporting period from the average rate to the exchange rate prevailing at the period-end are accounted for in a separate foreign exchange reserve. Exchange differences on a monetary item that are part of a net investment in a foreign operation are recognised in the income statement of the separate subsidiary financial statements. In consolidated financial statements, these exchange differences are recognised in the foreign exchange reserve in shareholders’ equity.

As permitted by IFRS 1, HSBC France set the cumulative translation differences for all foreign operations to zero at the date of transition to IFRS. On disposal of a foreign operation, exchange differences relating thereto and previously recognised in reserves are recognised in the income statement.

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### w *Provisions*

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

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### x *Debt securities in issue and subordinated liabilities*

Debt securities in issue and subordinated liabilities are initially measured at fair value, which is the consideration received net of directly attributable transaction costs incurred. Subsequent measurement is at amortised cost, using the effective interest rate method to amortise the difference between proceeds net of directly attributable transaction costs and the redemption amount over the expected life of the debt, unless the securities are designated at fair value (see Note 2 i).

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### y *Share capital*

Shares are classified as equity when there is no contractual obligation to transfer cash or other financial assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

## Consolidated financial statements (continued)

### 2 Principal accounting policies (continued)

#### z Cash and cash equivalents

For the purpose of the cash flow statement, 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, treasury bills and other eligible bills, loans and advances to banks, and certificates of deposit. HSBC France has taken into account the guidance issued by the "Autorité des marchés financiers" (AMF) in early 2006 in respect of "OPCVM de trésorerie" (cash unit trusts).

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#### aa Non-current assets held for sale

The group classifies a non-current asset or disposal group as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

The asset or disposal group must be available for immediate sale in its present condition and its sale must be highly probable.

A sale is highly probable if:

- the appropriate level of management is committed to a plan to sell the asset or disposal group;
- an active plan to locate a buyer and complete the plan has been initiated;
- the asset or disposal group is being actively marketed for sale at a price that is reasonable in relation to its current fair value;
- the sale is expected to be completed within one year from the date of classification;
- it is unlikely that there will be significant changes to the plan or that the plan will be withdrawn.

When the group classifies an asset or disposal group as held for sale it is measured at the lower of its carrying amount and fair value less costs to sell.

### 3 Business combination and disposal of subsidiaries

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In 2012, HSBC France carried on simplifying its structure through the mergers or liquidations of a number of entities detailed in Note 19.

#### 4 Net operating income

Net operating income for the year ended 31 December 2012 amounts to EUR 1,979 million (2011: EUR 1,672 million) and includes income, expense, gains and losses as follows:

| (in millions of euros)   | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| <b>Income</b>  |                   |                   |
| Fees earned on financial assets not held for trading nor designated at fair value and not included in their effective interest rates .....                 | 694               | 673               |
| Fees earned on trust and other fiduciary activities where HSBC France holds or invests assets on behalf of its customers .....                             | 208               | 253               |
| Income from listed investments <sup>1</sup> .....  | 849               | 1,447             |
| Income from unlisted investments <sup>1</sup> .....  | 55                | 32                |
| <b>Expense</b>   |                   |                   |
| Interest on financial instruments, excluding interest on financial liabilities held for trading or designated at fair value .....                          | (558)             | (1,059)           |
| Fees payable on financial assets or liabilities not held for trading nor designated at fair value and not included in their effective interest rates ..... | (223)             | (244)             |
| <b>Gains/(losses)</b>  |                   |                   |
| <b>Gains on disposal of property, plant and equipment, intangible assets and non-financial investments</b>   |                   |                   |
| – gain on disposal of HSBC France Headquarters .....   | –                 | –                 |
| – other .....  | 5                 | 10                |
| <b>Gains/(losses) on financial investments</b>   |                   |                   |
| – equity securities .....  | 24                | 52                |
| – debt securities .....  | 35                | 3                 |
| – impairment of available-for-sale equity shares .....   | (1)               | (5)               |
| <b>Loan impairment charges and other credit risk provisions</b>  |                   |                   |
| – net impairment charge on loans and advances .....  | (115)             | (107)             |
| – impairment of available-for-sale financial investments: debt securities .....  | (1)               | (2)               |
| – other credit risk impairment .....   | (1)               | –                 |

<sup>1</sup> Dividends and interest.

#### 5 Employee compensation and benefits

| (in millions of euros)         | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--------------------------------|-------------------|-------------------|
| Wages and salaries .....       | 722               | 678               |
| Social security costs .....    | 199               | 249               |
| Post-employment benefits ..... | 72                | 71                |
|                                | <u>993</u>        | <u>998</u>        |

The number of persons employed by the HSBC France group at the end of the year was as follows:

|   | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Retail Banking and Wealth Management and Commercial Banking ..... | 5,042             | 5,265             |
| Global Banking and Markets .....                                  | 1,161             | 1,224             |
| Asset Management .....  | 505               | 553               |
| Private Banking .....   | 134               | 208               |
| Support Functions and Others .....                                | 3,009             | 3,085             |
| <b>Total</b> .....  | <u>9,851</u>      | <u>10,335</u>     |

**Consolidated financial statements** (continued)**5 Employee compensation and benefits** (continued)**a Post-employment benefit plans**

Provisions for employee benefits cover commitments relating to end-of-career bonuses and long-service awards and commitments relating to supplementary pension schemes and early retirement plans (*Cessation d'activité des travailleurs salariés* (CATS)).

**b Post-employment defined benefit plans' principal actuarial assumptions**

The principal actuarial financial assumptions used to calculate the defined benefit pension plans at 31 December 2012, and the 2013 periodic costs, were:

| (in %)               | Discount rate | Expected rate of return on plan assets | Inflation assumption | Rate of increase for pensions in payment and deferred pensions | Rate of pay increase | Mortality rate |
|----------------------|---------------|--|----------------------|--|----------------------|----------------|
| <b>At 31.12.2012</b> |               |  |                      |  |                      |                |
| France .....         | 2.75          | 3.50 <sup>1</sup>                      | 2                    | 2  | 3                    | - <sup>2</sup> |
| <b>At 31.12.2011</b> |               |  |                      |  |                      |                |
| France .....         | 4.50          | 3.50 <sup>1</sup>                      | 2                    | 2  | 3                    | - <sup>2</sup> |

1 Expected Rate on Equities.

2 HSBC France uses "mortality tables" TV88-90 for retirement compensation and long-service awards and TGH/TGF05 for pension obligations.

HSBC France determines discount rates, in consultation with its actuary based upon the current average yield of high quality (AA rated) debt instruments, with maturities consistent with that of the pension obligations.

**c Defined benefit pension plans****Value recognised in the balance sheet**

| (in millions of euros)                      | 31.12.2012<br><i>HSBC France Pension Plan</i> | 31.12.2011<br><i>HSBC France Pension Plan</i> |
|---|---|---|
| Equities .....                              | -   | -   |
| Bonds .....                                 | 12  | 13  |
| Property .....                              | -   | -   |
| Other .....                                 | -   | -   |
| Fair value of plan assets .....             | 12  | 13  |
| Present value of funded obligations .....   | -   | -   |
| Present value of unfunded obligations ..... | (168)   | (135)   |
| Defined benefit obligation .....            | (168)   | (135)   |
| Unrecognised past service cost .....        | 4   | 5   |
| <b>Net liability .....</b>                  | <b>(152)</b>                                  | <b>(117)</b>                                  |

## 5 Employee compensation and benefits (continued)

### Changes in the present value of the defined benefit obligation

| (in millions of euros)                    | <b>31.12.2012</b>                   | 31.12.2011                          |
|---|-------------------------------------|-------------------------------------|
|   | <i>HSBC France<br/>Pension Plan</i> | <i>HSBC France<br/>Pension Plan</i> |
| At 1 January                              | 135                                 | 158                                 |
| Current service cost                      | 6                                   | 5                                   |
| Interest cost                             | 6                                   | 6                                   |
| Contributions by employees                | –                                   | –                                   |
| Actuarial (gains)/losses <sup>1</sup>     | 31                                  | 6                                   |
| Benefits paid                             | (8)                                 | (9)                                 |
| Past service cost – vested immediately    | –                                   | –                                   |
| Past service cost – unvested benefits     | (1)                                 | (1)                                 |
| Acquisitions                              | –                                   | –                                   |
| (Gains)/losses on curtailments            | –                                   | –                                   |
| (Gains)/losses on settlements             | (1)                                 | –                                   |
| Exchange and other movements <sup>2</sup> | –                                   | (30)                                |
| <b>At 31 December<sup>3</sup></b>         | <b>168</b>                          | <b>135</b>                          |

1 In 2012, total net actuarial losses included in the statement of comprehensive income were EUR 23 million in respect of defined benefit pension plans (2011: EUR 5 million).

2 In 2011, included EUR 30 million of Pension liabilities of Charterhouse Management Services Limited transferred to HSBC Bank plc (2012: Nil).

3 Of which non post-employment benefit obligations for EUR 9.7 million (2011: EUR 8.4 million) and post-employment benefit obligations for EUR 158.3 million (2011: EUR 126.6 million).

### Changes in the fair value of plan assets

| (in millions of euros)                    | <b>31.12.2012</b>                   | 31.12.2011                          |
|---|-------------------------------------|-------------------------------------|
|   | <i>HSBC France<br/>Pension Plan</i> | <i>HSBC France<br/>Pension Plan</i> |
| At 1 January                              | 13                                  | 46                                  |
| Expected return                           | 1                                   | 1                                   |
| Contributions by the group                | (2)                                 | –                                   |
| Contributions by employees                | –                                   | –                                   |
| Actuarial gain                            | –                                   | –                                   |
| Benefits paid                             | –                                   | (3)                                 |
| Acquisitions                              | –                                   | –                                   |
| (Gains)/losses on settlements             | –                                   | –                                   |
| Exchange and other movements <sup>1</sup> | –                                   | (31)                                |
| <b>At 31 December</b>                     | <b>12</b>                           | <b>13</b>                           |

1 Includes EUR 30 million of Pension Assets of Charterhouse Management Services Limited transferred to HSBC Bank plc in 2011.

### Total expense recognised in the income statement, in “Employee compensation and benefits”

| (in millions of euros)         | <b>31.12.2012</b>                   | 31.12.2011                          |
|--------------------------------|-------------------------------------|-------------------------------------|
|                                | <i>HSBC France<br/>Pension Plan</i> | <i>HSBC France<br/>Pension Plan</i> |
| Current service cost           | 6                                   | 5                                   |
| Interest cost                  | 6                                   | 6                                   |
| Expected return on plan assets | (1)                                 | (1)                                 |
| Past service cost              | –                                   | –                                   |
| (Gains)/losses on curtailments | –                                   | –                                   |
| (Gains)/losses on settlements  | (1)                                 | –                                   |
| <b>Total net expense</b>       | <b>10</b>                           | <b>10</b>                           |

## Consolidated financial statements (continued)

### 6 Share-based payments

The HSBC France group has no specific share-based payment arrangement of its own and participates in HSBC Holdings plc share option plans consisting of share-option awards and share awards.

In 2005, the HSBC Group significantly revised its share option and share policy to its employees. The new rules of share option and share plans were approved by its Annual General Meeting held in May 2005. These rules include a French sub-plan (Schedule 3 of the general rule) which complies with the legal and tax regulations applicable in France. This regulation was revised in 2011 firstly to take into account the regulatory changes impacting the plan and, secondly, to formalise the rules of the "Group Performance Share Plan", which aim the Senior Executives. In this context, the French sub-plan (Schedule 5 of the new rules) has also been subject of a review, to comply with local social and tax rules. Since 2006, the general policy of the HSBC Group is to award shares instead of share options (except in the case of specific legal and tax regulations).

#### Share Option Plan

The Group Share Options Plan was a long-term incentive plan available to certain group employees between 2000 and 2005. The aim of the plan was to align the interests of those higher performing employees to the creation of shareholder value. Options were granted at market value and are normally exercisable between the third and tenth anniversaries of the date when granted, subject to vesting conditions.

#### Share Options without performance conditions

Share options without performance conditions were granted between 2001 and 2005 to certain group employees. Options granted in 2001 and 2002 expired in 2011 and in 2012.

|                                   | 31.12.2012    |  | 31.12.2011    |  |
|-----------------------------------|---------------|--|---------------|--|
|                                   | <i>Number</i> | <i>Weighted average exercise price</i> | <i>Number</i> | <i>Weighted average exercise price</i> |
|                                   | <i>(000)</i>  | <i>(in GBP)</i>                        | <i>(000)</i>  | <i>(in GBP)</i>                        |
| Outstanding at 1 January          | 35,311        |  | 44,973        |  |
| Granted in the year               | –             |  | –             |  |
| Exercised in the year             | (388)         | 6.02                                   | (110)         | 6.02                                   |
| Transferred in the year           | –             |  | –             |  |
| Expired in the year               | (10,745)      | 7.28                                   | (9,552)       | 7.58                                   |
| <b>Outstanding at 31 December</b> | <b>24,178</b> |  | <b>35,311</b> |  |

#### Share Options with performance conditions

Share options with performance conditions were granted in 2003 and 2004 under the Rules of the HSBC Share Plan to Senior Executives in France and also to certain employees of the group; the 2011 figures now include all of these options.

|                                   | 31.12.2012    |  | 31.12.2011    |  |
|-----------------------------------|---------------|--|---------------|--|
|                                   | <i>Number</i> | <i>Weighted average exercise price</i> | <i>Number</i> | <i>Weighted average exercise price</i> |
|                                   | <i>(000)</i>  | <i>(in GBP)</i>                        | <i>(000)</i>  | <i>(in GBP)</i>                        |
| Outstanding at 1 January          | 1,343         |  | 1,343         |  |
| Granted in the year               | –             |  | –             |  |
| Exercised in the year             | –             |  | –             |  |
| Transferred in the year           | –             |  | –             |  |
| Forfeited in the year             | (23)          |  | –             |  |
| <b>Outstanding at 31 December</b> | <b>1,320</b>  |  | <b>1,343</b>  |  |

The amortisation of these plans was based on the fair value of the share-based payments transactions when contracted and runs over the three-year vesting period. These plans were completely amortised in 2008.

The HSBC Holdings plc shares held by the group to be delivered to the employees are reported in the available-for-sale portfolios and measured at fair value (quoted price).

## 6 Share-based payments (continued)

### Group share plan

The aim of the Group share plan is to recognise individual performance and to retain the highest level performing employees.

The shares can be:

- “Group Performance Shares” subject to performance conditions;
- “Restricted Shares” without performance conditions.

#### “Group Performance Shares”

|   | <b>31.12.2012</b> | 31.12.2011    |
|---|-------------------|---------------|
|   | <i>Number</i>     | <i>Number</i> |
|   | <i>(000)</i>      | <i>(000)</i>  |
| Outstanding at 1 January .....          | <b>8</b>          | –             |
| Capital increase .....                  | –                 | –             |
| Granted in the year .....               | –                 | 8             |
| Vested in the year .....                | –                 | –             |
| Transferred in the year .....           | –                 | –             |
| Expired in the year .....               | <b>(8)</b>        | –             |
| <b>Outstanding at 31 December</b> ..... | <b>–</b>          | <b>8</b>      |

This category of shares is available, beyond a vesting period of five years, at the retirement date.

#### “Restricted Shares”

These shares vest definitely after a two-year or three-year period and according to the rules of the plan. Shares granted in 2010 will vest 50 per cent after two years and 50 per cent after three years. Shares granted in 2011 and in 2012 will vest 66 per cent after two years and 34 per cent after three years.

|   | <b>31.12.2012</b> | 31.12.2011    |
|---|-------------------|---------------|
|   | <i>Number</i>     | <i>Number</i> |
|   | <i>(000)</i>      | <i>(000)</i>  |
| Outstanding at 1 January .....          | <b>9,542</b>      | 11,393        |
| Granted in the year .....               | <b>1,553</b>      | 3,717         |
| Vested in the year .....                | <b>(3,821)</b>    | (5,147)       |
| Transferred in the year .....           | –                 | –             |
| Expired in the year .....               | <b>(77)</b>       | (421)         |
| Shares issued .....                     | –                 | –             |
| <b>Outstanding at 31 December</b> ..... | <b>7,197</b>      | <b>9,542</b>  |

This category of shares cannot be sold before the end of a further two-year tax lock-up period after their vesting.

In 2011, EUR 40 million was charged to the income statement in respect of amortisation of the existing plans.

Regulatory and best practice guidance has clarified the required structure and terms of the vesting period that should be recognised in the financial statements of HSBC France. As a result, the vesting period for deferred share awards expected to be granted in 2013, in respect of the 2012 performance year, was determined to have started on 1 January 2012. Prior 2011, the charge started at the date of grant of the shares.

#### Employee share offering

In 2012, the HSBC Group made an employee share offering open to current employees. Employees of the HSBC France group took up a total of 2,274,523 HSBC Holdings plc shares, representing a total capital amount of EUR 12.9 million.

The cost of the discount based on the share price at the opening of the offer period amounted to EUR 3.7 million for the Group.

**Consolidated financial statements** (continued)**7 Tax expense**

| (in millions of euros)              | <b>31.12.2012</b> | 31.12.2011  |
|-------------------------------------|-------------------|-------------|
| Current tax .....                   | <b>106</b>        | (11)        |
| Deferred tax .....                  | <b>(39)</b>       | (55)        |
| <b>Tax expense</b> .....            | <b>67</b>         | <b>(66)</b> |
| Effective tax rate (per cent) ..... | <b>17.3</b>       | N/A         |

As mentioned in Note 2 s, pages 117 and 118, the CVAE contribution recorded in 2012 is included in "Income Tax". The impact of this accounting position was, in 2012, a classification of a charge of EUR 16 million (2011: EUR 17 million) on the "Tax Expenses" and the recognition of a deferred tax asset of EUR 4 million (2011: deferred tax liability: EUR 1 million).

Since 2011, France's tax rate increased from 34.43 per cent to 36.10 per cent for all companies which have a turnover over EUR 250 million.

Although deemed to be temporary up to 2012, the 2013 Finances Law ("*Loi de Finances*") proposes to maintain the additional 5 per cent tax for the 2013 and 2014 closing exercises.

In 2011, France tax group incurred a loss. The deferred tax asset for the carryforward of unused tax losses recognised at that time was utilised against 2012 taxable profit.

**Analysis of overall tax charges**

| (in millions of euros)  | <b>31.12.2012</b> |                | 31.12.2011    |            |
|---|-------------------|----------------|---------------|------------|
|   | <i>Amount</i>     | %              | <i>Amount</i> | %          |
| Taxation at French corporate tax rate .....   | <b>140</b>        | <b>36.08</b>   | 21            | 36.10      |
| Impact of overseas profits in principal locations<br>taxed at different rates ..... | <b>(2)</b>        | <b>(0.52)</b>  | –             | (0.46)     |
| Operations taxed at reduced tax rate in France .....                                | <b>(7)</b>        | <b>(1.80)</b>  | (16)          | (27.13)    |
| Other items including result for tax Group<br>integration .....                     | <b>(64)</b>       | <b>(16.49)</b> | (71)          | (119.67)   |
| <b>Overall tax charge</b> .....   | <b>67</b>         | <b>17.27</b>   | <b>(66)</b>   | <b>N/A</b> |



## 8 Dividends paid in 2012 and 2011

| (in millions of euros)                        | 31.12.2012           |               | 31.12.2011           |               |
|---|----------------------|---------------|----------------------|---------------|
|   | <i>EUR per share</i> | <i>Amount</i> | <i>EUR per share</i> | <i>Amount</i> |
| First interim dividend for current year ..... | –                    | –             | 1.75                 | 118           |
|   |                      | –             |                      | 118           |

### Dividends related to 2012

On 27 February 2013, the Board of Directors approved an interim dividend of EUR 3.56 per share in respect of the 2012 results. This interim dividend was paid on 1 March 2013.

The Board of Directors also proposed that at the Annual General Meeting, to be held on 30 April 2013, not to distribute any further dividend in respect of the 2012 results.

### Dividends related to 2011

On 26 July 2011, the Board of Directors approved an interim dividend of EUR 1.75 per share. This dividend was paid with respect to the 67,437,820 shares in issue at that date. The interim dividend was paid on 3 August 2011.

On 22 February 2012, the Board of Directors proposed at the Annual General Meeting held on 15 May 2012, to distribute a dividend of a total amount of EUR 118,016,197.25 in respect of the 2011 results. The dividend, approved by the shareholders, was paid on 1 June 2012, after deduction of the interim dividend of EUR 1.75 per share voted by the Board of Directors at its meeting of 26 July 2011 and already paid to shares issued as of that date.

## 9 Earnings and dividends per share

| (in euros)                       | 31.12.2012 | 31.12.2011 |
|----------------------------------|------------|------------|
| Basic earnings per share .....   | 4.75       | 1.83       |
| Diluted earnings per share ..... | 4.75       | 1.83       |
| Dividend per share .....         | 3.56       | 1.75       |

Basic earnings per ordinary share were calculated by dividing the earnings of EUR 320 million by the weighted average number of ordinary shares outstanding during the year, excluding own shares held, of 67,437,827 (full year 2011: earnings of EUR 123 million and 67,437,821 weighted average number of shares).

Diluted earnings per share were calculated by dividing the basic earnings, which require no adjustment for the dilutive of potential ordinary shares (including share options outstanding not yet exercised), by the weighted average number of ordinary shares outstanding, excluding own shares held, plus the weighted average number of ordinary shares that would be issued on ordinary conversion of all the potential dilutive ordinary shares of 67,437,827 (full year 2011: 67,437,821 shares).

## Consolidated financial statements (continued)

### 10 Segment analysis

The HSBC Group in France includes on the one hand the HSBC France group, and on the other hand the branch of HSBC Bank plc located in Paris, which is engaged in equity derivatives activities as well as HSBC Assurances Vie (France) and HSBC Assurances IARD (France), to the exclusion of the costs of funding and the debt on acquisition recognised by HSBC Bank plc Paris Branch.

The HSBC Group in France provides a comprehensive range of banking and related financial services to its customers. Products and services offered to customers are organised along the following business lines:

- Retail Banking and Wealth Management (including the Insurance and Asset Management business lines) offers a wide range of products and services to meet the retail banking and wealth management requirements of individual clients and professionals. The products offered include current accounts and the related payment and financial services, savings products and solutions for wealth accumulation, as well as mortgages and other loans to individuals and professionals. In the HSBC Group, life insurance business is accounted for using the embedded value approach which, *inter alia*, provides a risk and valuation framework. The present value of in-force long-term insurance business (“PVIF”) represents the present value of the shareholders’ interest in the profits expected to emerge from the book of in-force policies at that date. The PVIF calculation projects expected cash flows, adjusted for a variety of assumptions made by each insurance operation to reflect local market conditions and management’s judgement of future trends. The main assumptions relate to economic and non-economic assumptions and policyholder behaviour. Assumptions are subject to uncertainty and can contribute to volatility in the results of the Insurance business (see HSBC Holdings plc Annual Report and Accounts 2012 page 243).
- Commercial Banking offers its clients financial services, payment and cash management services, international financing, insurance, treasury operations, as well as capital market and other investment banking services.
- Global Banking and Markets provides tailored financial solutions to large corporate and institutional clients, governments and public-sector agencies. The global businesses offer a full range of investment banking and financing services as well as capital markets services in the field of credit, interest rates, foreign exchange, equities, money markets and securities administration.
- The services offered by Private Banking are designed to meet the needs of high-net worth individual customers in the field of banking services, investment advisory and wealth management.

The “Other” segment mainly includes the fair value variation of HSBC France’s own credit spread on issued debt under fair value option for EUR -118 million (2011: EUR 124 million).

HSBC France is supported by various central administrative and corporate functions whose costs are systematically and consistently allocated to the business lines.

Performance is assessed on the basis of the pre-tax profits of the business line, as set out in the internal management reports reviewed by the Group’s Executive Management.

No geographical information is given, as this information is not relevant for the HSBC France group which mainly operates in France.

## 10 Segment analysis (continued)

Profit/(loss) for the year on the managed perimeter

31.12.2012

| (in millions of euros)  | <i>Retail<br/>Banking<br/>and<br/>Wealth<br/>Manage-<br/>ment</i> | <i>Com-<br/>mercial<br/>Banking</i> | <i>Global<br/>Banking<br/>and<br/>Markets</i> | <i>Private<br/>Banking</i> | <i>Other</i> | <i>Inter-<br/>segment</i> | <i>Total</i>   |
|---|---|-------------------------------------|---|----------------------------|--------------|---------------------------|----------------|
| Interest income .....   | 941   | 403                                 | 759   | 22                         | 47           | –                         | 2,172          |
| Interest expense .....  | (86)  | (8)                                 | (486)   | (4)                        | (51)         | (39)                      | (674)          |
| Net interest income .....   | 855   | 395                                 | 273   | 18                         | (4)          | (39)                      | 1,498          |
| Other operating income .....                                      | 40  | 242                                 | 639   | 27                         | (94)         | 39                        | 893            |
| <b>Total operating income</b> .....                               | <b>895</b>  | <b>637</b>                          | <b>912</b>                                    | <b>45</b>                  | <b>(98)</b>  | <b>–</b>                  | <b>2,391</b>   |
| Loan impairment charges<br>and other credit risk provisions ..... | (23)  | (78)                                | (17)  | 1                          | –            | –                         | (117)          |
| <b>Net operating income</b> .....                                 | <b>872</b>  | <b>559</b>                          | <b>895</b>                                    | <b>46</b>                  | <b>(98)</b>  | <b>–</b>                  | <b>2,274</b>   |
| <b>Total operating expenses</b> .....                             | <b>(767)</b>  | <b>(401)</b>                        | <b>(485)</b>                                  | <b>(55)</b>                | <b>(7)</b>   | <b>–</b>                  | <b>(1,715)</b> |
| <b>Operating profit</b> .....                                     | <b>105</b>  | <b>158</b>                          | <b>410</b>                                    | <b>(9)</b>                 | <b>(105)</b> | <b>–</b>                  | <b>559</b>     |
| Share of profit in associates<br>and joint ventures .....         | –   | –                                   | –   | –                          | –            | –                         | –              |
| <b>Profit before tax</b> .....                                    | <b>105</b>  | <b>158</b>                          | <b>410</b>                                    | <b>(9)</b>                 | <b>(105)</b> | <b>–</b>                  | <b>559</b>     |
| Tax expense .....   |   |                                     |   |                            |              |                           | (127)          |
| <b>Profit for the year – France</b> .....                         |   |                                     |   |                            |              |                           | <b>432</b>     |
| Perimeter differences <sup>1</sup> .....                          |   |                                     |   |                            |              |                           | (111)          |
| <b>Profit for the year – Legal</b> .....                          |   |                                     |   |                            |              |                           | <b>321</b>     |

<sup>1</sup> Mainly Insurance.

**Consolidated financial statements** (continued)**10 Segment analysis** (continued)

31.12.2011

| (in millions of euros)  | <i>Retail<br/>Banking<br/>and<br/>Wealth<br/>Manage-<br/>ment</i> | <i>Com-<br/>mercial<br/>Banking</i> | <i>Global<br/>Banking<br/>and<br/>Markets</i> | <i>Private<br/>Banking</i> | <i>Other</i> | <i>Inter-<br/>segment</i> | <i>Total</i> |
|---|---|-------------------------------------|---|----------------------------|--------------|---------------------------|--------------|
| Interest income .....   | 977   | 501                                 | 1,084   | 19                         | (6)          | –                         | 2,575        |
| Interest expense .....  | (102)   | (86)                                | (844)   | 3                          | (8)          | (156)                     | (1,193)      |
| Net interest income .....   | 875   | 415                                 | 240   | 22                         | (14)         | (156)                     | 1,382        |
| Other operating income .....                                      | 19  | 219                                 | 105   | 52                         | 132          | 156                       | 683          |
| Total operating income .....                                      | 894   | 634                                 | 345   | 74                         | 118          | –                         | 2,065        |
| Loan impairment charges<br>and other credit risk provisions ..... | (38)  | (83)                                | (6)   | –                          | –            | –                         | (127)        |
| Net operating income .....  | 856   | 551                                 | 339   | 74                         | 118          | –                         | 1,938        |
| Total operating expenses .....                                    | (806)   | (413)                               | (468)   | (63)                       | 3            | –                         | (1,747)      |
| Operating profit .....  | 50  | 138                                 | (129)   | 11                         | 121          | –                         | 191          |
| Share of profit in associates<br>and joint ventures .....         | –   | –                                   | –   | –                          | –            | –                         | –            |
| Profit before tax .....   | 50  | 138                                 | (129)   | 11                         | 121          | –                         | 191          |
| Tax expense .....   |   |                                     |   |                            |              |                           | 21           |
| Profit for the year – France .....                                |   |                                     |   |                            |              |                           | 212          |
| Perimeter differences <sup>1</sup> .....                          |   |                                     |   |                            |              |                           | (88)         |
| Profit for the year – Legal .....                                 |   |                                     |   |                            |              |                           | 124          |

<sup>1</sup> Mainly Insurance.

## 10 Segment analysis (continued)

Other information about the profit/(loss) for the year on the managed perimeter

| (in millions of euros)   | <i>Retail<br/>Banking<br/>and<br/>Wealth<br/>Manage-<br/>ment</i> | <i>Com-<br/>mercial<br/>Banking</i> | <i>Global<br/>Banking<br/>and<br/>Markets</i> | <i>Private<br/>Banking</i> | <i>Other</i> | <i>Inter<br/>Segment</i> | <i>Total</i> |
|--|---|-------------------------------------|---|----------------------------|--------------|--------------------------|--------------|
| <b>31 December 2012</b>  |   |                                     |   |                            |              |                          |              |
| Net operating income.....  | 872   | 559                                 | 895   | 46                         | (98)         | –                        | 2,274        |
| – external .....   | 896   | 508                                 | 870   | 38                         | (104)        | –                        | 2,208        |
| – inter-segment .....  | (24)  | 51                                  | 25  | 8                          | 6            | –                        | 66           |
| Profit before tax includes the following   |   |                                     |   |                            |              |                          |              |
| significant non-cash items.....  | 105   | 158                                 | 410   | (9)                        | (105)        | –                        | 559          |
| – depreciation, amortisation and impairment  | (3)   | –                                   | –   | –                          | (53)         | –                        | (56)         |
| – loan impairment losses gross of recoveries<br>and other credit risk provisions ..... | (23)  | (78)                                | (17)  | 1                          | –            | –                        | (117)        |
| – impairment of financial investments .....  | –   | –                                   | –   | –                          | (1)          | –                        | (1)          |
| <b>31 December 2011</b>  |   |                                     |   |                            |              |                          |              |
| Net operating income.....  | 856   | 551                                 | 339   | 74                         | 118          | –                        | 1,938        |
| – external .....   | 864   | 463                                 | 259   | 68                         | 219          | –                        | 1,873        |
| – inter-segment .....  | (8)   | 88                                  | 80  | 6                          | (101)        | –                        | 65           |
| Profit before tax includes the following   |   |                                     |   |                            |              |                          |              |
| significant non-cash items.....  | 50  | 138                                 | (129)   | 11                         | 121          | –                        | 191          |
| – depreciation, amortisation and impairment  | (16)  | (11)                                | (5)   | –                          | (25)         | –                        | (57)         |
| – loan impairment losses gross of recoveries<br>and other credit risk provisions ..... | (38)  | (83)                                | (6)   | –                          | –            | –                        | (127)        |
| – impairment of financial investments .....  | –   | –                                   | (2)   | –                          | (1)          | –                        | (3)          |

**Consolidated financial statements** (continued)**10 Segment analysis** (continued)**Balance sheet information**

| (in millions of euros)                              | <i>Retail<br/>Banking<br/>and<br/>Wealth<br/>Manage-<br/>ment</i> | <i>Com-<br/>mercial<br/>Banking</i> | <i>Global<br/>Banking<br/>and<br/>Markets</i> | <i>Private<br/>Banking</i> | <i>Other</i> | <i>Inter<br/>Segment</i> | <i>Total</i>   |
|---|---|-------------------------------------|---|----------------------------|--------------|--------------------------|----------------|
| <b>31 December 2012</b>                             |   |                                     |   |                            |              |                          |                |
| Loans and advances to customers (net) . . . .       | <b>13,726</b>   | <b>10,590</b>                       | <b>23,353</b>                                 | <b>685</b>                 | –            | –                        | <b>48,354</b>  |
| Investment in associates and joint ventures . .     | <b>1</b>  | –                                   | <b>5</b>                                      | –                          | –            | –                        | <b>6</b>       |
| Total assets . . . . .                              | <b>17,586</b>   | <b>13,728</b>                       | <b>200,270</b>                                | <b>712</b>                 | <b>323</b>   | <b>(7,411)</b>           | <b>225,208</b> |
| Customer accounts . . . . .                         | <b>13,051</b>   | <b>9,877</b>                        | <b>18,880</b>                                 | <b>556</b>                 | –            | –                        | <b>42,364</b>  |
| Total liabilities . . . . .                         | <b>17,586</b>   | <b>13,728</b>                       | <b>200,270</b>                                | <b>712</b>                 | <b>323</b>   | <b>(7,411)</b>           | <b>225,208</b> |
| Capital expenditure incurred <sup>1</sup> . . . . . | <b>40</b>   | <b>25</b>                           | <b>22</b>                                     | –                          | –            | –                        | <b>87</b>      |
| <b>31 December 2011</b>                             |   |                                     |   |                            |              |                          |                |
| Loans and advances to customers (net) . . . .       | 12,577  | 10,282                              | 29,694  | 726                        | –            | –                        | 53,279         |
| Investment in associates and joint ventures . .     | 1   | –                                   | 5   | –                          | –            | –                        | 6              |
| Total assets . . . . .                              | 15,985  | 13,577                              | 197,600                                       | 675                        | 324          | (6,771)                  | 221,390        |
| Customer accounts . . . . .                         | 12,523  | 9,836                               | 20,157  | 380                        | –            | –                        | 42,896         |
| Total liabilities . . . . .                         | 15,985  | 13,577                              | 197,600                                       | 675                        | 324          | (6,771)                  | 221,390        |
| Capital expenditure incurred <sup>1</sup> . . . . . | 43  | 25                                  | 29  | –                          | –            | –                        | 97             |

<sup>1</sup> Expenditure incurred on property, plant and equipment and other intangible assets. Excludes assets acquired as part of business combination and goodwill.

**11 Analysis of financial assets and liabilities by measurement basis**

Financial assets and financial liabilities are measured on an ongoing basis either at fair value or at amortised cost. The principal accounting policies in Note 2 describe how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the financial assets and liabilities on the balance sheet by the class of financial instrument to which they are assigned, and therefore by the measurement basis.

**11 Analysis of financial assets and liabilities by measurement basis (continued)**

31.12.2012

|  | Held for trading | Designated at fair value | Loans and receivables | Available-for-sale securities | Financial assets and liabilities at amortised cost | Derivatives designated as fair value hedging instruments | Derivatives designated as cash flow hedging instruments | Total          |
|--|------------------|--------------------------|-----------------------|-------------------------------|--|--|---|----------------|
| <b>Financial assets</b>                            |                  |                          |                       |                               |  |  |   |                |
| Cash and balances at central banks                 | -                | -                        | -                     | -                             | 6,770  | -  | -   | 6,770          |
| Items in the course of collection from other banks | -                | -                        | -                     | -                             | 815  | -  | -   | 815            |
| Trading assets                                     | 40,577           | -                        | -                     | -                             | -  | -  | -   | 40,577         |
| Financial assets designated at fair value          | -                | 5                        | -                     | -                             | -  | -  | -   | 5              |
| Derivatives  | 89,420           | -                        | -                     | -                             | -  | 10   | 828   | 90,258         |
| Loans and advances to banks                        | -                | -                        | 28,132                | -                             | -  | -  | -   | 28,132         |
| Loans and advances to customers                    | -                | -                        | 48,354                | -                             | -  | -  | -   | 48,354         |
| Financial investments                              | -                | -                        | -                     | 8,258                         | -  | -  | -   | 8,258          |
| Other assets                                       | -                | -                        | -                     | -                             | 228  | -  | -   | 228            |
| Accrued income                                     | -                | -                        | -                     | -                             | 865  | -  | -   | 865            |
| <b>Total financial assets</b>                      | <b>129,997</b>   | <b>5</b>                 | <b>76,486</b>         | <b>8,258</b>                  | <b>8,678</b>                                       | <b>10</b>  | <b>828</b>  | <b>224,262</b> |
| Assets classified as held for sale                 | -                | -                        | -                     | -                             | -  | -  | -   | -              |
| Total non-financial assets                         | -                | -                        | -                     | -                             | -  | -  | -   | 946            |
| <b>Total assets</b>                                |                  |                          |                       |                               |  |  |   | <b>225,208</b> |
| <b>Financial Liabilities</b>                       |                  |                          |                       |                               |  |  |   |                |
| Deposits by banks                                  | -                | -                        | -                     | -                             | 32,992   | -  | -   | 32,992         |
| Customer accounts                                  | -                | -                        | -                     | -                             | 42,364   | -  | -   | 42,364         |
| Items in the course of transmission to other banks | -                | -                        | -                     | -                             | 771  | -  | -   | 771            |
| Trading liabilities                                | 36,271           | -                        | -                     | -                             | -  | -  | -   | 36,271         |
| Financial liabilities designated at fair value     | -                | 5,654                    | -                     | -                             | -  | -  | -   | 5,654          |
| Derivatives  | 87,979           | -                        | -                     | -                             | -  | 407  | 728   | 89,114         |
| Debt securities in issue                           | -                | -                        | -                     | -                             | 10,655   | -  | -   | 10,655         |
| Other liabilities                                  | -                | -                        | -                     | -                             | 539  | -  | -   | 539            |
| Subordinated liabilities                           | -                | -                        | -                     | -                             | 166  | -  | -   | 166            |
| Accruals   | -                | -                        | -                     | -                             | 1,143  | -  | -   | 1,143          |
| <b>Total financial liabilities</b>                 | <b>124,250</b>   | <b>5,654</b>             | -                     | -                             | <b>88,630</b>                                      | <b>407</b>   | <b>728</b>  | <b>219,669</b> |
| Liabilities classified as held for sale            | -                | -                        | -                     | -                             | -  | -  | -   | -              |
| Total non-financial liabilities                    | -                | -                        | -                     | -                             | -  | -  | -   | 5,539          |
| <b>Total liabilities</b>                           |                  |                          |                       |                               |  |  |   | <b>225,208</b> |

## Consolidated financial statements (continued)

## 11 Analysis of financial assets and liabilities by measurement basis (continued)

31.12.2011

| (in millions of euros)                             | Held for trading | Designated at fair value | Loans and receivables | Available-for-sale securities | Financial assets and liabilities at amortised cost | Derivatives designated as fair value hedging instruments | Derivatives designated as cash flow hedging instruments | Total          |
|--|------------------|--------------------------|-----------------------|-------------------------------|--|--|---|----------------|
| <b>Financial assets</b>                            |                  |                          |                       |                               |  |  |   |                |
| Cash and balances at central banks                 | -                | -                        | -                     | -                             | 4,805  | -  | -   | 4,805          |
| Items in the course of collection from other banks | -                | -                        | -                     | -                             | 806  | -  | -   | 806            |
| Trading assets                                     | 39,013           | -                        | -                     | -                             | -  | -  | -   | 39,013         |
| Financial assets designated at fair value          | -                | 598                      | -                     | -                             | -  | -  | -   | 598            |
| Derivatives  | 82,079           | -                        | -                     | -                             | -  | 12   | 647   | 82,738         |
| Loans and advances to banks                        | -                | -                        | 29,705                | -                             | -  | -  | -   | 29,705         |
| Loans and advances to customers                    | -                | -                        | 53,279                | -                             | -  | -  | -   | 53,279         |
| Financial investments                              | -                | -                        | -                     | 7,518                         | -  | -  | -   | 7,518          |
| Other assets                                       | -                | -                        | -                     | -                             | 969  | -  | -   | 969            |
| Accrued income                                     | -                | -                        | -                     | -                             | 946  | -  | -   | 946            |
| <b>Total financial assets</b>                      | <b>121,092</b>   | <b>598</b>               | <b>82,984</b>         | <b>7,518</b>                  | <b>7,526</b>                                       | <b>12</b>  | <b>647</b>  | <b>220,377</b> |
| <b>Assets classified as held for sale</b>          |                  |                          |                       |                               |  |  |   |                |
| Total non-financial assets                         | -                | -                        | -                     | -                             | -  | -  | -   | 5              |
| <b>Total assets</b>                                |                  |                          |                       |                               |  |  |   | <b>221,390</b> |
| <b>Financial Liabilities</b>                       |                  |                          |                       |                               |  |  |   |                |
| Deposits by banks                                  | -                | -                        | -                     | -                             | 32,338   | -  | -   | 32,338         |
| Customer accounts                                  | -                | -                        | -                     | -                             | 42,896   | -  | -   | 42,896         |
| Items in the course of transmission to other banks | -                | -                        | -                     | -                             | 757  | -  | -   | 757            |
| Trading liabilities                                | 38,257           | -                        | -                     | -                             | -  | -  | -   | 38,257         |
| Financial liabilities designated at fair value     | -                | 5,527                    | -                     | -                             | -  | -  | -   | 5,527          |
| Derivatives  | 80,980           | -                        | -                     | -                             | -  | 206  | 495   | 81,681         |
| Debt securities in issue                           | -                | -                        | -                     | -                             | 12,605   | -  | -   | 12,605         |
| Other liabilities                                  | -                | -                        | -                     | -                             | 837  | -  | -   | 837            |
| Subordinated liabilities                           | -                | -                        | -                     | -                             | 166  | -  | -   | 166            |
| Accruals   | -                | -                        | -                     | -                             | 1,217  | -  | -   | 1,217          |
| <b>Total financial liabilities</b>                 | <b>119,237</b>   | <b>5,527</b>             |                       |                               | <b>90,816</b>                                      | <b>206</b>   | <b>495</b>  | <b>216,281</b> |
| <b>Liabilities classified as held for sale</b>     |                  |                          |                       |                               |  |  |   |                |
| Total non-financial liabilities                    | -                | -                        | -                     | -                             | -  | -  | -   | -              |
| <b>Total liabilities</b>                           |                  |                          |                       |                               |  |  |   | <b>5,109</b>   |
| <b>Total liabilities</b>                           |                  |                          |                       |                               |  |  |   | <b>221,390</b> |



## 12 Trading assets

| (in millions of euros)                                      | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Trading assets:   |                   |            |
| – which may be repledged or resold by counterparties .....  | <b>21,250</b>     | 16,670     |
| – not subject to repledge or resale by counterparties ..... | <b>19,327</b>     | 22,343     |
|   | <b>40,577</b>     | 39,013     |
| <br>  |                   |            |
| (in millions of euros)                                      | <b>31.12.2012</b> | 31.12.2011 |
| Treasury and other eligible bills .....                     | <b>1,392</b>      | 669        |
| Debt securities .....                                       | <b>25,130</b>     | 24,762     |
| Loans and advances to banks .....                           | <b>11,320</b>     | 10,531     |
| Loans and advances to customers .....                       | <b>2,735</b>      | 3,021      |
|   | <b>40,577</b>     | 39,013     |

## 13 Derivatives

Fair values of third-party derivatives open positions by type of product contract:

| (in millions of euros)               | <b>31.12.2012</b> |                |                 |                    |                |                  |
|--------------------------------------|-------------------|----------------|-----------------|--------------------|----------------|------------------|
|                                      | <i>Assets</i>     |                |                 | <i>Liabilities</i> |                |                  |
|                                      | <i>Trading</i>    | <i>Hedging</i> | <i>Total</i>    | <i>Trading</i>     | <i>Hedging</i> | <i>Total</i>     |
| Exchange rate .....                  | <b>3,917</b>      | –              | <b>3,917</b>    | <b>(4,179)</b>     | –              | <b>(4,179)</b>   |
| Interest rate .....                  | <b>179,574</b>    | <b>838</b>     | <b>180,412</b>  | <b>(177,870)</b>   | <b>(1,135)</b> | <b>(179,005)</b> |
| Equities .....                       | <b>2</b>          | –              | <b>2</b>        | <b>(2)</b>         | –              | <b>(2)</b>       |
| Credit derivatives .....             | –                 | –              | –               | <b>(1)</b>         | –              | <b>(1)</b>       |
| Commodity and other .....            | –                 | –              | –               | –                  | –              | –                |
| <b>Gross total fair values</b> ..... | <b>183,493</b>    | <b>838</b>     | <b>184,331</b>  | <b>(182,052)</b>   | <b>(1,135)</b> | <b>(183,187)</b> |
| Netting .....                        |                   |                | <b>(94,073)</b> |                    |                | <b>94,073</b>    |
| <b>Net total</b> .....               |                   |                | <b>90,258</b>   |                    |                | <b>(89,114)</b>  |
| <br>                                 |                   |                |                 |                    |                |                  |
|                                      | 31.12.2011        |                |                 |                    |                |                  |
|                                      | <i>Assets</i>     |                |                 | <i>Liabilities</i> |                |                  |
|                                      | <i>Trading</i>    | <i>Hedging</i> | <i>Total</i>    | <i>Trading</i>     | <i>Hedging</i> | <i>Total</i>     |
| Exchange rate .....                  | 5,576             | –              | 5,576           | (5,502)            | (1)            | (5,503)          |
| Interest rate .....                  | 147,794           | 659            | 148,453         | (146,721)          | (700)          | (147,421)        |
| Equities .....                       | 2                 | –              | 2               | (1)                | –              | (1)              |
| Credit derivatives .....             | 6                 | –              | 6               | (55)               | –              | (55)             |
| Commodity and other .....            | –                 | –              | –               | –                  | –              | –                |
| <b>Gross total fair values</b> ..... | <b>153,378</b>    | <b>659</b>     | <b>154,037</b>  | <b>(152,279)</b>   | <b>(701)</b>   | <b>(152,980)</b> |
| Netting .....                        |                   |                | <b>(71,299)</b> |                    |                | <b>71,299</b>    |
| <b>Net total</b> .....               |                   |                | <b>82,738</b>   |                    |                | <b>(81,681)</b>  |

**Consolidated financial statements** (continued)**13 Derivatives** (continued)**a Use of derivatives**

HSBC France transacts derivatives for three primary purposes: to create risk management solutions for clients, for proprietary trading purposes and to manage and hedge the HSBC France 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 second held-for-trading category includes derivatives managed in conjunction with financial instruments designated at fair value. These activities are described in more detail below.

The HSBC France 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 utilised to achieve this where necessary. When entering into derivative transactions, the HSBC France group employs the same credit risk management procedures to assess and approve potential credit exposures as are used for traditional lending.

**b Trading derivatives**

Most of the HSBC France group's derivative transactions relate to 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. Trading activities in derivatives are entered into principally for the purpose of generating profits from short-term fluctuations in price or margin. Positions may be traded actively or be held over a period of time to benefit from expected changes in currency rates, interest rates, equity prices or other market parameters. Trading includes market-making, positioning and arbitrage activities. Market-making entails quoting bid and offer prices to other market participants for the purpose of generating revenues based on spread and volume; positioning means managing market risk positions in the expectation of benefitting from favourable movements in prices, rates or indices; arbitrage involves identifying and profiting from price differentials between markets and products.

As mentioned above, other derivatives classified as held-for-trading 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. These include derivatives managed in conjunction with financial instruments designated at fair value.

Ineffective hedging derivatives were previously designated as hedges, but no longer 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 "Trading income", except for derivatives managed in conjunction with financial instruments designated at fair value, where gains and losses are reported in "Net income from financial instruments designated at fair value".

*Notional contract amounts of derivatives held-for-trading purposes by product type*

| (in millions of euros)    | <b>31.12.2012</b> | 31.12.2011       |
|---------------------------|-------------------|------------------|
| Exchange rate .....       | <b>148,783</b>    | 187,472          |
| Interest rate .....       | <b>4,657,891</b>  | 4,918,658        |
| Equities .....            | <b>41</b>         | 80               |
| Credit derivatives .....  | <b>135</b>        | 775              |
| Commodity and other ..... | -                 | -                |
| <b>Total</b> .....        | <b>4,806,850</b>  | <b>5,106,985</b> |

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.

The contract amount of credit derivatives of EUR 135 million (2011: EUR 775 million) listed above consists of protection bought for EUR 135 million (2011: EUR 775 million) and without protection sold.

### 13 Derivatives (continued)

#### Derivatives valued using models with unobservable inputs

The difference between the fair value at initial recognition (the transaction price) and the value that would have been derived had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

| (in millions of euros)                                | 2012     | 2011     |
|---|----------|----------|
| <b>Unamortised balance at 1 January</b> .....         | <b>4</b> | <b>6</b> |
| Deferral on new transactions .....                    | –        | –        |
| Recognised in the income statement during the period: |          |          |
| – amortisation .....                                  | –        | –        |
| – subsequent to observability .....                   | –        | (2)      |
| – maturity or termination .....                       | –        | –        |
| – FX movements and other .....                        | –        | –        |
| <b>Unamortised balance at 31 December</b> .....       | <b>4</b> | <b>4</b> |

#### c Hedging instruments

HSBC France uses derivatives (principally interest rate swaps) for hedging purposes in the management of its own asset and liability portfolios and structural positions. This enables the group to optimise the overall cost of accessing debt capital markets, and to mitigate the market risk which would otherwise arise from structural imbalances in the maturity and other profiles of its assets and liabilities.

The accounting treatment of hedge transactions varies according to the nature of the instrument hedged and the type of hedge transactions. Derivatives may qualify as hedges for accounting purposes if they are fair value hedges, or cash flow hedges. These are described under the relevant headings below.

At 31 December 2012 and 31 December 2011, HSBC France does not hold derivatives designated as “net investment hedge”.

The table below shows the notional contract amount of derivatives held for hedging purposes by product type:

| (in millions of euros)        | 31.12.2012                 |                             | 31.12.2011                 |                             |
|-------------------------------|----------------------------|-----------------------------|----------------------------|-----------------------------|
|                               | <i>Cash flow<br/>hedge</i> | <i>Fair value<br/>hedge</i> | <i>Cash flow<br/>hedge</i> | <i>Fair value<br/>hedge</i> |
| Exchange rate contracts ..... | –                          | <b>85</b>                   | –                          | 81                          |
| Interest rate contracts ..... | <b>48,791</b>              | <b>6,737</b>                | 67,814                     | 6,617                       |
| Equity 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.

#### Fair value hedges

The HSBC France group’s fair value hedges principally consist of interest rate swaps that are used to protect against changes due to movements in market interest rates in the fair value of fixed-rate long-term financial instruments of Available for sale (AFS) portfolio and lease operations. For qualifying fair value hedges, all changes in the fair value of the derivative and in the fair value of the item in relation to the risk being hedged are recognised in income. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortised to income as a yield adjustment over the remainder of the hedging period.

The fair values of outstanding derivatives designated as fair value hedges at 31 December 2012, were assets of EUR 10 million and liabilities of EUR 407 million (31 December 2011: assets of EUR 12 million and liabilities of EUR 206 million).

Gains or losses arising from the change in fair value of fair value hedges:

| (in millions of euros)                                | 31.12.2012   | 31.12.2011 |
|---|--------------|------------|
| On hedging instruments .....                          | <b>(190)</b> | (154)      |
| On hedged items attributable to the hedged risk ..... | <b>187</b>   | 153        |

The amount reported in the income statement in respect of the ineffectiveness of fair value hedges was a loss of EUR 3 million for the year ended 31 December 2012 (a loss of EUR 0.2 million for the year ended 31 December 2011).

**Consolidated financial statements** (continued)**13 Derivatives** (continued)*Cash flow hedges*

The HSBC France group is exposed to variability in future interest cash flows on non-trading assets and liabilities which bear interest at variable rates or which are expected to be re-funded or reinvested in the future. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their contractual terms and other relevant factors, including estimates of prepayments and defaults. The aggregate principal balances and interest cash flows across all portfolios over time, form the basis for identifying gains and losses on the effective portions of derivatives designated as cash flow hedges of forecast transactions. These are initially recognised directly in equity as gains or losses not recognised in the income statement and are transferred to current period earnings when the forecast cash flows affect net profit or loss.

At 31 December 2012, the fair values of outstanding derivatives designated as cash flow hedges of forecast transactions were assets of EUR 828 million and liabilities of EUR 728 million (at 31 December 2011: assets of EUR 647 million and liabilities of EUR 495 million).

The schedule of forecast principal balances on which the expected interest cash flows arise as at 31 December is as follows:

|  | 31.12.2012                  |  |   |                              |
|--|-----------------------------|--|---|------------------------------|
|  | <i>3 months<br/>or less</i> | <i>More than<br/>3 months<br/>but less<br/>than 1 year</i> | <i>Less than<br/>5 years<br/>but more<br/>than 1 year</i> | <i>More than<br/>5 years</i> |
| (in millions of euros)                   |                             |  |   |                              |
| Cash inflows from assets .....           | 18,757                      | 9,524  | 9,339   | 3,604                        |
| Cash outflows from liabilities .....     | (16,751)                    | (7,708)  | (4,104)   | (1,343)                      |
| <b>Net cash inflows/(outflows) .....</b> | <b>2,006</b>                | <b>1,816</b>   | <b>5,235</b>  | <b>2,261</b>                 |

|  | 31.12.2011                  |  |   |                              |
|--|-----------------------------|--|---|------------------------------|
|  | <i>3 months<br/>or less</i> | <i>More than<br/>3 months<br/>but less<br/>than 1 year</i> | <i>Less than<br/>5 years<br/>but more<br/>than 1 year</i> | <i>More than<br/>5 years</i> |
| (in millions of euros)                   |                             |  |   |                              |
| Cash inflows from assets .....           | 31,374                      | 17,919   | 8,919   | 2,570                        |
| Cash outflows from liabilities .....     | (22,488)                    | (10,946)   | (3,387)   | (829)                        |
| <b>Net cash inflows/(outflows) .....</b> | <b>8,886</b>                | <b>6,973</b>   | <b>5,532</b>  | <b>1,741</b>                 |

## Reconciliation of movements in the cash flow hedge reserve

| (in millions of euros)  | 2012        | 2011 |
|---|-------------|------|
| <b>At 1 January</b> .....   | <b>63</b>   | 22   |
| Amounts recognised directly in equity during the year .....                         | <b>80</b>   | 92   |
| Amounts removed from equity and included in the income statement for the year ..... | <b>(57)</b> | (25) |
| Deferred taxation .....   | <b>(8)</b>  | (26) |
| <b>At 31 December</b> .....   | <b>78</b>   | 63   |

At 31 December 2012, the amount reported in the income statement in respect of the ineffectiveness of cash flow hedges was a gain of EUR 11.6 million (at 31 December 2011: a gain of EUR 0.2 million).

### 13 Derivatives (continued)

#### d Embedded derivatives: home purchase savings

Home purchase savings accounts (CEL) and plans (PEL) are specific financial instruments established by law 65-554 of 10 July 1965. Within these products, customers build up savings during a certain period and use them to obtain loans during a subsequent period. The latter phase depends on, and cannot be separated from, the build-up phase.

To recognise derivatives embedded in PEL/CEL home purchase savings products at fair value, HSBC France has developed a model with the following main characteristics:

- (i) the main accounting reference is IAS 39, concerning the calculation of fair value with respect to derivative instruments;
- (ii) the derivatives under consideration are borrowing and savings options embedded in contracts in force at the accounts-closing date:
  - the model calculates the fair value of exceptional payment and deferred payment options granted to customers (for home purchase savings plans only),
  - the model calculates the fair value of options to use acquired borrowing rights;
- (iii) the calculation is dependent on customer behaviour, and is carried out separately for each issue of PELs and on a combined basis for CELs.

At 31 December 2012, derivatives embedded in home purchase savings products represented a liability of EUR 12.1 million (at 31 December 2011: a liability of EUR 10 million).

### 14 Financial investments

| (in millions of euros)                                      | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Financial investments:                                      |                   |                   |
| – which may be pledged or resold by counterparties .....    | 3,705             | 4,226             |
| – not subject to repledge or resale by counterparties ..... | <u>4,551</u>      | <u>3,292</u>      |
|   | <u>8,256</u>      | <u>7,518</u>      |

| (in millions of euros)                         | <u>31.12.2012</u> |                   | <u>31.12.2011</u> |                   |
|--|-------------------|-------------------|-------------------|-------------------|
|  | <i>Book value</i> | <i>Fair value</i> | <i>Book value</i> | <i>Fair value</i> |
| <b>Treasury and other eligible bills</b> ..... | <u>273</u>        | <u>273</u>        | 200               | 200               |
| – available-for-sale .....                     | 273               | 273               | 200               | 200               |
| – held-to-maturity .....                       | –                 | –                 | –                 | –                 |
| <b>Debt securities</b> .....                   | <u>7,745</u>      | <u>7,745</u>      | 6,896             | 6,896             |
| – available-for-sale .....                     | 7,745             | 7,745             | 6,896             | 6,896             |
| – held-to-maturity .....                       | –                 | –                 | –                 | –                 |
| <b>Equity securities</b> .....                 | <u>240</u>        | <u>240</u>        | 422               | 422               |
| – available-for-sale .....                     | 240               | 240               | 422               | 422               |
| <b>Total financial investments</b> .....       | <u>8,258</u>      | <u>8,258</u>      | 7,518             | 7,518             |

**Consolidated financial statements** (continued)**15 Securitisations and other structured transactions**

The HSBC France group enters into transactions in the normal course of business by which it transfers recognised financial assets directly to third parties or to special purpose entities. These transfers may give rise to the full or partial derecognition of the financial assets concerned:

- (i) full derecognition occurs when the HSBC France group transfers its contractual right to receive cash flows from the financial assets and substantially, all the risks and rewards of ownership. The risks include credit, interest rate, currency, prepayment and other price risks. In addition, full derecognition occurs where the contractual rights to receive the cash flows of the financial assets are retained but a contractual obligation to pay the cash flows to one or more recipients is assumed;
- (ii) partial derecognition occurs when the HSBC France group sells, or otherwise transfers, financial assets in such a way that some, but not substantially all, of the risks and rewards of ownership are transferred but control is retained. These financial assets are recognised on the balance sheet to the extent of the HSBC France group's continuing involvement.

The majority of transferred financial assets that do not qualify for derecognition are (i) debt securities held by counterparties as collateral under repurchase agreements or (ii) equity securities lent under securities lending agreements. The following table analyses the carrying amount of financial assets that did not qualify for derecognition during the year and their associated financial liabilities:

|   | 31.12.2012                       |  | 31.12.2011                       |  |
|---|----------------------------------|--|----------------------------------|--|
|   | <i>Carrying amount of assets</i> | <i>Carrying amount of associated liabilities</i> | <i>Carrying amount of assets</i> | <i>Carrying amount of associated liabilities</i> |
| (in millions of euros)                  |                                  |  |                                  |  |
| <b>Nature of transaction</b>            |                                  |  |                                  |  |
| Repurchase agreements . . . . .         | 24,955                           | 24,955   | 20,897                           | 20,897   |
| Securities lending agreements . . . . . | –                                | –  | –                                | –  |
| <b>Total</b> . . . . .                  | <b>24,955</b>                    | <b>24,955</b>                                    | <b>20,897</b>                    | <b>20,897</b>                                    |

## 16 Interests in associates and joint ventures

### a *Principal associates*

At 31 December 2012, the HSBC France group only consolidated through equity accounting method a limited number of entities that had no significant impact on the consolidated financial statements.

### b *Summarised aggregate financial information on joint ventures*

|                        | <b>31.12.2012</b>             |                               |                |
|------------------------|-------------------------------|-------------------------------|----------------|
|                        | <i>Principal<br/>activity</i> | <i>Interest<br/>in equity</i> | <i>Capital</i> |
| HCM Holdings Ltd ..... | <b>Holding</b>                | <b>51%</b>                    | –              |
|                        | <b>31.12.2011</b>             |                               |                |
|                        | <i>Principal<br/>activity</i> | <i>Interest<br/>in equity</i> | <i>Capital</i> |
| HCM Holdings Ltd ..... | Holding                       | 51%                           | –              |

Although the HSBC France group owns more than 50 per cent of the equity capital of HCM Holdings Ltd, the agreement with the other shareholder includes restrictions on the rights of HSBC France as the majority shareholder and indicates joint control over HCM Holdings Ltd by the two shareholders.

### **Summarised aggregate financial information on joint ventures**

(Figures from local financial statements: 100 per cent)

| (in millions of euros)        | <b>2012</b> | 2011 |
|-------------------------------|-------------|------|
| Current assets .....          | <b>2</b>    | 1    |
| Non-current assets .....      | –           | –    |
| Current liabilities .....     | –           | –    |
| Non-current liabilities ..... | <b>2</b>    | 1    |
| Income .....                  | –           | –    |
| Expenses .....                | –           | –    |

**Consolidated financial statements** (continued)**17 Goodwill and intangible assets**

“Goodwill and intangible assets” includes goodwill arising on business combinations and other intangible assets.

**a Goodwill**

(in millions of euros)

|   | <b>2012</b> | 2011       |
|---|-------------|------------|
| <b>Cost</b>   |             |            |
| <b>At 1 January</b> .....                                 | <b>370</b>  | 375        |
| Additions .....   | –           | –          |
| Disposals <sup>1</sup> .....                              | –           | (5)        |
| Exchange translation differences .....                    | –           | –          |
| Changes in scope of consolidation and other changes ..... | –           | –          |
| <b>At 31 December</b> .....                               | <b>370</b>  | <b>370</b> |
| <b>Accumulated impairment losses</b>                      |             |            |
| <b>At 1 January</b> .....                                 | <b>(33)</b> | (33)       |
| Disposals .....   | –           | –          |
| Impairment losses recognised in profit or loss .....      | –           | –          |
| Changes in scope of consolidation and other changes ..... | –           | –          |
| <b>At 31 December</b> .....                               | <b>(33)</b> | (33)       |
| <b>Net book value at 31 December</b> .....                | <b>337</b>  | 337        |

<sup>1</sup> In 2011, includes sale of Asset Management and Private Banking entities.

During 2012 and 2011, no goodwill impairment was recognised. Impairment testing in respect of goodwill is performed annually by comparing the recoverable amount of Cash-Generating Units (“CGUs”), based on a value-in-use calculation. This calculation uses cash flow estimates based on management’s cash flow projections, extrapolated in perpetuity using a nominal long-term growth rate based on current market assessments of GDP and inflation. Cash flows are extrapolated in perpetuity due to the long-term perspective within the group of the business units making up the CGUs. The discount rate used is based on the cost of capital the group allocates to investments within which the CGU operates.

The cost of capital assigned to an individual CGU and used to discount its future cash flows can have a significant effect on its valuation. The cost of capital percentage is generally derived from an appropriate capital asset pricing model, which itself depends on inputs reflecting a number of financial and economic variables including the risk-free rate and a premium or discount to reflect the inherent risk of the business being evaluated. These variables are established on the basis of management judgement and current market assessments of economic variables.

The review of goodwill impairment represents management’s best estimates of the factors. These values are sensitive to the cash flows projected for the periods for which detailed forecasts are available, and to assumptions regarding the long-term sustainable pattern of cash flows thereafter. While the acceptable range within which underlying assumptions can be applied is governed by the requirement for resulting forecasts to be compared with actual performance and verifiable economic data in future years, the cash flow forecasts necessarily and appropriately reflect management’s view of future business prospects. The process of identifying and evaluating goodwill impairment is inherently uncertain because it requires significant management judgement in making a series of estimations, the results of which are highly sensitive to the assumptions used.



## 17 Goodwill and intangible assets (continued)

### b Other intangible assets

The analysis of intangible assets movements at 31 December 2012, is as follows:

| (in millions of euros)                                  | <i>Internally<br/>generated<br/>software</i> | <i>Purchased<br/>software</i> | <i>Other</i> | <i>Total</i> |
|---|--|-------------------------------|--------------|--------------|
| <b>Cost</b>   |  |                               |              |              |
| <b>At 1 January 2012</b> .....                          | <b>142</b>                                   | <b>59</b>                     | <b>34</b>    | <b>235</b>   |
| Additions .....   | –  | <b>8</b>                      | –            | <b>8</b>     |
| Disposals .....   | –  | <b>(3)</b>                    | –            | <b>(3)</b>   |
| Exchange translation differences .....                  | –  | –                             | –            | –            |
| Changes in scope of consolidation and other changes ... | –  | <b>2</b>                      | –            | <b>2</b>     |
| <b>At 31 December 2012</b> .....                        | <b>142</b>                                   | <b>66</b>                     | <b>34</b>    | <b>242</b>   |
| <b>Accumulated impairment losses</b>                    |  |                               |              |              |
| <b>At 1 January 2012</b> .....                          | <b>(142)</b>                                 | <b>(44)</b>                   | <b>(8)</b>   | <b>(194)</b> |
| Charges for the year <sup>1</sup> .....                 | –  | <b>(8)</b>                    | –            | <b>(8)</b>   |
| Disposals .....   | –  | <b>1</b>                      | –            | <b>1</b>     |
| Impairment losses .....                                 | –  | –                             | –            | –            |
| Reversal of impairment losses .....                     | –  | –                             | –            | –            |
| Exchange translation differences .....                  | –  | –                             | –            | –            |
| Changes in scope of consolidation and other changes ... | –  | <b>(1)</b>                    | –            | <b>(1)</b>   |
| <b>At 31 December 2012</b> .....                        | <b>(142)</b>                                 | <b>(52)</b>                   | <b>(8)</b>   | <b>(202)</b> |
| <b>Net book value at 31 December 2012</b> .....         | <b>–</b>                                     | <b>14</b>                     | <b>26</b>    | <b>40</b>    |

<sup>1</sup> The amortisation charge for the year is recognised within the income statement under “Amortisation of intangible assets and impairment of goodwill”.

| (in millions of euros)                                  | <i>Internally<br/>generated<br/>software</i> | <i>Purchased<br/>software</i> | <i>Other</i> | <i>Total</i> |
|---|--|-------------------------------|--------------|--------------|
| <b>Cost</b>   |  |                               |              |              |
| <b>At 1 January 2011</b> .....                          | <b>142</b>                                   | <b>57</b>                     | <b>34</b>    | <b>233</b>   |
| Additions .....   | –  | <b>10</b>                     | –            | <b>10</b>    |
| Disposals .....   | –  | <b>(1)</b>                    | –            | <b>(1)</b>   |
| Exchange translation differences .....                  | –  | –                             | –            | –            |
| Changes in scope of consolidation and other changes ... | –  | <b>(7)</b>                    | –            | <b>(7)</b>   |
| <b>At 31 December 2011</b> .....                        | <b>142</b>                                   | <b>59</b>                     | <b>34</b>    | <b>235</b>   |
| <b>Accumulated impairment losses</b>                    |  |                               |              |              |
| <b>At 1 January 2011</b> .....                          | <b>(142)</b>                                 | <b>(43)</b>                   | <b>(9)</b>   | <b>(194)</b> |
| Charges for the year <sup>1</sup> .....                 | –  | <b>(8)</b>                    | –            | <b>(8)</b>   |
| Disposals .....   | –  | <b>1</b>                      | –            | <b>1</b>     |
| Impairment losses .....                                 | –  | –                             | –            | –            |
| Reversal of impairment losses .....                     | –  | –                             | –            | –            |
| Exchange translation differences .....                  | –  | –                             | –            | –            |
| Changes in scope of consolidation and other changes ... | –  | <b>6</b>                      | <b>1</b>     | <b>7</b>     |
| <b>At 31 December 2011</b> .....                        | <b>(142)</b>                                 | <b>(44)</b>                   | <b>(8)</b>   | <b>194</b>   |
| <b>Net book value at 31 December 2011</b> .....         | <b>–</b>                                     | <b>15</b>                     | <b>26</b>    | <b>41</b>    |

<sup>1</sup> The amortisation charge for the year is recognised within the income statement under “Amortisation of intangible assets and impairment of goodwill”.

**Consolidated financial statements** (continued)**17 Goodwill and intangible assets** (continued)**c Goodwill and intangible assets**

|  |             |             |
|--|-------------|-------------|
| (in millions of euros)   | <u>2012</u> | <u>2011</u> |
| <b>Cost</b>  |             |             |
| Goodwill – net book value (see Note 17 a) .....                | 337         | 337         |
| Other intangible assets – net book value (see Note 17 b) ..... | <u>40</u>   | <u>41</u>   |
|  | <u>377</u>  | <u>378</u>  |

**18 Property, plant and equipment****a Property, plant and equipment**

|  |  |   |              |
|--|--|---|--------------|
| (in millions of euros)   | <i>Freehold<br/>land and<br/>buildings</i> | <i>Equipment,<br/>fixtures<br/>and fittings</i> | <i>Total</i> |
| <b>Cost or fair value</b>  |  |   |              |
| <b>At 1 January 2012</b> .....   | 93   | 363   | 456          |
| Additions at cost <sup>1</sup> .....                                   | 5  | 74  | 79           |
| Fair value adjustments .....   | –  | –   | –            |
| Disposals .....  | (1)  | (2)   | (3)          |
| Exchange translation differences .....                                 | –  | –   | –            |
| Changes in scope of consolidation and other changes <sup>2</sup> ..... | <u>6</u>                                   | <u>(13)</u>                                     | <u>(7)</u>   |
| <b>At 31 December 2012</b> .....                                       | <u>103</u>                                 | <u>422</u>                                      | <u>525</u>   |
| <b>Accumulated depreciation</b>  |  |   |              |
| <b>At 1 January 2012</b> .....   | (14)                                       | (177)   | (191)        |
| Depreciation charge for the year .....                                 | (2)  | (45)  | (47)         |
| Disposals .....  | –  | 2   | 2            |
| Exchange translation differences .....                                 | –  | –   | –            |
| Changes in scope of consolidation and other changes <sup>2</sup> ..... | <u>(8)</u>                                 | <u>14</u>                                       | <u>6</u>     |
| <b>At 31 December 2012</b> .....                                       | <u>(24)</u>                                | <u>(206)</u>                                    | <u>(230)</u> |
| <b>Net book value at 31 December 2012</b> .....                        | <u>79</u>                                  | <u>216</u>                                      | <u>295</u>   |

1 Includes additions in equipment, fixtures and fittings for “Strategic Plan” (Renovation/creation of new branches with 96 branches renovated by the end of 2012).

2 Includes write-offs of equipment, fixtures and fittings discarded.

## 18 Property, plant and equipment (continued)

| (in millions of euros)   | <i>Freehold<br/>land and<br/>buildings</i> | <i>Equipment,<br/>fixtures<br/>and fittings</i> | <i>Total</i> |
|--|--|---|--------------|
| Cost or fair value   |  |   |              |
| At 1 January 2011 .....  | 88   | 335   | 423          |
| Additions at cost <sup>1</sup> .....                                   | 6  | 80  | 86           |
| Fair value adjustments .....   | –  | –   | –            |
| Disposals .....  | (1)  | (3)   | (4)          |
| Exchange translation differences .....                                 | –  | –   | –            |
| Changes in scope of consolidation and other changes <sup>2</sup> ..... | –  | (49)  | (49)         |
| At 31 December 2011 .....  | <u>93</u>                                  | <u>363</u>                                      | <u>456</u>   |
| Accumulated depreciation   |  |   |              |
| At 1 January 2011 .....  | (12)                                       | (178)   | (190)        |
| Depreciation charge for the year .....                                 | (2)  | (47)  | (49)         |
| Disposals .....  | 1  | 2   | 3            |
| Exchange translation differences .....                                 | –  | –   | –            |
| Changes in scope of consolidation and other changes <sup>2</sup> ..... | (1)  | 46  | 45           |
| At 31 December 2011 .....  | <u>(14)</u>                                | <u>(177)</u>                                    | <u>(191)</u> |
| Net book value at 31 December 2011 .....                               | <u>79</u>                                  | <u>186</u>                                      | <u>265</u>   |

1 Includes additions in equipment, fixtures and fittings for "Strategic Plan" (Renovation/creation of new branches with 95 branches renovated by the end of 2011).

2 Includes write-offs of equipment, fixtures and fittings discarded.

### b Investment properties

At 31 December 2012 and 31 December 2011, the HSBC France group did not own investment properties.

### c Property, plant and equipment

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Property, plant and equipment goodwill – net book value (see Note 18 a) ..... | 295               | 265               |
| Investment properties – net book value (see Note 18 b) .....                  | –                 | –                 |
|   | <u>295</u>        | <u>265</u>        |

## Consolidated financial statements (continued)

## 19 Investments

| Consolidated companies                          | Country   | Consolidation method* | Main line of business | HSBC France group interest |        |
|---|-----------|-----------------------|-----------------------|----------------------------|--------|
|   |           |                       |                       | % 2012                     | % 2011 |
| <b>Retail and Commercial Banking</b>            |           |                       |                       |                            |        |
| COPARI  | France    | FC                    | Holding company       | 100.0                      | 100.0  |
| Financière d'Uzès                               | France    | EM                    | Financial company     | 34.0                       | 34.0   |
| HSBC Factoring (France) (ex-Elysées Factor)     | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| SAPC Ufipro Recouvrement                        | France    | FC                    | Bank                  | 100.0                      | 100.0  |
| SARL Neuilly Valeurs                            | France    | FC                    | Investment company    | 100.0                      | 100.0  |
| SCI Hervet Mathurins                            | France    | FC                    | Holding company       | 100.0                      | 100.0  |
| Union pour la Gestion et les Transactions (UGT) | France    | FC                    | Service company       | 100.0                      | 100.0  |
| Vernet Expansion <sup>1</sup>                   | France    |                       | Investment company    | –                          | 100.0  |
| <b>Global Banking and Markets</b>               |           |                       |                       |                            |        |
| Beau Soleil Limited Partnership                 | Hong Kong | FC                    | Financial company     | 85.0                       | 85.0   |
| CCF Charterhouse GmbH                           | Germany   | FC                    | Service company       | 100.0                      | 100.0  |
| CCF Charterhouse GmbH<br>& Co Asset Leasing KG  | Germany   | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 5   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 9   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 10  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 22  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 23  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 24  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEM 25  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEMPAR 1  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| DEMPAR 2 <sup>1</sup>                           | France    | FC                    | Financial company     | –                          | 100.0  |
| DEMPAR 4  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| Elysées GmbH                                    | Germany   | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 1   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 2   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 3   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 4   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 5   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 6   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 7   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 8   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 9   | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| FDM 10  | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| Finanpar 2                                      | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| Finanpar 5                                      | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| Finanpar 6 <sup>1</sup>                         | France    | FC                    | Financial company     | –                          | 100.0  |
| Finanpar 7                                      | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| Foncière Elysées                                | France    | FC                    | Holding company       | 100.0                      | 100.0  |
| HSBC Leasing (Belgium)                          | Belgium   | FC                    | Financial company     | 100.0                      | 100.0  |
| HSBC Leasing (France)                           | France    | FC                    | Financial company     | 100.0                      | 100.0  |
| HSBC Middle East Leasing Partnership            | Dubai     | FC                    | Financial company     | 85.0                       | 85.0   |

\* FC: Full Consolidation – EM: Equity Method.

<sup>1</sup> Merger.

## 19 Investments (continued)

| <i>Consolidated companies</i>  | <i>Country</i> | <i>Consolidation method*</i> | <i>Main line of business</i> | HSBC France group interest |               |
|--|----------------|------------------------------|------------------------------|----------------------------|---------------|
|  |                |                              |                              | <i>% 2012</i>              | <i>% 2011</i> |
| HSBC Real Estate Leasing (France)  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| HSBC REIM (France)   | France         | FC                           | Service company              | 100.0                      | 100.0         |
| HSBC Services (France)<br>(ex-HSBC Securities (France))                          | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| HSBC SFH (France) (ex-HSBC Covered<br>Bonds (France)) (ex-Hervet Participations) | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| Immobilière Bauchard <sup>1</sup>  | France         | FC                           | Holding company              | –                          | 100.0         |
| Realimo Negotiations <sup>1</sup>  | France         | FC                           | Service company              | –                          | 100.0         |
| SAF Baiyun   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang ba   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang er   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang jiu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang liu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang qi   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang san  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang shi  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang shi'er   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang shiyi  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang shi liu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang shi wu   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang wu   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Chang jiang yi   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Guangzhou  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Leasing Holding (France)   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Palissandre  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang ba   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang er   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang jiu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang liu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang qi   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang san  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shi  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu Jiang shi ba (ex-DEM 20)   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shi er   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu Jiang shi jiu (ex-DEM 21)  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shi liu  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shi qi   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shi wu   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang shiyi  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang wu   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| SAF Zhu jiang yi   | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| Société Financière et Mobilière (SFM)  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| Société Immobilière Malesherbes-Anjou  | France         | FC                           | Holding company              | 100.0                      | 100.0         |
| Sopingest  | France         | FC                           | Financial company            | 100.0                      | 100.0         |
| Thasosfin  | France         | FC                           | Financial company            | 100.0                      | 100.0         |

\* FC: Full Consolidation – EM: Equity Method.

<sup>1</sup> Merger.

**Consolidated financial statements** (continued)**19 Investments** (continued)

| <i>Consolidated companies</i>  | <i>Country</i> | <i>Consolidation method*</i> | <i>Main line of business</i> | HSBC France group interest |                  |
|--|----------------|------------------------------|------------------------------|----------------------------|------------------|
|  |                |                              |                              | <i>%</i><br><b>2012</b>    | <i>%</i><br>2011 |
| <b>Asset Management</b>  |                |                              |                              |                            |                  |
| CCF & Partners Asset Management Ltd  | United Kingdom | FC                           | Financial company            | <b>100.0</b>               | 100.0            |
| HCM Holdings Ltd   | United Kingdom | Joint control                | Financial company            | <b>51.0</b>                | 51.0             |
| HSBC Duoblig (ex-HSBC Dynamic Cash) <sup>1</sup>   | France         | FC                           | Financial company            | –                          | 97.7             |
| HSBC Epargne Entreprise (France)   | France         | FC                           | Financial company            | <b>100.0</b>               | 100.0            |
| Service Epargne Entreprise   | France         | EM                           | Service company              | <b>18.1</b>                | 18.1             |
| HSBC Global Asset Management Financial Services (ex-Sinopia Financial Services) <sup>1</sup> | France         | FC                           | Financial company            | –                          | 100.0            |
| HSBC Global Asset Management (France) (ex-HSBC Investments (France))                         | France         | FC                           | Asset management             | <b>100.0</b>               | 100.0            |
| HSBC Global Asset Management (Switzerland) AG  | Switzerland    | EM                           | Financial company            | <b>50.0</b>                | 50.0             |
| HSBC Private Wealth Managers (ex-Louvre Gestion) <sup>1</sup>                                | France         | FC                           | Financial company            | –                          | 100.0            |
| Sinopia TRS1   | France         | FC                           | Financial company            | <b>100.0</b>               | 100.0            |
| SNC les Oliviers d'Antibes   | France         | FC                           | Financial company            | <b>60.0</b>                | 60.0             |
| Trinkaus Gesellschaft für KMI oHG  | Germany        | FC                           | Financial company            | <b>90.0</b>                | 90.0             |
| <b>Private Banking</b>   |                |                              |                              |                            |                  |
| Eurofin Capital Partners (ECP)   | France         | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Octogone Immobilier  | France         | FC                           | Holding company              | <b>100.0</b>               | 100.0            |
| <b>Others</b>  |                |                              |                              |                            |                  |
| Charterhouse Management Services Limited (CMSL)  | United Kingdom | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Charterhouse Administrators Ltd  | United Kingdom | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Contrarian and Value Fund <sup>1</sup>   | France         | FC                           | Investment company           | –                          | 100.0            |
| Elysées Formation <sup>2</sup>   | France         | FC                           | Service company              | –                          | 100.0            |
| Enership   | France         | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Euro Stock Picking <sup>1</sup>  | France         | FC                           | Investment company           | –                          | 100.0            |
| Excofina   | France         | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| FinanCités   | France         | EM                           | Capital Risk company         | <b>15.4</b>                | 15.4             |
| Fund Nominees Limited  | United Kingdom | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Keyser Ullman Ltd  | United Kingdom | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Serdac <sup>2</sup>  | Switzerland    | FC                           | Investment company           | –                          | 100.0            |
| Shield Properties & Investments Limited (Holdings)   | United Kingdom | FC                           | Service company              | <b>100.0</b>               | 100.0            |
| Société Française et Suisse (SFS)  | France         | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Valeurs Mobilières Elysées (ex-Nobel)  | France         | FC                           | Investment company           | <b>100.0</b>               | 100.0            |
| Value Fund 2 <sup>1</sup>  | France         | FC                           | Financial company            | –                          | 100.0            |

\* FC: Full Consolidation – EM: Equity Method.

1 Merger.

2 Liquidation.

## 19 Investments (continued)

| <u>Additions</u>                   | <u>Year</u> |
|------------------------------------|-------------|
| SAF Leasing Holding (France) ..... | 2011        |

### **Mergers:**

DEMPAR 2 merged with Société Financière et Mobilière (SFM)  
Finanpar 6 merged with Société Financière et Mobilière (SFM)  
Vernet Expansion merged with HSBC France  
HSBC Global Asset Management Financial Services merged  
with HSBC Global Asset Management (France)  
HSBC Private Wealth Managers merged  
with HSBC Global Asset Management (France)  
Euro Stock Picking merged with Enership  
Value Fund 2 merged with Enership  
Realimo Negociation merged with Foncière Elysées  
Immobilière Bauchard merged with Foncière Elysées  
Contrarian and Value Fund merged with Valeurs Mobilières  
Elysées

### **Disposal or liquidation:**

HSBC Duoblig (ex-HSBC Dynamic Cash)  
Elysées Formation  
Serdac

**Consolidated financial statements** (continued)**20 Other assets and non-current assets held for sale****a Other assets**

| (in millions of euros)             | <b>31.12.2012</b> | 31.12.2011 |
|------------------------------------|-------------------|------------|
| Current taxation recoverable ..... | <b>58</b>         | 148        |
| Other accounts .....               | <b>238</b>        | 969        |
|                                    | <b>296</b>        | 1,117      |

**b Non-currents assets held for sale**

| (in millions of euros)                                | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Property, plant and equipment .....                   | -                 | 5          |
| Investment properties .....                           | -                 | -          |
| <b>Total assets classified as held for sale</b> ..... | <b>-</b>          | <b>5</b>   |

The assets classified as “Non-current assets held for sale” follow the conditions of the IFRS 5 (see Note 2 aa).

**21 Financial liabilities designated at fair value**

| (in millions of euros)         | <b>31.12.2012</b> | 31.12.2011 |
|--------------------------------|-------------------|------------|
| Deposits by banks .....        | -                 | -          |
| Customer accounts .....        | <b>215</b>        | 209        |
| Debt securities in issue ..... | <b>5,423</b>      | 5,304      |
| Subordinated liabilities ..... | <b>16</b>         | 14         |
|                                | <b>5,654</b>      | 5,527      |

The difference between the carrying amount of financial liabilities designated at fair value and the contractual amount at maturity at 31 December 2012 was EUR 370 million (at 31 December 2011: EUR 250 million).

At 31 December 2012, the accumulated amount of the change in fair value attributable to changes in credit risk for the group was EUR 59 million (at 31 December 2011: EUR -59 million).

In 2012, the amount reported in the income statement in respect of HSBC France’s own credit spread was a loss of EUR -118 million (2011: a gain of EUR 124 million).

**22 Other liabilities**

| (in millions of euros)  | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Amounts due to investors in funds consolidated by the group ..... | -                 | 3          |
| Share-based payments .....  | <b>61</b>         | 44         |
| Obligations under finance leases .....                            | -                 | -          |
| Other liabilities .....   | <b>478</b>        | 790        |
|   | <b>539</b>        | 837        |



## 23 Deferred taxation

| (in millions of euros)                      | 31.12.2012                |                               |              | 31.12.2011                |                               |              |
|---|---------------------------|-------------------------------|--------------|---------------------------|-------------------------------|--------------|
|   | <i>Deferred tax asset</i> | <i>Deferred tax liability</i> | <i>Total</i> | <i>Deferred tax asset</i> | <i>Deferred tax liability</i> | <i>Total</i> |
| Temporary differences:                      |                           |                               |              |                           |                               |              |
| – retirement benefits . . . . .             | 36                        | –                             | (36)         | 28                        | –                             | (28)         |
| – assets leased . . . . .                   | 65                        | –                             | (65)         | 47                        | –                             | (47)         |
| – revaluation of property . . .             | (11)                      | –                             | 11           | (12)                      | –                             | 12           |
| – other temporary differences . . . . .     | 110                       | 2                             | (108)        | 59                        | 2                             | (57)         |
| – deferred losses carried forward . . . . . | –                         | –                             | –            | 89                        | –                             | (89)         |
|   | <b>200</b>                | <b>2</b>                      | <b>(198)</b> | <b>211</b>                | <b>2</b>                      | <b>(209)</b> |

The main amounts of deferred tax related to items that are charged directly to equity are detailed as follows:

| (in millions of euros)               | 31.12.2012 | 31.12.2011 |
|--------------------------------------|------------|------------|
| Cash flow hedge . . . . .            | 43         | 35         |
| Available-for-sale reserve . . . . . | 28         | (24)       |
| Actuarial losses . . . . .           | (15)       | (8)        |

## 24 Provisions for liabilities and charges

| (in millions of euros)  | <i>Provisions</i> |
|---|-------------------|
| <b>At 1 January 2012</b> . . . . .  | <b>97</b>         |
| Additional provisions/increase in provisions . . . . .                    | 51                |
| Provisions utilised . . . . .   | (26)              |
| Amounts reversed . . . . .  | (25)              |
| Exchange, changes in scope of consolidation and other movements . . . . . | –                 |
| <b>At 31 December 2012</b> . . . . .                                      | <b>97</b>         |

Movements on provision recognised in 2012 consist mainly of restructuring provision.

| (in millions of euros)  | <i>Provisions</i> |
|---|-------------------|
| At 1 January 2011 . . . . .   | 62                |
| Additional provisions/increase in provisions . . . . .                    | 71                |
| Provisions utilised . . . . .   | (17)              |
| Amounts reversed . . . . .  | (20)              |
| Exchange, changes in scope of consolidation and other movements . . . . . | 1                 |
| At 31 December 2011 . . . . .   | 97                |

Movements on provision recognised in 2011 consist mainly of restructuring provision.

## 25 Sale and repurchase and settlement accounts

| (in millions of euros)                                  | 31.12.2012 | 31.12.2011 |
|---|------------|------------|
| <b>Assets</b>   |            |            |
| Loans and advances to customers include:                |            |            |
| – assets under sale and repurchase agreements . . . . . | 14,512     | 20,745     |
| – settlement accounts . . . . .                         | 548        | 117        |
| Loans and advances to banks include:                    |            |            |
| – assets under sale and repurchase agreements . . . . . | 22,949     | 25,762     |
| – settlement accounts . . . . .                         | 1,366      | 792        |

**Consolidated financial statements** (continued)**25 Sale and repurchase and settlement accounts** (continued)

| (in millions of euros)                                   | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| <b>Liabilities</b>                                       |                   |                   |
| Customer accounts include:                               |                   |                   |
| – liabilities under sale and repurchase agreements ..... | <b>12,339</b>     | 13,196            |
| – settlement accounts .....                              | <b>1,057</b>      | 399               |
| Deposits by banks include:                               |                   |                   |
| – liabilities under sale and repurchase agreements ..... | <b>23,836</b>     | 20,503            |
| – settlement accounts .....                              | <b>1,073</b>      | 660               |

**26 Subordinated liabilities**

| (in millions of euros)           | <i>Book value</i> |                   |
|----------------------------------|-------------------|-------------------|
|                                  | <u>31.12.2012</u> | <u>31.12.2011</u> |
| Subordinated liabilities:        |                   |                   |
| – at amortised cost .....        | <b>166</b>        | 166               |
| – designated at fair value ..... | <b>16</b>         | 14                |
|                                  | <b>182</b>        | 180               |

Subordinated borrowings issued by HSBC France:

| (in millions of euros)                                       | <i>Book value</i> |                   |
|--|-------------------|-------------------|
|  | <u>31.12.2012</u> | <u>31.12.2011</u> |
| EUR150m <sup>1</sup> Floating rate notes maturing 2014 ..... | <b>150</b>        | 150               |
| EUR15m Floating rate notes maturing 2015 .....               | <b>16</b>         | 14                |
| EUR16m Undated subordinated variable rate notes .....        | <b>16</b>         | 16                |
|  | <b>182</b>        | 180               |

<sup>1</sup> Debt issued to HSBC Bank plc.

**27 Trading liabilities**

| (in millions of euros)                    | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Other liabilities – short positions ..... | <b>18,683</b>     | 21,537            |
| Deposits by banks .....                   | <b>11,154</b>     | 8,772             |
| Customer accounts .....                   | <b>4,923</b>      | 6,565             |
| Debt securities in issue .....            | <b>1,511</b>      | 1,384             |
| <b>Total</b> .....                        | <b>36,271</b>     | 38,258            |

In 2012, the amount reported in the income statement with respect to HSBC France's own credit spread in the debt securities in issue was a loss of EUR -100 million (2011: a gain of EUR 64 million).

## 28 Fair value of financial instruments

The classification of financial instruments is determined in accordance with the accounting policies set out in Note 2. The use of assumption and estimation in valuing financial instruments is described in Note 1 c on page 107.

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.

The following table sets out the financial instrument carried at fair value.

| (in millions of euros)                            | Valuation techniques                   |  |  | Third Party<br>Total | Amounts<br>with HSBC<br>entities | Total  |
|---|--|--|--|----------------------|----------------------------------|--------|
|   | Level 1 -<br>quoted<br>market<br>price | Level 2 -<br>using<br>observable<br>inputs | Level 3 -<br>with<br>significant<br>non-<br>observable<br>inputs |                      |                                  |        |
| <b>At 31 December 2012</b>                        |  |  |  |                      |                                  |        |
| <b>Assets</b>                                     |  |  |  |                      |                                  |        |
| Trading assets                                    | 35,152                                 | 505  | –  | 35,657               | 4,920                            | 40,577 |
| Financial assets<br>designated at fair value      | –                                      | –  | –  | –                    | 5                                | 5      |
| Derivatives                                       | 8                                      | 65,641                                     | 47   | 65,696               | 24,562                           | 90,258 |
| Financial investments<br>available-for-sale       | 7,767                                  | 224  | 97   | 8,088                | 170                              | 8,258  |
| <b>Liabilities</b>                                |  |  |  |                      |                                  |        |
| Trading liabilities                               | 31,387                                 | 3,298                                      | –  | 34,685               | 1,586                            | 36,271 |
| Financial liabilities<br>designated at fair value | –                                      | 5,654                                      | –  | 5,654                | –                                | 5,654  |
| Derivatives                                       | 3                                      | 61,657                                     | 57   | 61,717               | 27,396                           | 89,114 |
| <b>At 31 December 2011</b>                        |  |  |  |                      |                                  |        |
| <b>Assets</b>                                     |  |  |  |                      |                                  |        |
| Trading assets                                    | 31,657                                 | 1,835                                      | –  | 33,492               | 5,521                            | 39,013 |
| Financial assets<br>designated at fair value      | –                                      | 593  | –  | 593                  | 4                                | 598    |
| Derivatives                                       | 2                                      | 57,905                                     | 46   | 57,953               | 24,784                           | 82,738 |
| Financial investments<br>available-for-sale       | 6,754                                  | 472  | 122  | 7,348                | 170                              | 7,518  |
| <b>Liabilities</b>                                |  |  |  |                      |                                  |        |
| Trading liabilities                               | 33,821                                 | 3,477                                      | –  | 37,298               | 960                              | 38,258 |
| Financial liabilities<br>designated at fair value | –                                      | 5,527                                      | –  | 5,527                | –                                | 5,527  |
| Derivatives                                       | –                                      | 52,214                                     | 102  | 52,316               | 29,365                           | 81,681 |

## Consolidated financial statements (continued)

### 28 Fair value of financial instruments (continued)

#### Control framework

Fair values are subject to a control framework that aims to ensure that they are either determined, or validated, by a function independent of the risk taker. For fair values determined by reference to external quotation or evidenced pricing parameters, independent price determination or validation is used. In less liquid markets, direct observation of a traded price may not be possible. In these circumstances, the group will source alternative market information to validate the financial instrument's fair value. Greater weight will be given to information that is considered to be more relevant and reliable. The factors that are considered in this regard are, *inter alia*:

- the extent to which prices may be expected to represent genuine traded or tradeable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the balance sheet date;
- the manner in which the data was sourced.

For fair values determined using a valuation model, the control framework may include, as applicable, independent development or validation of the logic within valuation models, the inputs to those models, any adjustments required outside the valuation models and, where possible, model outputs.

#### Determination of fair value of financial instruments carried at fair value

Financial instruments measured at fair value on an ongoing basis include trading assets and liabilities, instruments designated at fair value through profit or loss, derivatives, and financial investments classified as available-for-sale (including treasury and other eligible bills, debt securities, and equity securities).

The reliability of the fair value measurement for financial instruments reported on the group's consolidated balance sheet at fair value is assessed according to how the fair values have been determined.

Fair values are determined according to the following hierarchy:

- a *Level 1 – Quoted market price*: financial instruments with quoted prices for identical instruments in active markets.
- b *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 or financial instruments valued using models where all significant inputs are observable.
- c *Level 3 – Valuation technique with significant non-observable inputs*: financial instruments valued using models where one or more significant inputs are not observable.

The best evidence of fair value is a quoted price in an actively traded market. The fair values of financial instruments that are quoted in active markets are based on bid prices for assets held and offer prices for liabilities issued. When a financial instrument has a quoted price in an active market and it is part of a portfolio, the fair value of the portfolio is calculated as the product of the number of units and quoted price and no block discounts are made. In the event that the market for a financial instrument is not active, a valuation technique is used.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices necessary to measure the fair value of the instrument, requires additional work during the valuation process.

Valuation techniques incorporate assumptions about factors that other market participants would use in their valuations, including interest rate yield curves, exchange rates, volatilities, and prepayment and default rates.

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are not observable. For these instruments, the fair value measurement derived is more judgemental. "Not observable" in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would likely occur, but it generally does not mean that there is absolutely no market data available upon which to base a determination of fair value (consensus pricing data may, for example, be used).

## 28 Fair value of financial instruments (continued)

In certain circumstances, primarily where debt is hedged with interest rate derivatives, the group uses fair value to measure the carrying value of its own debt in issue. Where available, the fair value will be based upon quoted prices in an active market for the specific instrument concerned. Where not available, the fair value will either be based upon quoted prices in an inactive market for the specific instrument concerned, or estimated by comparison with quoted prices in an active market for similar instruments. The fair value of these instruments therefore includes the effect of applying the credit spread which is appropriate to the group's liabilities. For all issued debt securities, discounted cash flow modelling is utilised to isolate that element of change in fair value that may be attributed to the group's credit spread movements rather than movements in other market factors, such as benchmark interest rates or foreign exchange rates.

Issued structured notes and certain other hybrid instrument liabilities are included within trading liabilities, and marked at fair value. The credit spread applied to these instruments is derived from the spreads at which the group issues structured notes. These market spreads are significantly tighter than credit spreads observed in vanilla debt or credit default swap markets.

Gains and losses arising from changes in the credit spread of liabilities issued by the group reverse over the contractual life of the debt, provided that the debt is not repaid at a premium or a discount.

### Credit valuation adjustment methodology

All net positions in non-derivative financial instruments, and all derivative portfolios, are valued at bid or offer price as appropriate. Long positions are marked at bid price; short positions are marked at offer price.

The fair values of large holdings of non-derivative financial instruments are based on a multiple of the value of a single instrument, and do not include block adjustments for the size of the holding.

The valuation techniques used when quoted market prices are not available incorporate certain assumptions that HSBC believes would be made by a market participant to establish fair value. When HSBC considers that there are additional considerations not included within the valuation model, appropriate adjustments may be made. Examples of such adjustments are:

- credit risk adjustment: an adjustment to reflect the creditworthiness of OTC derivative counterparties.

A separate "credit valuation adjustment" (CVA) is calculated for each legal entity of the group, and within each entity for each counterparty to which the entity has exposure. The total CVA and "debit valuation adjustment" (DVA) at 31 December 2012 was EUR -98 million.

As set out on page 106, from 31 December 2012 the group calculates the CVA by applying the probability of default of the counterparty conditional on the non-default of HSBC, to the expected positive exposure of the group to the counterparty and multiplying by the loss expected in the event of default. Conversely, the group calculates the DVA by applying the probability of default of HSBC conditional on the non-default of the counterparty, to the expected positive exposure of the counterparty to the group and multiplying by the loss expected in the event of default. Both calculations are performed over the life of the potential exposure.

The calculation maximises the use of relevant, observable market data. The probability of default is derived from CDS spreads where these are available and reliable for a specific counterparty, including for HSBC with respect to the DVA, or relevant proxies where not. The derivation of a proxy has regard to the range of market practice, and considers relevant data in this context, including CDS index and rating transition data.

With the exception of certain central clearing parties, the group includes all third party counterparties in the CVA and DVA calculations and does not net these calculations across group entities;

- market data/model uncertainty: an adjustment to reflect uncertainties in fair values based on unobservable market data inputs (for example, as a result of illiquidity), or in areas where the choice of valuation model is particularly subjective.

However, in certain cases, the fair value of an instrument is determined in comparison with other observable market transactions concerning the same instrument or using a valuation method based solely on observable market data, in particular interest rate curves, volatility ranges deduced from option prices and exchange rates. Where such data is available, HSBC France recognises a gain or loss on trading portfolio transactions on the date the instrument is implemented.

If no observable market data is available, the profit generated from the trading of certain complex financial instruments (day-1 profit corresponding to the difference between the trading price and the valuation obtained from the valuation model) is not recognised immediately as income but recognised over the life of the transaction on an appropriate basis, or recognised in the income statement when the parameters become observable, either on maturity or at the end of the transaction.

An analysis of the movement in the deferred day-1 gain or loss is provided on page 136.

**Consolidated financial statements** (continued)**28 Fair value of financial instruments** (continued)

Reported amounts as part of Level 3 category (unobservable parameters) are in line with the day-1 policy. The underlying and structured products targeted by HSBC France are covered by products given by Market consensus: this coverage is monitored in valuation committees for derivatives on rates and equities. When required, an analysis of the collateral and of broker quotes completes the available market information, thus reducing products and parameters that could be considered as unobservable.

Trade origination costs such as brokerage, fee expense, and post-trade costs are included in operating expenses.

Financial instruments measured at fair value using a valuation technique with unobservable inputs – Level 3

| (in millions of euros)                  | <i>Assets</i>             |                         |  |                    | <i>Liabilities</i>      |  |                    |  |
|---|---------------------------|-------------------------|--|--------------------|-------------------------|--|--------------------|--|
|   | <i>Available for sale</i> | <i>Held for Trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> | <i>Held for trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> |  |
| Private equity investments . . . . .    | 97                        | –                       | –  | –                  | –                       | –  | –                  |  |
| Asset-backed securities . . . . .       | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Leverage finance . . . . .              | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Loans held for securitisation . . . . . | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Structured notes . . . . .              | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Derivatives with monolines . . . . .    | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Other derivatives . . . . .             | –                         | –                       | –  | 47                 | –                       | –  | 57                 |  |
| Other portfolio . . . . .               | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| <b>At 31 December 2012 . . . . .</b>    | <b>97</b>                 | <b>–</b>                | <b>–</b>   | <b>47</b>          | <b>–</b>                | <b>–</b>   | <b>57</b>          |  |
| Private equity investments . . . . .    | 122                       | –                       | –  | –                  | –                       | –  | –                  |  |
| Asset-backed securities . . . . .       | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Leverage finance . . . . .              | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Loans held for securitisation . . . . . | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Structured notes . . . . .              | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Derivatives with monolines . . . . .    | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Other derivatives . . . . .             | –                         | –                       | –  | 46                 | –                       | –  | 102                |  |
| Other portfolio . . . . .               | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| <b>At 31 December 2011 . . . . .</b>    | <b>122</b>                | <b>–</b>                | <b>–</b>   | <b>46</b>          | <b>–</b>                | <b>–</b>   | <b>102</b>         |  |

Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

| (in millions of euros)   | <i>Assets</i>             |                         |  |                    | <i>Liabilities</i>      |  |                    |  |
|--|---------------------------|-------------------------|--|--------------------|-------------------------|--|--------------------|--|
|  | <i>Available for sale</i> | <i>Held for Trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> | <i>Held for trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> |  |
| <b>At 1 January 2012 . . . . .</b>                                       | <b>122</b>                | <b>–</b>                | <b>–</b>   | <b>46</b>          | <b>–</b>                | <b>–</b>   | <b>102</b>         |  |
| Total gains or losses recognised in profit or loss . . . . .             | (12)                      | –                       | –  | 1                  | –                       | –  | (45)               |  |
| Total gains or losses recognised in other comprehensive income . . . . . | (2)                       | –                       | –  | –                  | –                       | –  | –                  |  |
| Purchases . . . . .  | 4                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Issues . . . . .   | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Sales . . . . .  | (11)                      | –                       | –  | –                  | –                       | –  | –                  |  |
| Settlements . . . . .  | (4)                       | –                       | –  | –                  | –                       | –  | –                  |  |
| Transfer out . . . . .   | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| Transfer in . . . . .  | –                         | –                       | –  | –                  | –                       | –  | –                  |  |
| <b>At 31 December 2012 . . . . .</b>                                     | <b>97</b>                 | <b>–</b>                | <b>–</b>   | <b>47</b>          | <b>–</b>                | <b>–</b>   | <b>57</b>          |  |

## 28 Fair value of financial instruments (continued)

| (in millions of euros)   | <i>Assets</i>             |                         |  |                    | <i>Liabilities</i>      |  |                    |     |
|--|---------------------------|-------------------------|--|--------------------|-------------------------|--|--------------------|-----|
|  | <i>Available for sale</i> | <i>Held for Trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> | <i>Held for trading</i> | <i>Designated at fair value through profit or loss</i> | <i>Derivatives</i> |     |
| At 1 January 2011  | 106                       | –                       | –  | 21                 | –                       | –  | –                  | 39  |
| Total gains or losses recognised in profit or loss             | 14                        | –                       | –  | 25                 | –                       | –  | –                  | 63  |
| Total gains or losses recognised in other comprehensive income | (5)                       | –                       | –  | –                  | –                       | –  | –                  | –   |
| Purchases  | 18                        | –                       | –  | –                  | –                       | –  | –                  | –   |
| Issues   | –                         | –                       | –  | –                  | –                       | –  | –                  | –   |
| Sales  | (11)                      | –                       | –  | –                  | –                       | –  | –                  | –   |
| Settlements  | –                         | –                       | –  | –                  | –                       | –  | –                  | –   |
| Transfer out   | –                         | –                       | –  | –                  | –                       | –  | –                  | –   |
| Transfer in  | –                         | –                       | –  | –                  | –                       | –  | –                  | –   |
| At 31 December 2011  | 122                       | –                       | –  | 46                 | –                       | –  | –                  | 102 |

### Private equity

The group's private equity positions are generally classified as available for sale and are not traded in an active market. In the absence of an active market for the investment, fair value is estimated based upon an analysis of the investee's financial position and results, risk profile, prospects and other factors as well as reference to market valuations for similar entities quoted in an active market, or the price at which similar companies have changed ownership. The exercise of judgement is required because of uncertainties inherent in estimating fair value for private equity investments.

### Asset-backed securities (ABS)

Illiquidity and a lack of transparency in the ABS market have resulted in less observable data. While quoted market prices are generally used to determine the fair value of these securities, valuation models are used to substantiate the reliability of the limited market data available and to identify whether any adjustments to quoted market prices are required. For ABS, including residential mortgage backed securities, the valuation uses an industry standard model and the assumptions relating to prepayment speeds, default rates and loss severity based on collateral type, and performance, as appropriate. The valuations output is benchmarked for consistency against observable data for securities of a similar nature.

### Derivatives

Over-the-counter (*i.e.* non-exchange traded) derivatives are valued using valuation models. Valuation models calculate the present value of expected future cash flows, based upon "no-arbitrage" principles. For many vanilla derivative products, such as interest rate swaps and European options, the modelling approaches used are standard across the industry. For more complex derivative products, there may be some divergence in practice.

Inputs to valuation models are determined from observable market data wherever possible, including prices available from exchanges, dealers, brokers or providers of consensus pricing. Certain inputs may not be observable in the market directly, but can be determined from observable prices *via* model calibration procedures. Finally, some inputs are not observable, but can generally be estimated from historic data or other sources.

### Loans

Loans held at fair value are valued from broker quotes and/or market data consensus providers where available. Where unavailable, fair value will be determined based on an appropriate credit spread derived from other market instruments issued by the same or comparable entities.

### Structured notes

For structured notes whose fair value is derived from a valuation technique, the fair value will be derived from the fair value of the underlying debt security as described above, and the fair value of the embedded derivative will be determined as described in the section above on derivatives.

## Consolidated financial statements (continued)

### 28 Fair value of financial instruments (continued)

The table below provides an analysis of the various bases described above which have been deployed for valuing financial assets and financial liabilities measured at fair value in the consolidated financial statements. The movement in the balances of assets and liabilities measured at fair value with significant unobservable inputs was mainly attributable to a reclassification in Level 2.

For assets and liabilities classified as held for trading, realised and unrealised gains and losses are presented in the income statement under "Trading income excluding net interest income". Fair value changes on long-term debt designated at fair value and related derivatives are presented in the income statement under "Changes in fair value of long-term debt issued and related derivatives". The income statement line item "Net income/(expense) from other financial instruments designated at fair value" captures fair value movements on all other financial instruments designated at fair value and related derivatives.

Realised gains and losses from available-for-sale securities are presented under "Gains less losses of financial investments" in the income statement, while unrealised gains and losses are presented in "Fair value gains/(losses) taken to equity" within "Available-for-sale investments" in other comprehensive income.

#### Fair value of financial instruments not carried at fair value

Fair values at the balance sheet date of the assets and liabilities set out below are estimated for the purpose of disclosure as follows:

##### (i) Loans and advances to banks and customers

The fair value of loans and advances is based on observable market transactions where available. In the absence of observable market transactions, fair value is estimated using discounted cash flow models. Performing loans are grouped, as far as possible, into homogeneous pools segregated by amount, customer type, currency, facility grade, maturity and coupon rates. In general, contractual cash flows are discounted using the group's estimate of the discount rate that a market participant would use in valuing instruments with similar maturity, repricing and credit risk characteristics. For maturity buckets where there is no recent price information, a linear trend is assumed between known points.

For loans and deposits, the fair value of the amounts repayable on demand is estimated as the carrying value at the balance sheet date.

The fair value of a loan portfolio reflects both loan impairments at the balance sheet date and estimates of market participants' expectations of credit losses over the life of the loans.

For impaired loans, fair value is estimated by discounting the future cash flows over the time period they are expected to be recovered.

##### (ii) Financial investments

The fair values of listed financial investments are determined using bid market prices. The fair values of unlisted financial investments are determined using valuation techniques that take into consideration either the prices or future earnings streams of equivalent quoted securities.

##### (iii) Deposits by banks and customer accounts

For the purposes of estimating fair value, deposits by banks and customer accounts are grouped by residual maturity. Fair values are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities. The fair value of a deposit repayable on demand is assumed to be the amount payable on demand at the balance sheet date.

##### (iv) Debt securities in issue and subordinated liabilities

Fair values are determined using quoted market prices at the balance sheet date where available, or by reference to quoted market prices for similar instruments.

The fair values in this Note are stated at a specific date and may be significantly different from the amounts that will actually be paid on the maturity or settlement dates of the instruments. In many cases, it would not be possible to realise immediately the estimated fair values given the size of the portfolios measured. Accordingly, these fair values do not represent the value of these financial instruments to the group as a going concern.

For all classes of financial instruments, fair value represents the product of the value of a single instrument, multiplied by the number of instruments held. No block discount or premium adjustments are made.



## 28 Fair value of financial instruments (continued)

The following table provides an analysis of the fair value of financial instruments not measured at fair value in the balance sheet. For all other instruments the fair value is equal to the carrying value:

| (in millions of euros)                | 31.12.2012     |            | 31.12.2011     |            |
|---------------------------------------|----------------|------------|----------------|------------|
|                                       | Carrying value | Fair value | Carrying value | Fair value |
| <b>Assets</b>                         |                |            |                |            |
| Loans and advances to banks .....     | 28,132         | 28,134     | 29,705         | 29,706     |
| Loans and advances to customers ..... | 48,354         | 47,543     | 53,279         | 52,566     |
| <b>Liabilities</b>                    |                |            |                |            |
| Deposits by banks .....               | 32,992         | 32,992     | 32,338         | 32,340     |
| Customer accounts .....               | 42,364         | 42,412     | 42,896         | 42,919     |
| Debt securities in issue .....        | 10,655         | 10,712     | 12,605         | 12,669     |
| Subordinated liabilities .....        | 166            | 167        | 166            | 168        |

## 29 Maturity analysis of financial assets and liabilities

The following is an analysis of undiscounted cash flows payable under financial liabilities by remaining contractual maturities at the balance sheet date.

Trading liabilities and trading derivatives have been included in the “On demand” time bucket and not by contractual maturity, because trading liabilities are typically held for short periods of time. The undiscounted cash flows on hedging derivative liabilities are classified according to their contractual maturity.

| (in millions of euros)               | 31.12.2012     |                     |                             |                           |                   | Total          |
|--------------------------------------|----------------|---------------------|-----------------------------|---------------------------|-------------------|----------------|
|                                      | On demand      | Due within 3 months | Due between 3 and 12 months | Due between 1 and 5 years | Due after 5 years |                |
| Deposits by banks <sup>1</sup> ..... | 232            | 29,453              | 2,199                       | 6,342                     | 345               | 38,571         |
| Customer accounts <sup>1</sup> ..... | 22,945         | 26,741              | 1,795                       | 207                       | 179               | 51,867         |
| Trading liabilities .....            | 36,271         | –                   | –                           | –                         | –                 | 36,271         |
| Financial liabilities                |                |                     |                             |                           |                   |                |
| designated at fair value. . .        | –              | 7                   | 2,004                       | 4,075                     | 750               | 6,836          |
| Derivatives .....                    | 87,984         | –                   | –                           | 1,131                     | –                 | 89,115         |
| Debt securities in issue . . . .     | –              | 5,854               | 2,143                       | 3,478                     | 65                | 11,540         |
| Subordinated liabilities . . . .     | –              | –                   | –                           | 153                       | 35                | 188            |
| Other financial liabilities. . .     | 352            | 810                 | 314                         | 561                       | 187               | 2,224          |
| Loan commitments. . . . .            | 22             | 2,662               | 1,268                       | 12,387                    | 1,746             | 18,085         |
| <b>Total at 31 December 2012</b>     | <b>147,806</b> | <b>65,527</b>       | <b>9,723</b>                | <b>28,334</b>             | <b>3,307</b>      | <b>254,697</b> |

<sup>1</sup> Deposits by banks and customer accounts do not include netting of the repurchase agreements transactions.

**Consolidated financial statements** (continued)**29 Maturity analysis of financial assets and liabilities** (continued)

| (in millions of euros)           | 31.12.2011       |                            |                                    |                                  |                          | <i>Total</i>   |
|----------------------------------|------------------|----------------------------|------------------------------------|----------------------------------|--------------------------|----------------|
|                                  | <i>On demand</i> | <i>Due within 3 months</i> | <i>Due between 3 and 12 months</i> | <i>Due between 1 and 5 years</i> | <i>Due after 5 years</i> |                |
| Deposits by banks <sup>1</sup>   | 419              | 34,817                     | 2,910                              | 6,482                            | 493                      | 45,121         |
| Customer accounts <sup>1</sup>   | 21,637           | 23,806                     | 9,171                              | 567                              | 208                      | 55,389         |
| Trading liabilities              | 38,258           | –                          | –                                  | –                                | –                        | 38,258         |
| <b>Financial liabilities</b>     |                  |                            |                                    |                                  |                          |                |
| designated at fair value         | –                | –                          | –                                  | 4,152                            | 826                      | 4,978          |
| Derivatives                      | 80,989           | –                          | –                                  | 692                              | –                        | 81,681         |
| Debt securities in issue         | –                | 6,906                      | 1,947                              | 4,036                            | 87                       | 12,976         |
| Subordinated liabilities         | –                | –                          | –                                  | 171                              | 35                       | 206            |
| Other financial liabilities      | 765              | 758                        | 371                                | 293                              | 538                      | 2,725          |
| Loan commitments                 | 29               | 3,612                      | 3,974                              | 11,791                           | 1,637                    | 21,043         |
| <b>Total at 31 December 2011</b> | <b>142,097</b>   | <b>69,899</b>              | <b>18,373</b>                      | <b>28,184</b>                    | <b>3,824</b>             | <b>262,377</b> |

<sup>1</sup> Deposits by banks and customer accounts do not include netting of the repurchase agreements transactions.

The following is an analysis of assets and liabilities by remaining contractual maturities at the balance sheet date for assets and liability line items.

Contractual maturity is considered to be a reasonable approximation of expected maturity for the assets and liabilities analysed below. However, for items such as demand deposits and overdrafts, the contractual maturities could differ from expected maturities.

Trading assets and liabilities are excluded because they are not held for collection or settlement over the period of contractual maturity.

| (in millions of euros)          | 31.12.2012                |                                       |                                   |                                  |                          |  | <i>Total</i>  |
|---------------------------------|---------------------------|---------------------------------------|-----------------------------------|----------------------------------|--------------------------|--|---------------|
|                                 | <i>Due within 1 month</i> | <i>Due between 1 month and 1 year</i> | <i>Subtotal due within 1 year</i> | <i>Due between 1 and 5 years</i> | <i>Due after 5 years</i> | <i>Subtotal due after more than 1 year</i> |               |
| <b>Assets</b>                   |                           |                                       |                                   |                                  |                          |  |               |
| <b>Financial assets</b>         |                           |                                       |                                   |                                  |                          |  |               |
| designated at fair value        | –                         | –                                     | –                                 | 5                                | –                        | 5  | 5             |
| Loans and advances to banks     | 22,362                    | 2,951                                 | 25,313                            | 2,585                            | 234                      | 2,819                                      | 28,132        |
| Loans and advances to customers | 14,330                    | 11,174                                | 25,504                            | 11,903                           | 10,947                   | 22,850                                     | 48,354        |
| Financial investments           | –                         | 1,208                                 | 1,208                             | 2,038                            | 5,012                    | 7,050                                      | 8,258         |
| Other financial assets          | 229                       | –                                     | 229                               | –                                | –                        | –  | 229           |
|                                 | <b>36,921</b>             | <b>15,333</b>                         | <b>52,254</b>                     | <b>16,531</b>                    | <b>16,193</b>            | <b>32,724</b>                              | <b>84,978</b> |
| <b>Liabilities</b>              |                           |                                       |                                   |                                  |                          |  |               |
| Deposits by banks               | 22,955                    | 3,783                                 | 26,738                            | 6,022                            | 232                      | 6,254                                      | 32,992        |
| Customer accounts               | 37,442                    | 4,668                                 | 42,110                            | 146                              | 108                      | 254  | 42,364        |
| <b>Financial liabilities</b>    |                           |                                       |                                   |                                  |                          |  |               |
| designated at fair value        | –                         | 1,557                                 | 1,557                             | 3,481                            | 616                      | 4,097                                      | 5,654         |
| Debt securities in issue        | 2,275                     | 5,562                                 | 7,837                             | 2,756                            | 62                       | 2,818                                      | 10,655        |
| Other financial liabilities     | 539                       | –                                     | 539                               | –                                | –                        | –  | 539           |
| Subordinated liabilities        | –                         | –                                     | –                                 | 166                              | –                        | 166  | 166           |
|                                 | <b>63,211</b>             | <b>15,570</b>                         | <b>78,781</b>                     | <b>12,571</b>                    | <b>1,018</b>             | <b>13,589</b>                              | <b>92,370</b> |

## 29 Maturity analysis of financial assets and liabilities (continued)

| (in millions of euros)                                  | 31.12.2011         |                                |                            |                           |                   |                                     | Total         |
|---|--------------------|--------------------------------|----------------------------|---------------------------|-------------------|-------------------------------------|---------------|
|   | Due within 1 month | Due between 1 month and 1 year | Subtotal due within 1 year | Due between 1 and 5 years | Due after 5 years | Subtotal due after more than 1 year |               |
| <b>Assets</b>   |                    |                                |                            |                           |                   |                                     |               |
| Financial assets designated at fair value. . . . .      | –                  | –                              | –                          | 598                       | –                 | 598                                 | 598           |
| Loans and advances to banks . . . . .                   | 22,736             | 4,598                          | 27,334                     | 1,706                     | 665               | 2,371                               | 29,705        |
| Loans and advances to customers . . . . .               | 18,236             | 12,181                         | 30,417                     | 12,226                    | 10,636            | 22,862                              | 53,279        |
| Financial investments . . . . .                         | 15                 | 513                            | 528                        | 4,338                     | 2,652             | 6,990                               | 7,518         |
| Other financial assets . . . . .                        | 1,078              | 28                             | 1,106                      | 11                        | –                 | 11                                  | 1,117         |
|   | <u>42,065</u>      | <u>17,320</u>                  | <u>59,385</u>              | <u>18,879</u>             | <u>13,953</u>     | <u>32,832</u>                       | <u>92,217</u> |
| <b>Liabilities</b>                                      |                    |                                |                            |                           |                   |                                     |               |
| Deposits by banks . . . . .                             | 21,234             | 4,536                          | 25,770                     | 6,179                     | 389               | 6,568                               | 32,338        |
| Customer accounts . . . . .                             | 29,056             | 13,172                         | 42,228                     | 559                       | 109               | 668                                 | 42,896        |
| Financial liabilities designated at fair value. . . . . | –                  | –                              | –                          | 4,880                     | 646               | 5,527                               | 5,527         |
| Debt securities in issue . . . . .                      | 2,756              | 6,013                          | 8,769                      | 3,761                     | 75                | 3,836                               | 12,605        |
| Other financial liabilities . . . . .                   | 576                | 189                            | 765                        | 43                        | 29                | 72                                  | 837           |
| Subordinated liabilities . . . . .                      | –                  | –                              | –                          | 166                       | –                 | 166                                 | 166           |
|   | <u>53,622</u>      | <u>23,910</u>                  | <u>77,532</u>              | <u>15,588</u>             | <u>1,249</u>      | <u>17,837</u>                       | <u>94,369</u> |

Further information regarding the group's liquidity and funding management is available in the Risk management section pages 83 to 85.

## 30 Assets charged as security for liabilities and collateral accepted as security for assets

Financial assets pledged to secure liabilities are as follows:

| (in millions of euros)                                 | 31.12.2012    | 31.12.2011    |
|--|---------------|---------------|
| Treasury bills and other eligible securities . . . . . | 592           | 527           |
| Loans and advances to banks . . . . .                  | 9,660         | 9,300         |
| Loans and advances to customers . . . . .              | 12,521        | 10,000        |
| Debt securities . . . . .                              | 26,215        | 28,898        |
| Equity shares . . . . .                                | –             | –             |
|  | <u>48,988</u> | <u>48,725</u> |

These transactions are conducted under terms that are usual and customary to standard securities lending and repurchase agreements.

### Collateral accepted as security for assets

In 2012, the fair value of financial assets accepted as collateral that the group is permitted to sell or repledge in the absence of default was EUR 51,709 million at 31 December 2012 (EUR 70,455 million at 31 December 2011).

The fair value of financial assets accepted as collateral that have been sold or repledged was EUR 47,162 million at 31 December 2012 (EUR 60,600 million at 31 December 2011). The group is required to return these assets.

These transactions are conducted under terms that are usual and customary to standard stock borrowing and lending activities.

**Consolidated financial statements** (continued)**31 Called up share capital**

The share capital of HSBC France at 31 December 2012 was EUR 337 million divided into 67,437,827 ordinary shares of EUR 5 each.

|                                  | <i>Number of<br/>HSBC France<br/>ordinary<br/>shares</i> | <i>Amount<br/>(in millions<br/>of euros)</i> |
|----------------------------------|--|--|
| <b>At 1 January 2012</b> .....   | <b>67,437,827</b>  | <b>337</b>                                   |
| Shares issued .....              | —  | —  |
| <b>At 31 December 2012</b> ..... | <b>67,437,827</b>  | <b>337</b>                                   |
| <br>                             |  |  |
| At 1 January 2011 .....          | 67,437,820   | 337  |
| Shares issued .....              | 7  | —  |
| At 31 December 2011 .....        | <b>67,437,827</b>  | <b>337</b>                                   |

**32 Notes on the cash flow statement****Non-cash items included in income**

| (in millions of euros)                                    | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Depreciation and amortisation .....                       | <b>55</b>         | 57         |
| Share-based payments .....                                | <b>54</b>         | 9          |
| Loan impairment losses .....                              | <b>117</b>        | 109        |
| Loans written off net of recoveries .....                 | <b>(109)</b>      | (74)       |
| Provisions raised .....                                   | <b>24</b>         | 49         |
| Provisions utilised .....                                 | <b>(25)</b>       | (17)       |
| Impairment of financial investments .....                 | <b>2</b>          | 5          |
| Accretion of discounts and amortisation of premiums ..... | —                 | —          |
| Other .....   | <b>(56)</b>       | (25)       |
|   | <b>59</b>         | 114        |

**Change in operating assets**

| (in millions of euros)                                     | <b>31.12.2012</b> | 31.12.2011 |
|--|-------------------|------------|
| Change in prepayments and accrued income .....             | <b>81</b>         | 146        |
| Change in net trading securities and net derivatives ..... | <b>(1,637)</b>    | 6,783      |
| Change in loans and advances to banks .....                | <b>(1,382)</b>    | 5,826      |
| Change in loans and advances to customers .....            | <b>4,928</b>      | 4,640      |
| Change in financial assets designated at fair value .....  | <b>592</b>        | (3)        |
| Change in other assets .....                               | <b>740</b>        | (177)      |
|  | <b>3,322</b>      | 17,215     |

**Change in operating liabilities**

| (in millions of euros)   | <b>31.12.2012</b> | 31.12.2011 |
|--|-------------------|------------|
| Change in accruals and deferred income .....                   | <b>(72)</b>       | (236)      |
| Change in deposits by banks .....                              | <b>654</b>        | (4,523)    |
| Change in customer accounts .....                              | <b>(532)</b>      | (6,298)    |
| Change in debt securities in issue .....                       | <b>(1,950)</b>    | (1,680)    |
| Change in financial liabilities designated at fair value ..... | <b>126</b>        | (89)       |
| Change in other liabilities .....                              | <b>(444)</b>      | (381)      |
|  | <b>(2,219)</b>    | (13,207)   |

## 32 Notes on the cash flow statement (continued)

### Breakdown of cash and cash equivalents

| (in millions of euros)  | 31.12.2012    | 31.12.2011    |
|---|---------------|---------------|
| Cash and balances at central banks . . . . .  | 6,770         | 4,805         |
| Items in the course of collection from other banks . . . . .                                    | 815           | 806           |
| Loans and advances to banks due in one month or less . . . . .                                  | 22,605        | 23,984        |
| Treasury bills, other bills and certificates of deposit due in less than three months . . . . . | 401           | 195           |
| Less: cash accounts (liabilities) . . . . .   | (771)         | (757)         |
|   | <b>29,820</b> | <b>29,033</b> |

## 33 Risk management

All the HSBC France group's activities involve analysis, evaluation, acceptance and management of some degree of risk or combination of risks.

The most important types of risk arising from financial instruments are credit risk (which includes country and cross-border risk), liquidity risk and market risk. Market risk includes foreign exchange, interest rate and equity price risk. In addition, risk also arises from transactions with special purpose entities, both on- and off-balance sheet, and other types of off-balance sheet arrangements, including financial guarantees, letters of credit and lending commitments.

The management of risks that are significant to the group is discussed in the Risk management section on pages 75 to 97.

### Credit risk management

#### *Initiatives undertaken and risks identified*

The management of credit risk within the HSBC France is discussed in the Risk management section on pages 75 to 80.

#### *Impairment assessment*

Management regularly evaluates the adequacy of the established allowances for impaired loans by conducting a detailed review of the loan portfolio, comparing performance and delinquency statistics with historical trends and assessing the impact of current economic conditions.

Two types of impairment allowance are in place: individually assessed and collectively assessed, which are discussed in Note 2 g.

#### *Exposure to countries in the eurozone*

The transfer of private sector liabilities to sovereign bodies, which started after the 2007 financial crisis, continued to put pressure on government balance sheets. The resulting fiscal imbalance in some industrialised economies led to intensified market concerns about sovereign credit risk in these countries.

In 2012, the decisions of the European governments and the European Central Bank (ECB) calmed significantly the stress about the loans and advances to banks and states and the investors' worries related to the systemic risk inside the eurozone.

The ECB organised LTRO (Long-Term Refinancing Operations) on 22 December 2011 and on 3 March 2012 which suppressed, for the banks, the liquidity risk providing more than EUR 1,000 billion cash into the European financial system.

Moreover, the proposal of the European Commission to create a European Banking Union to sooth the relationship between banks and governments, the creation for the ECB of a European banking monitoring power by the European Meeting, the Outright Monetary Transactions, permitted a tightening of spreads among the entirety of the eurozone.

The eurozone sovereign debt crisis remained the centre of attention throughout the year. The difficulties in implementing the prescribed austerity measures and fiscal discipline, the possibility of countries exiting the eurozone, the escalating fears around high debt to GDP ratios and the need for aid to recapitalise banks weighed down on market sentiment.

HSBC France Global Markets acts as a market-maker and primary dealer on the sovereign debt of eurozone countries for the Group. HSBC France continued to closely manage its exposure in 2012 and regularly updated its assessment of higher risk countries and adjusted its risk appetite accordingly.

**Consolidated financial statements** (continued)**33 Risk management** (continued)

The table overleaf summarises group exposures to selected eurozone countries, for governments and central banks of selected eurozone countries along with near/quasi government agencies.

The countries presented were selected because, during the period considered, they exhibited levels of market volatility which exceeded other eurozone countries and demonstrated fiscal or political uncertainty during 2012. In addition, certain of these countries exhibit high sovereign debt to GDP ratios and short to medium-term maturity concentration of those liabilities.

*Exposures to selected Eurozone countries – sovereigns and agencies***At 31 December 2012**

(in millions of euros)

|                                       | <i>Greece</i> | <i>Ireland</i> | <i>Italy</i> | <i>Portugal</i> | <i>Spain</i> | <i>Total</i> |
|---------------------------------------|---------------|----------------|--------------|-----------------|--------------|--------------|
| Cash and balances                     |               |                |              |                 |              |              |
| at central banks .....                | –             | –              | –            | –               | –            | –            |
| Assets held at amortised cost .....   | –             | –              | –            | –               | –            | –            |
| Financial investments                 |               |                |              |                 |              |              |
| available for sale .....              | –             | –              | 273          | –               | –            | 273          |
| Net trading assets <sup>1</sup> ..... | –             | 85             | 1,070        | 27              | 206          | 1,388        |
| Derivatives <sup>2</sup> .....        | –             | –              | 3            | –               | –            | 3            |
| <b>Total</b> .....                    | <b>–</b>      | <b>85</b>      | <b>1,346</b> | <b>27</b>       | <b>206</b>   | <b>1,664</b> |
| Off-balance sheet exposures .....     | –             | –              | –            | –               | –            | –            |

1 Treasury bills and debt securities held for trading net of short positions.

2 Derivative assets net of collateral and derivative liabilities for which a legally enforceable right of offset exists.

During the first half of 2011, HSBC Group decided to impair the Greek sovereign and agency exposures classified as available for sale, reflecting the further deterioration in Greece's fiscal position and the announced support measures. Since then, HSBC Group didn't impair its sovereign exposures to Ireland, Portugal, Italy and Spain because, despite financial difficulties in these countries, the situation is not severe enough to conclude that loss events have occurred which will have an impact on the future cash flows of these countries' sovereign securities.

In the HSBC France group, the vast majority of the sovereign exposure is classified as trading and the group has no Greek sovereign exposure classified as available for sale. Nevertheless, HSBC in France includes the insurance business which held in 2011 limited exposures classified as available for sale. An impairment charge of EUR 19 million was recognised in 2011 on Greek bonds which represented the cumulative fair value loss on these securities as at 31 December 2011. At the end of 2012, HSBC Assurance sold all of its Greek government securities. The impairment of EUR 19 million was recovered, generating a small positive income.

### 33 Risk management (continued)

#### Maximum exposure to credit risk

The following table presents the maximum exposure to credit risk with respect to financial instruments, before taking account of any collateral held or other credit enhancements, unless such credit enhancements meet offsetting requirements as set out in Note 2. For financial assets recognised in the balance sheet, the exposure to credit risk equals their carrying amount. For financial guarantees granted, the maximum exposure to credit risk is the maximum amount that the group would have to pay if the guarantees were called upon. For loan commitments and other credit-related commitments that are irrevocable over the life of the respective facilities, the maximum exposure to credit risk is the full amount of the committed facilities.

With respect to certain financial assets, the group typically has legally enforceable rights to offset certain credit exposures against amounts owing to the same counterparty. In normal circumstances, there would be no intention of settling net, or of realising the financial assets and settling the financial liabilities simultaneously. Consequently, for reporting purposes, the financial assets are not offset against the respective financial liabilities. However, the exposure to credit risk relating to the respective financial assets is reduced as tabulated below.

|  | 31.12.2012              |                  |                                    |
|--|-------------------------|------------------|------------------------------------|
| (in millions of euros)   | <i>Maximum exposure</i> | <i>Offset</i>    | <i>Net exposure to credit risk</i> |
| <b>Cash and balances at central banks</b> .....                  | 6,770                   | –                | 6,770                              |
| <b>Items in the course of collection from other banks</b> .....  | 815                     | –                | 815                                |
| <b>Trading assets</b> .....                                      | 40,577                  | –                | 40,577                             |
| – treasury and other eligible bills .....                        | 1,392                   | –                | 1,392                              |
| – debt securities .....  | 25,130                  | –                | 25,130                             |
| – loans and advances .....                                       | 14,055                  | –                | 14,055                             |
| <b>Financial assets designated at fair value</b> .....           | 5                       | –                | 5                                  |
| – debt securities .....  | 5                       | –                | 5                                  |
| – loans and advances .....                                       | –                       | –                | –                                  |
| <b>Derivatives</b> .....   | 90,258                  | (87,742)         | 2,516                              |
| <b>Loans and advances held at amortised cost</b> .....           | 76,486                  | (17,119)         | 59,367                             |
| – loans and advances to banks .....                              | 28,132                  | (11,863)         | 16,269                             |
| – loans and advances to customers .....                          | 48,354                  | (5,256)          | 43,098                             |
| <b>Financial investments</b> .....                               | 8,018                   | –                | 8,018                              |
| – treasury and other eligible bills .....                        | 273                     | –                | 273                                |
| – debt securities .....  | 7,745                   | –                | 7,745                              |
| <b>Other assets</b> .....  | 1,084                   | –                | 1,084                              |
| <b>Off-balance sheet</b> .....                                   | 22,594                  | –                | 22,594                             |
| – financial guarantees and other credit-related guarantees ..... | 4,509                   | –                | 4,509                              |
| – loan commitments and other credit-related commitments .....    | 18,085                  | –                | 18,085                             |
| <b>Total</b> .....   | <b>246,607</b>          | <b>(104,861)</b> | <b>141,746</b>                     |

## Consolidated financial statements (continued)

## 33 Risk management (continued)

| (in millions of euros)   | 31.12.2011          |                 | Net exposure<br>to credit<br>risk |
|--|---------------------|-----------------|-----------------------------------|
|  | Maximum<br>exposure | Offset          |                                   |
| Cash and balances at central banks .....                         | 4,805               | –               | 4,805                             |
| Items in the course of collection from other banks .....         | 806                 | –               | 806                               |
| Trading assets .....   | 39,013              | –               | 39,013                            |
| – treasury and other eligible bills .....                        | 699                 | –               | 699                               |
| – debt securities .....  | 24,762              | –               | 24,762                            |
| – loans and advances .....                                       | 13,552              | –               | 13,552                            |
| Financial assets designated at fair value .....                  | 598                 | –               | 598                               |
| – debt securities .....  | 4                   | –               | 4                                 |
| – loans and advances .....                                       | 594                 | –               | 594                               |
| Derivatives .....  | 82,738              | (80,594)        | 2,144                             |
| Loans and advances held at amortised cost .....                  | 82,984              | (12,805)        | 70,179                            |
| – loans and advances to banks .....                              | 29,705              | (2,305)         | 27,400                            |
| – loans and advances to customers .....                          | 53,279              | (10,500)        | 42,779                            |
| Financial investments .....                                      | 7,096               | –               | 7,096                             |
| – treasury and other eligible bills .....                        | 200                 | –               | 200                               |
| – debt securities .....  | 6,896               | –               | 6,896                             |
| Other assets .....   | 1,896               | –               | 1,896                             |
| Off-balance sheet .....  | 27,073              | –               | 27,073                            |
| – financial guarantees and other credit-related guarantees ..... | 6,031               | –               | 6,031                             |
| – loan commitments and other credit-related commitments .....    | 21,042              | –               | 21,042                            |
| <b>Total .....</b>   | <b>247,009</b>      | <b>(93,398)</b> | <b>153,610</b>                    |

## Loans and advances to customers by industry sector

|  | 31.12.2012  |   | 31.12.2011  |   |
|--|---|---|---|---|
|  | Gross<br>loans and<br>advances to<br>customers<br>(in millions<br>of euros) | Gross loans<br>by industry<br>sector as a<br>% of total<br>gross loans<br>(%) | Gross<br>loans and<br>advances to<br>customers<br>(in millions<br>of euros) | Gross loans<br>by industry<br>sector as a<br>% of total<br>gross loans<br>(%) |
| <b>Personal .....</b>  | <b>10,315</b>   | <b>21.00</b>  | 9,786   | 18.11   |
| – residential mortgages .....  | 2,004   | 4.08  | 2,592   | 4.80  |
| – other personal .....   | 8,311   | 16.92   | 7,194   | 13.31   |
| <b>Corporate and commercial .....</b>  | <b>21,856</b>   | <b>44.51</b>  | 22,481  | 41.61   |
| – commercial, industrial and international trade .....                       | 11,099  | 22.60   | 11,102  | 20.55   |
| – commercial real estate<br>(including private real estate companies*) ..... | 6,195   | 12.62   | 6,110   | 11.31   |
| – other property-related .....   | 254   | 0.52  | 267   | 0.49  |
| – government .....   | 248   | 0.50  | 141   | 0.26  |
| – other commercial .....   | 4,060   | 8.27  | 4,861   | 9.00  |
| <b>Financial .....</b>   | <b>16,935</b>   | <b>34.49</b>  | 21,767  | 40.28   |
| – non-bank financial institutions .....                                      | 16,934  | 34.48   | 21,748  | 40.24   |
| – settlement accounts .....  | 1   | 0.01  | 19  | 0.04  |
| <b>Total gross loans and advances to customers .....</b>                     | <b>49,106</b>   | <b>100.00</b>   | <b>54,034</b>   | <b>100.00</b>   |

\* SCI familiales.



### 33 Risk management (continued)

#### *Loans and advances to customers by geographical area (excluding reverse repo transactions and settlement accounts)*

As at 31 December 2012, 87 per cent of loans to customers (excluding reverse repo transactions and settlement accounts) were to French counterparties (84 per cent as at 31 December 2011).

Reverse repo transactions amounted to 29 per cent with French counterparties and 71 per cent with counterparties in other European countries (primarily in the United Kingdom).

#### *Credit quality of financial instruments*

The five classifications below describe the credit quality of the group's lending, debt securities portfolios and derivatives. These categories each encompass a range of more granular internal credit rating grades assigned to wholesale and retail lending business, as well as the external ratings attributed by external agencies to debt securities.

There is no direct correlation between the internal and external ratings at granular level, except insofar as both fall within one of the five classifications.

#### Quality Classification

|                        | <i>Wholesale lending<br/>and derivatives</i> | <i>Retail lending</i> | <i>Debt securities/other</i> |
|------------------------|--|-----------------------|------------------------------|
| Strong . . . . .       | CRR 1 and CRR 2                              | EL 1 and EL 2         | A- and above                 |
| Good . . . . .         | CRR 3  | EL 3                  | BBB+ to BBB-                 |
| Satisfactory . . . . . | CRR 4 and CRR 5                              | EL 4 and EL 5         | BB+ to B+ and unrated        |
| Sub-standard . . . . . | CRR 6 and CRR 8                              | EL 6 and EL 8         | B and below                  |
| Impaired . . . . .     | CRR 9 and CRR 10                             | EL 9 and EL 10        | Impaired                     |

#### Quality classification definitions

“Strong”: exposures demonstrate a strong capacity to meet financial commitments, with negligible or low probability of default and/or low levels of expected loss. Retail accounts operate within applicable product parameters and only exceptionally show any period of delinquency.

“Good”: exposures require closer monitoring and demonstrate a good capacity to meet financial commitments, with low default risk. Retail accounts typically showing only short periods of delinquency, with any losses expected to be minor following the adoption of recovery processes.

“Satisfactory”: exposures require closer monitoring and demonstrate an average to fair capacity to meet financial commitments, with moderate default risk. Retail accounts typically showing only short periods of delinquency, with any losses expected to be minor following the adoption of recovery processes.

“Sub-standard”: exposures require varying degrees of special attention and default risk is of greater concern. Retail portfolio segments showing longer delinquency periods of generally up to 90 days; past due and/or expected losses are higher due to a reduced ability to mitigate these through security realisation or other recovery processes.

“Impaired”: exposures have been assessed, individually or collectively, as impaired. The group observes the disclosure convention, reflected in the quality classification definitions above, that all retail accounts delinquent by 90 days or more (180 days for mortgage loans) are considered impaired.

#### Granular risk rating scales

The CRR (Customer Risk Rating) 10-grade scale maps to a more granular underlying 22-grade scale of obligor probability of default. The scales are used group-wide for all distinct customers, depending on the Basel II approach adopted for the exposure in question. The EL (Expected Loss) 10-grade scale for retail business summarises a more granular, group-wide, 29-grade scale combining obligor and facility/product risk factors in a composite measure. The composite EL measure enables the diverse risk profiles of retail portfolios across the HSBC Group to be assessed on a more comparable scale than through the direct utilisation of Probability of Default (PD) and Loss Given Default (LGD) measures. For consistency of disclosure and based on market practice for transactions in debt securities and certain other financial instruments, external ratings have been aligned as above, and in the table of “Distribution of financial instruments by credit quality” below, to the five quality classifications defined for internally-rated exposures, although it should be noted that there is no fixed correlation between internal and external ratings. The Standard and Poor's ratings are cited, along with those of other agencies being treated in an equivalent fashion. Debt securities with short-term ratings are reported below against the long-term rating of the issuer of the short-term debt securities. If major rating agencies have different ratings for the same debt securities, the securities are reported against the lower rating.

**Consolidated financial statements** (continued)**33 Risk management** (continued)

Impairment is not measured for assets held in trading portfolios or designated at fair value, as assets in such portfolios are managed according to movements in fair value, and the fair value movement is taken directly through the profit and loss statement. Consequently, all such balances are reported under “Neither past due nor impaired”.

For details of impairment incurred on available-for-sale debt and equity securities, see “Accounting policies” in Note 2 j page 113.

*Distribution of financial instruments by credit quality*

|   | 31.12.2012                       |               |                   |                  |                             |              |                                    | Total          |
|---|----------------------------------|---------------|-------------------|------------------|-----------------------------|--------------|------------------------------------|----------------|
|   | Neither past due<br>nor impaired |               |                   |                  | Past<br>due not<br>impaired | Impaired     | Impair-<br>ment<br>allow-<br>ances |                |
| (in millions of euros)  | Strong                           | Good          | Satis-<br>factory | Sub-<br>standard |                             |              |                                    |                |
| <b>Cash and balances<br/>at central banks</b> .....                     | 6,770                            | –             | –                 | –                | –                           | –            | –                                  | 6,770          |
| <b>Items in the course of<br/>collection from other<br/>banks</b> ..... | 815                              | –             | –                 | –                | –                           | –            | –                                  | 815            |
| <b>Trading assets</b> .....   | 30,535                           | 6,284         | 3,727             | 31               | –                           | –            | –                                  | 40,577         |
| Treasury and other eligible<br>bills and debt securities . . . .        | 20,690                           | 4,952         | 880               | –                | –                           | –            | –                                  | 26,522         |
| Loans and advances to banks .   | 8,088                            | 1,038         | 2,163             | 31               | –                           | –            | –                                  | 11,320         |
| Loans and advances<br>to customers .....                                | 1,757                            | 294           | 684               | –                | –                           | –            | –                                  | 2,735          |
| <b>Financial assets<br/>designated at fair value</b> . . . .            | 5                                | –             | –                 | –                | –                           | –            | –                                  | 5              |
| Treasury and other eligible<br>bills and debt securities . . . .        | 5                                | –             | –                 | –                | –                           | –            | –                                  | 5              |
| Loans and advances to banks .   | –                                | –             | –                 | –                | –                           | –            | –                                  | –              |
| Loans and advances<br>to customers .....                                | –                                | –             | –                 | –                | –                           | –            | –                                  | –              |
| <b>Derivatives</b> .....  | 85,243                           | 2,582         | 2,397             | 36               | –                           | –            | –                                  | 90,258         |
| <b>Loans and advances held at<br/>amortised cost</b> .....              | 57,832                           | 10,230        | 6,885             | 693              | 135                         | 1,463        | (752)                              | 76,486         |
| Loans and advances<br>to banks .....                                    | 27,158                           | 900           | 63                | 11               | –                           | –            | –                                  | 28,132         |
| Loans and advances<br>to customers .....                                | 30,674                           | 9,330         | 6,822             | 682              | 135                         | 1,463        | (752)                              | 48,354         |
| <b>Financial investments</b> .....                                      | 7,661                            | 302           | 55                | –                | –                           | 6            | (5)                                | 8,019          |
| Treasury and other similar<br>bills and debt securities . . . .         | 7,661                            | 302           | 55                | –                | –                           | 6            | (5)                                | 8,019          |
| <b>Other assets</b> .....   | 30                               | –             | 1,053             | –                | –                           | –            | –                                  | 1,083          |
| Endorsements and<br>acceptances .....                                   | –                                | –             | –                 | –                | –                           | –            | –                                  | –              |
| Accrued income and other . . .  | 30                               | –             | 1,053             | –                | –                           | –            | –                                  | 1,083          |
| <b>Total</b> .....  | <b>188,889</b>                   | <b>19,398</b> | <b>14,117</b>     | <b>760</b>       | <b>135</b>                  | <b>1,469</b> | <b>(757)</b>                       | <b>224,011</b> |

**33 Risk management (continued)**

31.12.2011

| (in millions of euros)  | Neither past due<br>Nor impaired |               |                   |                  |                             |              | Impair-<br>ment<br>allow-<br>ances | Total          |
|---|----------------------------------|---------------|-------------------|------------------|-----------------------------|--------------|------------------------------------|----------------|
|   | Strong                           | Good          | Satis-<br>factory | Sub-<br>standard | Past<br>due not<br>impaired | Impaired     |                                    |                |
| Cash and balances<br>at central banks .....                   | 4,805                            | –             | –                 | –                | –                           | –            | –                                  | 4,805          |
| Items in the course of<br>collection from other banks ..      | 806                              | –             | –                 | –                | –                           | –            | –                                  | 806            |
| Trading assets .....  | 34,800                           | 2,291         | 1,864             | 58               | –                           | –            | –                                  | 39,013         |
| Treasury and other eligible<br>bills and debt securities .... | 24,710                           | 312           | 439               | –                | –                           | –            | –                                  | 25,461         |
| Loans and advances to banks ..                                | 7,643                            | 1,860         | 970               | 58               | –                           | –            | –                                  | 10,531         |
| Loans and advances<br>to customers .....                      | 2,447                            | 119           | 455               | –                | –                           | –            | –                                  | 3,021          |
| Financial assets<br>designated at fair value .....            | 598                              | –             | –                 | –                | –                           | –            | –                                  | 598            |
| Treasury and other eligible<br>bills and debt securities .... | 5                                | –             | –                 | –                | –                           | –            | –                                  | 5              |
| Loans and advances to banks ..                                | –                                | –             | –                 | –                | –                           | –            | –                                  | –              |
| Loans and advances<br>to customers .....                      | 593                              | –             | –                 | –                | –                           | –            | –                                  | 593            |
| Derivatives .....   | 77,524                           | 3,636         | 1,530             | 48               | –                           | –            | –                                  | 82,738         |
| Loans and advances held at<br>amortised cost .....            | 64,111                           | 10,431        | 6,648             | 865              | 234                         | 1,449        | (755)                              | 82,983         |
| Loans and advances<br>to banks .....                          | 29,434                           | 232           | 33                | 6                | –                           | –            | –                                  | 29,705         |
| Loans and advances<br>to customers .....                      | 34,678                           | 10,199        | 6,615             | 859              | 234                         | 1,449        | (755)                              | 53,279         |
| Financial investments .....                                   | 6,955                            | 30            | 110               | –                | –                           | 6            | (5)                                | 7,096          |
| Treasury and other similar<br>bills and debt securities ....  | 6,955                            | 30            | 110               | –                | –                           | 6            | (5)                                | 7,096          |
| Other assets .....  | 88                               | –             | 1,809             | –                | –                           | –            | –                                  | 1,897          |
| Endorsements and<br>acceptances .....                         | –                                | –             | –                 | –                | –                           | –            | –                                  | –              |
| Accrued income and other ...                                  | 88                               | –             | 1,809             | –                | –                           | –            | –                                  | 1,897          |
| <b>Total .....</b>  | <b>189,687</b>                   | <b>16,388</b> | <b>11,961</b>     | <b>971</b>       | <b>234</b>                  | <b>1,455</b> | <b>(760)</b>                       | <b>219,936</b> |

**Consolidated financial statements** (continued)**33 Risk management** (continued)**Ageing analysis of past due but not impaired gross financial instruments**

The following table provides an analysis of gross loans and advances to customers held at amortised cost which are past due but not considered impaired. There are no other significant balance sheet items where past due balances are not considered impaired.

| (in millions of euros)           | <i>Up to<br/>29 days</i> | <i>30-59 days</i> | <i>60-89 days</i> | <i>Total</i> |
|----------------------------------|--------------------------|-------------------|-------------------|--------------|
| <b>At 31 December 2012</b> ..... | <b>100</b>               | <b>21</b>         | <b>14</b>         | <b>135</b>   |
| At 31 December 2011 .....        | 178                      | 41                | 15                | 234          |

**Movement in allowance accounts for total loans and advances**

| (in millions of euros)                         | <b>Year ended 31.12.2012</b>     |                                  |              |
|--|----------------------------------|----------------------------------|--------------|
|  | <i>Individually<br/>assessed</i> | <i>Collectively<br/>assessed</i> | <i>Total</i> |
| <b>At 1 January</b> .....                      | <b>(684)</b>                     | <b>(71)</b>                      | <b>(755)</b> |
| Amounts written off .....                      | <b>114</b>                       | –                                | <b>114</b>   |
| Release of allowances no longer required ..... | <b>145</b>                       | <b>4</b>                         | <b>149</b>   |
| (Charge) to income statement .....             | <b>(259)</b>                     | <b>(10)</b>                      | <b>(269)</b> |
| Exchange and other movements .....             | <b>7</b>                         | <b>1</b>                         | <b>8</b>     |
| <b>At 31 December</b> .....                    | <b>(676)</b>                     | <b>(76)</b>                      | <b>(752)</b> |

| (in millions of euros)                         | <b>Year ended 31.12.2011</b>     |                                  |              |
|--|----------------------------------|----------------------------------|--------------|
|  | <i>Individually<br/>assessed</i> | <i>Collectively<br/>assessed</i> | <i>Total</i> |
| <b>At 1 January</b> .....                      | <b>(661)</b>                     | <b>(68)</b>                      | <b>(729)</b> |
| Amounts written off .....                      | 75                               | –                                | 75           |
| Release of allowances no longer required ..... | 150                              | 2                                | 152          |
| (Charge) to income statement .....             | (255)                            | (5)                              | (260)        |
| Exchange and other movements .....             | 7                                | –                                | 7            |
| <b>At 31 December</b> .....                    | <b>(684)</b>                     | <b>(71)</b>                      | <b>(755)</b> |

**Impairment allowances against loans and advances to customers**

| (in per cent)   | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| Total impairment allowances in percentage to gross lending <sup>1</sup> ..... |                   |            |
| – individually assessed impairment allowances .....                           | <b>1.95</b>       | 1.99       |
| – collectively assessed impairment allowances .....                           | <b>0.22</b>       | 0.21       |
| <b>Total</b> .....  | <b>2.17</b>       | 2.20       |

<sup>1</sup> Net of repurchase agreement transactions and settlement accounts.

### 33 Risk management (continued)

#### Loan impairment charges and other credit risk provisions

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Individually assessed impairment allowances</b>  |                   |                   |
| New allowances and unprovided losses .....  | 258               | 255               |
| Release of allowances no longer required .....  | (145)             | (150)             |
| Recoveries of amounts previously written off .....  | (4)               | (1)               |
| Amount written off .....  | 114               | 75                |
| Utilisation of allowance .....  | <u>(114)</u>      | <u>(75)</u>       |
|   | <u>109</u>        | <u>104</u>        |
| <b>Collectively assessed impairment allowances</b>  |                   |                   |
| New allowances .....  | 10                | 5                 |
| Release of allowances no longer required .....  | (4)               | (2)               |
| Recoveries of amounts previously written off .....  | –                 | –                 |
|   | <u>6</u>          | <u>3</u>          |
| <b>Total charge for impairment losses</b> .....   | <u>115</u>        | <u>107</u>        |
| – banks .....   | –                 | –                 |
| – customers .....   | 115               | 107               |
| Other credit risk provisions .....  | –                 | –                 |
| Impairment charges on debt security investments available-for-sale .....  | <u>2</u>          | <u>2</u>          |
| <b>Loan impairment charges and other credit risk provisions</b> .....   | <u>117</u>        | <u>109</u>        |
| Customer charge for impairment losses as a percentage<br>of closing gross loans and advances to customers ..... | <u>0.23%</u>      | <u>0.20%</u>      |
| <b>Balances outstanding</b>   |                   |                   |
| Non-performing loans .....  | 1,463             | 1,449             |
| Individually impairment allowances .....  | 676               | 684               |
| Gross loans and advances  |                   |                   |
| – banks .....   | 28,132            | 29,705            |
| – customers .....   | <u>49,106</u>     | <u>54,034</u>     |
| <b>Total</b> .....  | <u>77,238</u>     | <u>83,739</u>     |
| <b>Total allowances cover as a percentage of non-performing loans and advances</b> .....                        | <u>46.21%</u>     | <u>47.20%</u>     |

#### Collateral and other credit enhancements

Although collateral can be an important mitigant of credit risk, the HSBC Group's practice is to lend on the basis of the customer's ability to meet their obligations out of their resources rather than rely on the value of security. For some loans, a charge over collateral is obtained and considered in determining the credit decision and pricing. In the event of a default, HSBC France may use the collateral as a source of repayment.

Depending upon its nature, collateral can have a significant financial effect in mitigating exposure to credit risk of the HSBC France group. The value of this collateral is based on fixed charges the HSBC France group holds over a borrower's specific asset. As at 31 December 2012, the total collateral value accepted by HSBC France is EUR 44,636 million (EUR 58,117 million in 2011).

Moreover, note the HSBC France group may employ other types of collateral and credit risk enhancements, such as second charges, unsupported guarantees, but the valuation of such mitigants is less certain and their financial effect has not been quantified.

## Consolidated financial statements (continued)

### 33 Risk management (continued)

#### Market risk management

The objective of the Group's market risk monitoring is to manage and control market risk exposures in order to optimise return on risk while maintaining a market profile consistent with its status as a major provider of financial products and services.

#### Market risk assessment tools

- Value at Risk

One of the principal tools used by the Group to monitor and limit market risk exposure is VaR (Value at Risk). An internal model of HSBC France is used to calculate VaR.

VaR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence (for the Group, 99 per cent). HSBC France calculates VaR daily. The VaR model used by HSBC France, as for the Group, is based on historical simulation.

The historical simulation model derives plausible future scenarios from historical market rates time series, taking account of inter relationships between different markets and rates, for example between interest rates and foreign exchange rates.

Potential variations in market prices are calculated with reference to market data from the last two years. The internal model of HSBC France was revalidated by the French regulator in 2007 for capital requirement calculations. Since January 2007, HSBC France has been calculating a one-day VaR.

Although a useful guide to risk, VaR should always be viewed in the context of its limitations. For example:

- the use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

HSBC France recognises these limitations by supplementing its VaR limits by sensitivity limit structures. Additionally, stress testing scenarios are applied, both on individual portfolios and on HSBC France's consolidated positions. Stress scenarios are defined by a group of specialists in Paris (market heads, controllers) in accordance with Group rules and practices.

VaR captures the traditional risk factors directly observable on a daily basis, such as exchange rates, interest rates, equity prices, etc., but does not take account of potential changes in more exotic factors such as correlations, basis risk, return to mean parameters, etc. Therefore, since 31 December 2007, HSBC France also calculates an additional VaR measure called "Add-On VaR" in respect of these exotic risk factors.

In addition, since 31 December 2011, HSBC France reports a stressed VaR number. Similarly to VaR, stressed VaR is computed using historical simulations and a 99 per cent confidence interval. However, unlike VaR, stressed VaR considers a 10-day holding period, and is based on stressed historical data. Stressed VaR can be rescaled to a one-day equivalent holding period by dividing it by the square root of 10.

### 33 Risk management (continued)

The one-day VaR on market exposures, taking into account both market trading and structural interest rate risk, amounted to:

| (in millions of euros)           | <i>One-day<br/>VaR<br/>without<br/>Add-On<br/>perimeter</i> | <i>Add-On<br/>VaR</i> |
|----------------------------------|---|-----------------------|
| <b>At 31 December 2012</b> ..... | <b>15.40</b>  | <b>1.3</b>            |
| At 31 December 2011 .....        | 22.18   | 5.75                  |

| (in millions of euros) | <i>One-day VaR without Add-On perimeter</i> |                |                | <i>Add-On VaR</i> |                |                |
|------------------------|---|----------------|----------------|-------------------|----------------|----------------|
|                        | <i>Average</i>                              | <i>Minimum</i> | <i>Maximum</i> | <i>Average</i>    | <i>Minimum</i> | <i>Maximum</i> |
| <b>2012</b> .....      | <b>15,89</b>                                | <b>10,16</b>   | <b>23,77</b>   | <b>3,9</b>        | <b>1,3</b>     | <b>6,1</b>     |
| 2011 .....             | 24,92                                       | 14,51          | 41,47          | 5,82              | 4,68           | 6,95           |

It can be noted that as a consequence of the risk reduction exercises run by HSBC France in the past year, VaR levels were usually lower in 2012 than in 2011.

The one-day equivalent stressed VaR amounted to:

| (in millions of euros)           | <i>One-day equivalent<br/>stressed VaR</i> |
|----------------------------------|--|
| <b>At 31 December 2012</b> ..... | <b>14.23</b>                               |
| At 31 December 2011 .....        | 14.72                                      |

| (in millions of euros)           | <i>One-day equivalent stressed VaR</i> |                |                |
|----------------------------------|--|----------------|----------------|
|                                  | <i>Average</i>                         | <i>Minimum</i> | <i>Maximum</i> |
| <b>At 31 December 2012</b> ..... | <b>12.34</b>                           | <b>9.51</b>    | <b>14.68</b>   |

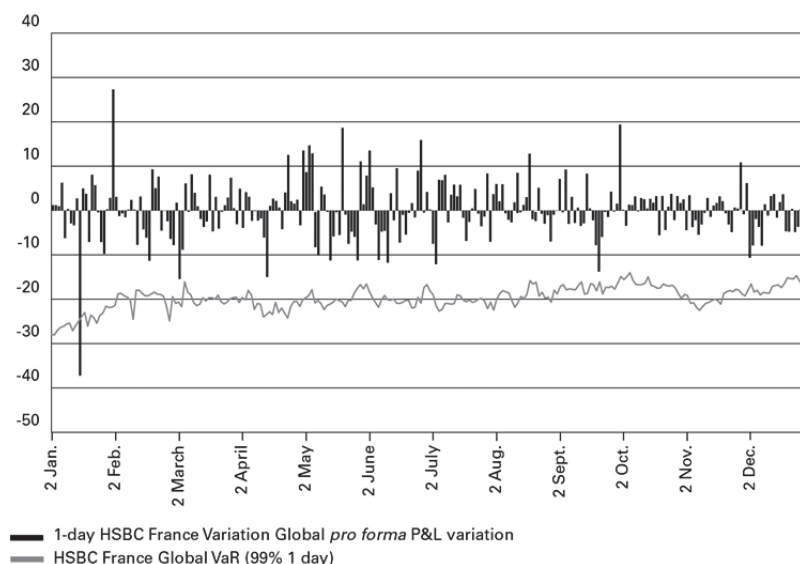
- Backtesting

The model is back-tested by taking 99 per cent, one-day VaR figures and comparing them with daily *pro forma* results determined from changes in market prices assuming constant positions. Backtesting is carried out on a D+2 basis by business area and for all of the HSBC France group's market positions.

It allows the model to be validated, ensuring that the recorded result, in absolute terms, is lower than the calculated one-day VaR in 99 per cent of cases.

#### **Pro forma backtesting January 2012 – December 2012**

(in millions of euros)



**Consolidated financial statements** (continued)**33 Risk management** (continued)

The reduction in risk positions performed in 2012, combined with lower observed market volatility resulted in a decrease in the number of backtesting exceptions from nine in 2011 to one in 2012.

*Fair value and price verification control*

Where certain financial instruments are carried on the Group's balance sheet at fair values, it is the Group policy that the valuation and the related price verification processes be subject to independent testing across the Group. Financial instruments which are accounted for on a fair value basis include assets held in the trading portfolio, financial instruments designated at fair value, obligations related to securities sold short, all derivative financial instruments and available-for-sale securities.

The determination of fair values is therefore a significant element in the reporting of the Group's Global Markets activities.

All significant valuation policies, and any changes thereto, must be approved by Senior Finance Management. The Group's governance of financial reporting requires that Financial Control Departments across the Group be independent of the risk-taking businesses, with the Finance functions having ultimate responsibility for the determination of fair values included in the financial statements, and for ensuring that the Group's policies and relevant accounting standards are adhered to.

*Trading*

Market risk in trading portfolios is monitored and controlled at both portfolio and position levels using a complementary set of techniques, such as VaR and present value of a basis point, together with stress and sensitivity testing and concentration limits. These techniques quantify the impact on capital of defined market movements.

Other controls include restricting individual operations to trading within a list of permissible instruments authorised by Wholesale & Market Risk, and enforcing rigorous new product approval procedures. In particular, trading in the more complex derivative products is concentrated with appropriate levels of product expertise and robust system controls.

HSBC France's policy on hedging is to manage economic risk in the most appropriate way without regard as to whether hedge accounting is available, within limits regarding the potential volatility of reported earnings. Trading VaR is further analysed below by risk types, by positions taken with trading intent and by positions taken without trading intent:

**Total trading VaR by risk type**

| (in millions of euros)           | <i>Foreign<br/>exchange</i> | <i>Interest<br/>rate trading</i> | <i>Equity</i> | <i>Total</i> |
|----------------------------------|-----------------------------|----------------------------------|---------------|--------------|
| <b>At 31 December 2012</b> ..... | <b>0.07</b>                 | <b>15.78</b>                     | –             | <b>15.76</b> |
| At 31 December 2011 .....        | 0.04                        | 22.65                            | –             | 22.6         |
| <b>Average</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | <b>0.04</b>                 | <b>15.78</b>                     | –             | <b>15.79</b> |
| 2011 .....                       | 0.08                        | 24.36                            | 0.01          | 24.36        |
| <b>Minimum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | –                           | <b>11.36</b>                     | –             | <b>11.36</b> |
| 2011 .....                       | 0.01                        | 13.53                            | –             | 13.55        |
| <b>Maximum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | <b>0.17</b>                 | <b>22.9</b>                      | –             | <b>22.43</b> |
| 2011 .....                       | 0.24                        | 40.25                            | 0.08          | 40.26        |



### 33 Risk management (continued)

#### Positions taken with trading intent – VaR by risk type

| (in millions of euros)           | <i>Foreign<br/>exchange</i> | <i>Interest<br/>rate trading</i> | <i>Equity</i> | <i>Total</i> |
|----------------------------------|-----------------------------|----------------------------------|---------------|--------------|
| <b>At 31 December 2012</b> ..... | <b>0.07</b>                 | <b>15.52</b>                     | –             | <b>15.51</b> |
| At 31 December 2011 .....        | 0.04                        | 22.65                            | –             | 22.59        |
| <b>Average</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | <b>0.04</b>                 | <b>15.8</b>                      | –             | <b>15.73</b> |
| 2011 .....                       | 0.08                        | 24.5                             | 0.01          | 24.5         |
| <b>Minimum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | –                           | <b>11.27</b>                     | –             | <b>11.26</b> |
| 2011 .....                       | 0.01                        | 15.32                            | –             | 15.38        |
| <b>Maximum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | <b>0.17</b>                 | <b>22.87</b>                     | –             | <b>22.43</b> |
| 2011 .....                       | 0.24                        | 41.17                            | 0.08          | 41.19        |

#### Positions taken without trading intent – VaR by risk type

| (in millions of euros)           | <i>Foreign<br/>exchange</i> | <i>Interest<br/>rate trading</i> | <i>Equity</i> | <i>Total</i> |
|----------------------------------|-----------------------------|----------------------------------|---------------|--------------|
| <b>At 31 December 2012</b> ..... | –                           | <b>2.37</b>                      | –             | <b>2.37</b>  |
| At 31 December 2011 .....        | –                           | 0.99                             | –             | 0.99         |
| <b>Average</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | –                           | <b>0.95</b>                      | –             | <b>0.95</b>  |
| 2011 .....                       | –                           | 1.50                             | –             | 1.50         |
| <b>Minimum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | –                           | <b>0.24</b>                      | –             | <b>0.24</b>  |
| 2011 .....                       | –                           | –                                | –             | –            |
| <b>Maximum</b>                   |                             |                                  |               |              |
| <b>2012</b> .....                | –                           | <b>2.43</b>                      | –             | <b>2.43</b>  |
| 2011 .....                       | –                           | 3.14                             | –             | 3.14         |

#### Sensitivity analysis

As of 31 December 2012, HSBC France Global Markets was mainly exposed to interest rate curve and spread risks (*i.e.* relative difference) coming from the swap and reference bond curves, denominated in euros, whether these notes are from sovereign eurozone government, supranational issuers, government agencies or issuers of covered bonds. In line with the risk reduction policy conducted in 2011, exposures to Euro sovereign issuers, and in particular Euro peripherals, were reduced over the past year. Limits expressed in terms of interest rates sensitivities were downsized accordingly.

HSBC France Global Markets is also subject to sensitivities in terms of interest rate volatility and interest rate correlation, primarily in relation to EUR and USD.

All of these sensitivities are assessed and measured on a daily basis using standard conventional methods as used by the industry.

An aggregate representation is HSBC France Global Markets' 1-day 99 per cent VaR as of 31 December 2012: EUR -15.4 million.

In addition to its trading activities, HSBC France has developed since 2011 a non-trading accrual portfolio. Bonds held in this portfolio are hedged using swaps so as to reduce their exposure to interest rate moves. In addition, holdings are in high quality sovereign and quasi sovereign eurozone issuers.

**Consolidated financial statements** (continued)**33 Risk management** (continued)

Financial instruments of Global Banking and Markets non-trading portfolios are valued for financial reporting purposes, and the sensitivity of the value to these instruments to fluctuations in interest rates is also computed.

*Capital adequacy reporting*

The internal model allows for the daily calculation of Value at Risk for all positions. It has been approved by the French *Autorité de contrôle prudentiel* for regulatory capital adequacy calculations. It covers the quasi-totality of market risks within HSBC France. Key risks not covered by the internal model are measured using the standardised approach devised by the Bank of International Settlements and transposed into French law by CRBF regulation 95-02.

Capital requirements with respect to market risks break down as follows (in millions of euros):

| (in millions of euros)                        | 31.12.2012    |               | 31.12.2011 |        |
|---|---------------|---------------|------------|--------|
|   | BIS           | CAD           | BIS        | CAD    |
| <b>Internal Model VaR<sup>1</sup>:</b>        | <b>196.8</b>  | <b>196.8</b>  | 381.97     | 381.97 |
| Foreign exchange risk                         | 0.39          | 0.39          | 1.29       | 1.29   |
| General interest rate risk                    | 196.63        | 196.63        | 380.4      | 380.4  |
| General equities risk                         | –             | –             | –          | –      |
| Netting effect                                | (0.21)        | (0.21)        | 0.28       | 0.28   |
| <b>Internal Model Stress VaR<sup>1</sup>:</b> | <b>154.94</b> | <b>154.94</b> | 311.63     | 311.63 |
| Foreign exchange risk                         | 0.79          | 0.79          | 1.51       | 1.51   |
| General interest rate risk                    | 154.69        | 154.69        | 311.63     | 311.63 |
| General equities risk                         | –             | –             | –          | –      |
| Netting effect                                | (0.54)        | (0.54)        | (1.51)     | (1.51) |
| <b>Standards methods:</b>                     | <b>56.72</b>  | <b>56.72</b>  | 64.78      | 64.78  |
| Foreign exchange risk                         | –             | –             | –          | –      |
| General interest rate risk                    | 15.4          | 15.4          | –          | –      |
| Specific interest rate risk                   | 41.28         | 41.28         | 64.78      | 64.78  |
| General equities risk                         | –             | –             | –          | –      |
| Specific equities risk                        | –             | –             | –          | –      |
| <b>Total</b>                                  | <b>408.46</b> | <b>408.46</b> | 758.38     | 758.38 |

<sup>1</sup> Including the Add-On perimeter.

It can be observed that following regulatory changes (Basel 2.5), HSBC France cost of capital includes a stressed VaR item since 31 December 2011. Stressed VaR is a market risk indicator calibrated to historical data from a period of significant financial stress. It is computed considering a 10-day holding period and a 99 per cent one-tailed confidence interval.

### 33 Risk management (continued)

#### Analysis of Asset-Backed Securities (ABS)

The table below shows the group's market risk exposure to Asset-Backed Securities.

|  | 31.12.2012                   |                                   |                                     |                              |
|--|------------------------------|-----------------------------------|-------------------------------------|------------------------------|
| (in millions of euros)                               | Gross principal <sup>2</sup> | CDS gross protection <sup>3</sup> | Net Principal exposure <sup>4</sup> | Carrying amount <sup>5</sup> |
| – High grade <sup>1</sup> .....                      | 510                          | –                                 | 510                                 | 506                          |
| – Rated C to A .....                                 | 69                           | –                                 | 69                                  | 67                           |
| – Not publicly rated .....                           | 15                           | –                                 | 15                                  | 13                           |
| <b>Total Asset-Backed Securities</b> .....           | <b>593</b>                   | <b>–</b>                          | <b>593</b>                          | <b>586</b>                   |
| Of which:  |                              |                                   |                                     |                              |
| – loans and advances to customers <sup>6</sup> ..... | 445                          | –                                 | 445                                 | 445                          |
| – available-for-sale portfolio .....                 | 149                          | –                                 | 149                                 | 141                          |

|  | 31.12.2011                   |                                   |                                     |                              |
|--|------------------------------|-----------------------------------|-------------------------------------|------------------------------|
| (in millions of euros)                               | Gross principal <sup>2</sup> | CDS gross protection <sup>3</sup> | Net Principal exposure <sup>4</sup> | Carrying amount <sup>5</sup> |
| – High grade <sup>1</sup> .....                      | 701                          | –                                 | 701                                 | 683                          |
| – Rated C to A .....                                 | 27                           | –                                 | 27                                  | 21                           |
| – Not publicly rated .....                           | 9                            | –                                 | 9                                   | 9                            |
| <b>Total Asset-Backed Securities</b> .....           | <b>737</b>                   | <b>–</b>                          | <b>737</b>                          | <b>713</b>                   |
| Of which:  |                              |                                   |                                     |                              |
| – loans and advances to customers <sup>6</sup> ..... | 530                          | –                                 | 530                                 | 530                          |
| – available-for-sale portfolio .....                 | 207                          | –                                 | 207                                 | 183                          |

1 High grade assets rated AA or AAA.

2 The gross principal is the redemption amount on maturity or, in the case of an amortising instrument, the sum of the future redemption amounts through the residual life of the security.

3 A CDS is a credit default swap. CDS gross protection is the gross principal of the underlying instruments that is protected by CDSs.

4 Net principal exposure is the gross principal amount of assets that are not protected by CDSs. It includes assets that benefit from mono-line protection except where this protection is purchased with a CDS.

5 Carrying amount of the net principal exposure.

6 ABS held by HSBC Trinkhaus Gesellschaft für Kapitalmarktinvestments oHG. HSBC Trinkhaus Gesellschaft für Kapitalmarktinvestments oHG is a partnership created in 2010 and 90 per cent held by HSBC France group, whose object is to invest in securitisation transactions structured by the HSBC Group and which holds mainly assets of German transferors.

|  | 31.12.2012   |  |                             | 31.12.2011   |  |                             |
|--|--|--|-----------------------------|--|--|-----------------------------|
| (in millions of euros)                     | Gross fair value movements other comprehensive income <sup>2</sup> | Reclassified from equity on impairment, disposal or payment <sup>3</sup> | AFS Impairment <sup>4</sup> | Gross fair value movements other comprehensive income <sup>2</sup> | Reclassified from equity on impairment, disposal or payment <sup>3</sup> | AFS Impairment <sup>4</sup> |
| – High grade <sup>1</sup> .....            | 2  | (1)  | –                           | 3  | –  | –                           |
| – Rated C to A .....                       | 2  | 2  | –                           | (3)  | 4  | –                           |
| – Not publicly rated .....                 | (2)  | –  | –                           | (2)  | –  | –                           |
| <b>Total Asset Backed Securities</b> ..... | <b>2</b>   | <b>1</b>   | <b>–</b>                    | <b>(2)</b>   | <b>4</b>   | <b>–</b>                    |

1 High grade assets rated AA or AAA.

2 Fair value gains and losses on the net principal exposure recognised in equity at the end of the year as a result of the changes in fair value of available for sale assets.

3 Reclassification with respect to AFS assets, includes impairment losses recognised at the end of the year as a result of sale, disposal, accretion or payment.

4 Impairment losses recognised in the income statement with respect to the net principal amount (see footnote 4 above) of available-for-sale.

**Consolidated financial statements** (continued)**33 Risk management** (continued)**Risk cover and regulatory ratios***Large exposures*

The HSBC France group complies with the French *Autorité de contrôle prudentiel*'s rules, which require the following:

- exposure to a group of clients deemed to have the same beneficial owner is limited to 20 per cent of net capital if the beneficial owner is investment grade and 15 per cent if non-investment grade;
- the aggregate of individual exposures exceeding 10 per cent of net capital is limited to eight times net capital. 23 groups had individual exposures exceeding 10 per cent of net capital at 31 December 2012.

*Loan loss provisions*

At 31 December 2012, loan impairment represented 46.2 per cent of the HSBC France group's total doubtful and non-performing exposure.

*Liquidity ratio*

The HSBC France group's regulatory ratios reflect its good liquidity risk cover. The regulatory liquidity ratio, which measures the potential one-month liquidity gap, averaged 130.9 per cent in 2012 on an individual basis.

*Basel II international solvency ratio*

The HSBC France group's Basel II international solvency ratio was 12.6 per cent at 31 December 2012, compared with a minimum requirement of 8 per cent. The group's Tier 1 capital ratio was 12.6 per cent, compared with a minimum requirement of 4 per cent.

Under the Basel II definitions, total HSBC France group capital amounted to EUR 4,128 million at 31 December 2012, of which EUR 4,133 million was Tier 1 capital.

The corresponding risk-weighted assets broke down as follows:

| (in billions of euros)       | <b>31.12.2012</b> | 31.12.2011  |
|------------------------------|-------------------|-------------|
| Credit risks .....           | <b>21.8</b>       | 23.7        |
| Market risks .....           | <b>5.1</b>        | 9.5         |
| Operational risks .....      | <b>3.6</b>        | 3.7         |
| Additional requirement ..... | <b>2.2</b>        | –           |
| <b>Total</b> .....           | <b>32.7</b>       | <b>36.9</b> |

Commentaries related to the risk-weighted assets are disclosed in the Risk management section on page 87.

**Special Purpose Entities**

The group enters into certain transactions with customers in the ordinary course of business which involve the establishment of Special Purpose Entities (SPEs), some of which have been included in the group's consolidated balance sheet.

Transactions involving use of SPEs are authorised centrally upon establishment to ensure appropriate purpose and governance. The activities of SPEs administered by the group are closely monitored by Senior Management. The use of SPEs is not a significant part of the group's activities and the group is not reliant on the use of SPEs for any major part of its business operations or profitability.

*Vehicles sponsored by the group*

The group re-assesses the required consolidation accounting tests whenever there is a change in the substance of a relationship between the group and an SPE, for example, when there is a change in the group's involvement or in the governing rules, in the contractual arrangements or in the capital structure of the SPE.

*Money market funds*

The group has established and manages a number of money market funds which provide customers with tailored investment opportunities. These funds have narrow and well-defined objectives and typically the group does not aim to have any holdings in the SPEs large enough to represent the majority of the risks and rewards of ownership.

### 33 Risk management (continued)

Since July 2007, French dynamic money market funds have experienced high redemption requests caused by the investors' lack of confidence in funds which could contain exposure to subprime assets. From the third quarter of 2007, the group acquired underlying assets and shares in two of its dynamic money market funds, HSBC EOTOP and HSBC Duoblig; no additional shares were acquired by the group in 2010 and 2011. As a result of continued redemptions by unit holders, the group's holding in the two funds increased to a level where it obtained the majority of the risks and rewards of ownership during the first quarter of 2008. These two funds were consolidated by HSBC France since 31 December 2008, and have now been liquidated (HSBC Duoblig in 2012 and HSBC EOTOP in 2010). The market value of the assets transferred to HSBC France was EUR 178 million at the end of 2012.

#### Asset finance transactions

HSBC France's Asset and Structured Finance (ASF) business specialises in leasing and arranging finance for aircraft and other physical assets as well as financial assets, which is customary to ring-fence through the use of SPEs, and in structured loans and deposits where SPEs introduce cost efficiencies. HSBC France consolidates these SPEs where the substance of the relationship indicates that HSBC France controls the SPE.

### 34 Contingent liabilities and contractual commitments

#### a Contingent liabilities and commitments

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Contract amounts</b>   |                   |                   |
| <i>Guarantees and other contingent liabilities</i>                            |                   |                   |
| Guarantees .....  | 4,509             | 5,996             |
| Other contingent liabilities .....  | –                 | 35                |
|   | <u>4,509</u>      | <u>6,031</u>      |
| <br><i>Commitments</i>  |                   |                   |
| Documentary credits and short-term trade-related transactions .....           | 843               | 398               |
| Undrawn formal standby facilities, credit lines and other commitments to lend |                   |                   |
| – 1 year and under .....  | 3,109             | 7,217             |
| – over 1 year .....   | 14,133            | 13,428            |
|   | <u>18,085</u>     | <u>21,043</u>     |

The above table discloses the nominal principal amounts of third-party off-balance sheet transactions. Nominal principal amounts represent the amounts at risk should contracts be fully drawn upon and clients default.

The total of the nominal principal amounts is not representative of future liquidity requirements.

#### b Guarantees

The group provides guarantees and similar undertakings on behalf of both third-party customers and other entities within the group. These guarantees are generally provided in the normal course of the group's banking business. The principal types of guarantees provided, and the maximum potential amount of future payments which the group could be required to make at 31 December were as follows:

| (in millions of euros)                        | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Guarantee type</b>                         |                   |                   |
| Financial guarantees <sup>1</sup> .....       | 645               | 941               |
| Credit-related substitutes <sup>2</sup> ..... | 1,954             | 1,610             |
| Other guarantees <sup>3</sup> .....           | 1,910             | 3,480             |
| <b>Total</b> .....                            | <u>4,509</u>      | <u>6,031</u>      |

<sup>1</sup> Financial guarantees include undertakings to fulfil the obligations of customers or group entities, should the obligated party fail to do so. The inter-company financial guarantees include a specific guarantee related to debt issued by the group for the benefit of other entities of the group and with respect to regulatory requirements. Financial guarantees also include stand-by letters of credit, which are financial guarantees given irrevocable obligations on the part of HSBC France to pay a third party when a customer fails to meet a commitment.

<sup>2</sup> Credit-related substitutes include performance bonds and stand-by letters of credit related to particular transactions which are undertakings by which the requirement to make payment under the guarantee depends on the outcome of a future event which is unconnected to the creditworthiness of the customer.

<sup>3</sup> Other guarantees include bid bonds and other transaction-related guarantees which are undertakings by which the requirement to make payment under the guarantee depends on the outcome of a future event which is unconnected to the creditworthiness of the customer.

**Consolidated financial statements** (continued)**34 Contingent liabilities and contractual commitments** (continued)

The amounts disclosed in the above table reflect the group's maximum exposure under a large number of individual guarantee undertakings. The risks and exposures arising from guarantees are captured and managed in accordance with the group's overall credit risk management policies and procedures.

The majority of the above guarantees have a term of more than one year. Those guarantees are subject to the group's annual credit review process.

When the group gives a guarantee on behalf of a customer, it retains the right to recover from that customer amounts paid under the guarantee.

**Provisions with respect to the group's obligations under outstanding guarantees**

|                                    |                   |            |
|------------------------------------|-------------------|------------|
| (in millions of euros)             | <b>31.12.2012</b> | 31.12.2011 |
| Acceptances and endorsements ..... | –                 | –          |
| Other items .....                  | <b>2</b>          | 2          |

**35 Lease commitments****Finance lease commitments**

| (in millions of euros)                                | <b>31.12.2012</b>                            |                             |                          | 31.12.2011                                   |                             |                          |
|---|--|-----------------------------|--------------------------|--|-----------------------------|--------------------------|
|   | <i>Total future<br/>minimum<br/>payments</i> | <i>Interest<br/>charges</i> | <i>Present<br/>value</i> | <i>Total future<br/>minimum<br/>payments</i> | <i>Interest<br/>charges</i> | <i>Present<br/>value</i> |
| Lease commitments:                                    |  |                             |                          |  |                             |                          |
| – no later than one year .....                        | –  | –                           | –                        | –  | –                           | –                        |
| – later than one year<br>and no later than five years | –  | –                           | –                        | –  | –                           | –                        |
| – later than five years .....                         | –  | –                           | –                        | –  | –                           | –                        |
| <b>Total</b> .....                                    | <b>–</b>                                     | <b>–</b>                    | <b>–</b>                 | <b>–</b>                                     | <b>–</b>                    | <b>–</b>                 |

There were no future minimum sublease payments expected to be received under non-cancellable subleases.

**Finance lease receivables**

| (in millions of euros)                                    | <b>31.12.2012</b>                            |                             |                          | 31.12.2011                                   |                             |                          |
|---|--|-----------------------------|--------------------------|--|-----------------------------|--------------------------|
|   | <i>Total future<br/>minimum<br/>payments</i> | <i>Interest<br/>charges</i> | <i>Present<br/>value</i> | <i>Total future<br/>minimum<br/>payments</i> | <i>Interest<br/>charges</i> | <i>Present<br/>value</i> |
| Lease receivables:  |  |                             |                          |  |                             |                          |
| – no later than one year .....                            | <b>525</b>                                   | <b>(58)</b>                 | <b>467</b>               | 473  | (61)                        | 412                      |
| – later than one year and<br>no later than five years ... | <b>1,655</b>                                 | <b>(224)</b>                | <b>1,431</b>             | 1,717  | (220)                       | 1,497                    |
| – later than five years .....                             | <b>967</b>                                   | <b>(219)</b>                | <b>748</b>               | 1,200  | (227)                       | 973                      |
| <b>Total</b> .....  | <b>3,147</b>                                 | <b>(501)</b>                | <b>2,646</b>             | <b>3,390</b>                                 | <b>(508)</b>                | <b>2,882</b>             |

At 31 December 2012, unguaranteed residual values of EUR 130 million (2011: EUR 140 million) had been accrued, and there was no accumulated allowance for uncollectible minimum lease payments receivable.

**36 Litigation**

Various regulators and competition and enforcement authorities around the world including in the United Kingdom (UK), the United States of America (US), Canada, the European Union, Switzerland and Asia, are conducting investigations and reviews related to certain past submissions made by panel banks and the processes for making submissions in connection with the setting of London interbank offered rates ("Libor"), European interbank offered rates ("Euribor") and other benchmark interest and foreign exchange rates. Several of these panel banks have reached settlements with various regulatory authorities.

### 36 Litigation (continued)

As a member of such panel for “Euribor”, HSBC France has been the subject of regulatory demands for information and is cooperating with those investigations and reviews. Based on the facts currently known, there is a high degree of uncertainty as to the resolution of these regulatory investigations and reviews, including the timing. The potential impact and size of any fines or penalties that could be imposed on HSBC France cannot be measured reliably.

As at 31 December 2012, there were no other litigation or arbitration proceedings likely to have a material impact on HSBC France’s financial position, its activities or results.

### 37 Related party transactions

The ultimate parent company of the group is HSBC Holdings plc, which is incorporated in the UK.

All transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

#### a Transactions, arrangements and agreements involving Directors and others

The table below sets out transactions which fall under IAS 24 “Related Party Disclosures” between HSBC France and the Key Management Personnel of HSBC France, and their connected persons or controlled companies.

| (in thousands of euros) | 31.12.2012           |                                       |  | 31.12.2011           |                                       |  |
|-------------------------|----------------------|---------------------------------------|--|----------------------|---------------------------------------|--|
|                         | Number<br>of persons | Highest<br>balance during<br>the year | Balance at<br>31 December <sup>1</sup> | Number<br>of persons | Highest<br>balance during<br>the year | Balance at<br>31 December <sup>1</sup> |
| Loans . . . . .         | 3                    | 1,112                                 | 979                                    | 4                    | 9,020                                 | 8,738                                  |
| Credit cards . . . . .  | 3                    | 41                                    | 9                                      | 4                    | 73                                    | 32                                     |
| Guarantees . . . . .    | 3                    | –                                     | –                                      | 4                    | –                                     | –                                      |

<sup>1</sup> The highest balance during the year and the balance at 31 December are considered to be the most significant information to show the transactions during the year.

Compensation to the Key Management Personnel of the group under IAS 24 is disclosed as follows:

| (in thousands of euros)                | 31.12.2012   | 31.12.2011   |
|--|--------------|--------------|
| Short-term employee benefits . . . . . | 135          | 170          |
| Post-employment benefits . . . . .     | 148          | 189          |
| Long-term benefits . . . . .           | –            | –            |
| Termination fees . . . . .             | 140          | 145          |
| Share-based payment . . . . .          | 1,755        | 3,135        |
|  | <b>2,178</b> | <b>3,639</b> |

Directors and other Key Management Personnel shareholdings and options:

|  | 31.12.2012             | 31.12.2011 <sup>1</sup> |
|--|------------------------|-------------------------|
| Number of share options from equity participation plans held by Directors and other key management personnel (and their connected persons) . . . . . | 441,799                | 1,181,958               |
| Number of shares held by Directors and other key management personnel (and their connected persons) . . . . .  | 1,054,028 <sup>2</sup> | 2,260,977 <sup>2</sup>  |

<sup>1</sup> The number of Directors was three persons at 31 December 2012 and four persons at 31 December 2011.

<sup>2</sup> The HSBC shares held through the mutual fund invested in HSBC shares and forming part of the group employee share ownership plan are not included.

The Annual Report and Accounts also includes a detailed description of Directors’ remuneration (see pages 26 to 38).

**Consolidated financial statements** (continued)**37 Related party transactions** (continued)**b Transactions with other related parties**

Transactions with other related parties of the Group

There is no significant amount due to joint ventures and associates.

Transactions detailed below include amounts due to/from HSBC France and fellow subsidiaries of HSBC Holdings plc.

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Assets</b>   |                   |                   |
| Trading assets.....   | 4,920             | 5,521             |
| Derivatives.....  | 24,562            | 24,784            |
| Loans and advances to banks.....                                | 11,414            | 5,714             |
| Loans and advances to customers.....                            | 87                | 69                |
| Financial investments.....                                      | 170               | 170               |
| Other assets <sup>1</sup> .....                                 | 175               | 160               |
| Prepayments and accrued income.....                             | 99                | 125               |
| Financial assets designated at fair value.....                  | 5                 | 4                 |
| <b>Liabilities</b>  |                   |                   |
| Deposits by banks.....  | 16,233            | 11,913            |
| Customer accounts.....  | 220               | 159               |
| Trading liabilities.....  | 1,586             | 960               |
| Derivatives.....  | 27,396            | 29,365            |
| Other liabilities.....  | 134               | 26                |
| Accruals and deferred income.....                               | 72                | 54                |
| Subordinated liabilities.....                                   | 150               | 150               |
| <b>Guarantees</b>   |                   |                   |
| Financial guarantees.....                                       | 12                | 67                |
| Credit-related substitutes.....                                 | 40                | 45                |
| Other guarantees.....   | 301               | 438               |
|   | <u>353</u>        | <u>550</u>        |
| <b>Income Statement</b>   |                   |                   |
| Interest income <sup>1</sup> .....                              | 106               | 145               |
| Interest expense <sup>1</sup> .....                             | 22                | 124               |
| Fee income.....   | 145               | 134               |
| Fee expense.....  | 82                | 88                |
| Gains less losses from financial investments <sup>2</sup> ..... | –                 | 13                |
| Other operating income.....                                     | –                 | –                 |
| Dividend income.....  | –                 | –                 |
| General and administrative expenses.....                        | 60                | 30                |

<sup>1</sup> Including interests on trading assets and trading liabilities for EUR 10 million in 2012 (2011: EUR 26 million).

<sup>2</sup> Gains/(Losses) on sale of Sinopia Asset Management (Asia Pacific) Ltd for EUR 12 million, Sinopia Asset Management (UK) Ltd for EUR 3 million and LGI EUR -2 million in 2011.



### 38 Audit fees

#### Auditors' fees paid in 2012 and 2011 within the HSBC France group

| (in thousands of euros<br>excluding VAT)  | KPMG         |       |             |      | BDO France –<br>Léger & Associés |      |            |      | Others     |      |             |      |
|---|--------------|-------|-------------|------|----------------------------------|------|------------|------|------------|------|-------------|------|
|   | Amount       |       | %           |      | Amount                           |      | %          |      | Amount     |      | %           |      |
|   | 2012         | 2011  | 2012        | 2011 | 2012                             | 2011 | 2012       | 2011 | 2012       | 2011 | 2012        | 2011 |
| <b>Audit</b>  |              |       |             |      |                                  |      |            |      |            |      |             |      |
| Statutory audit, certification,<br>examination of Parent company<br>and consolidated accounts . . . . . | <b>1,322</b> | 1,398 | <b>68%</b>  | 66%  | <b>393</b>                       | 446  | <b>95%</b> | 97%  | <b>148</b> | 212  | <b>100%</b> | 100% |
| – issuer . . . . .  | <b>948</b>   | 948   | –           | –    | <b>338</b>                       | 338  | –          | –    | –          | –    | –           | –    |
| – fully-consolidated subsidiaries . .   | <b>374</b>   | 450   | –           | –    | <b>55</b>                        | 108  | –          | –    | <b>148</b> | 212  | –           | –    |
| Related assignments . . . . .   | <b>624</b>   | 727   | <b>32%</b>  | 34%  | <b>21</b>                        | 12   | –          | 3%   | –          | –    | –           | –    |
| – issuer . . . . .  | <b>507</b>   | 666   | –           | –    | <b>15</b>                        | 6    | –          | –    | –          | –    | –           | –    |
| – fully-consolidated subsidiaries . .   | <b>117</b>   | 61    | –           | –    | <b>6</b>                         | 6    | –          | –    | –          | –    | –           | –    |
| Sub-total . . . . .   | <b>1,946</b> | 2,125 | <b>100%</b> | 100% | <b>414</b>                       | 458  | <b>95%</b> | 100% | <b>148</b> | 212  | <b>100%</b> | 100% |
| <b>Other services</b>   |              |       |             |      |                                  |      |            |      |            |      |             |      |
| Legal, tax, social . . . . .  | –            | –     | –           | –    | –                                | –    | –          | –    | –          | –    | –           | –    |
| Other (if > 10 per cent of audit<br>fees) . . . . .   | –            | –     | –           | –    | –                                | –    | –          | –    | –          | –    | –           | –    |
| Sub-total . . . . .   | –            | –     | –           | –    | –                                | –    | –          | –    | –          | –    | –           | –    |
| <b>Total . . . . .</b>  | <b>1,946</b> | 2,125 | <b>100%</b> | 100% | <b>414</b>                       | 458  | <b>95%</b> | 100% | <b>148</b> | 212  | <b>100%</b> | 100% |

### 39 Events after the balance sheet date

There have been no material events after the balance sheet date which would require disclosure or adjustment to the 31 December 2012 financial statements.

## Consolidated financial statements (continued)

### Statutory Auditors' report on the consolidated financial statements

*This is a free translation into English of the Statutory Auditors' report on the consolidated financial statements issued in French and it is provided solely for the convenience of English-speaking users. The Statutory Auditors' report includes information specifically required by French law in such reports, whether modified or not. This information is presented below the audit opinion on the consolidated financial statements and includes an explanatory paragraph discussing the Auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the consolidated financial statements taken as a whole and not to provide separate assurance on individual account balances, transactions, or disclosures. This report also includes information relating to the specific verification of information given in the Group's management report. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

Year ended 31 December 2012

To the shareholders,

In compliance with the assignment entrusted to us by your Annual General Meeting, we hereby report to you, for the year ended 31 December 2012, on:

- the audit of the accompanying annual financial statements of HSBC France ;
- the justification of our assessments;
- the specific verifications and information required by law.

These consolidated financial statements have been approved by the Board of Directors. Our role is to express an opinion on these consolidated financial statements based on our audit.

#### I - Opinion on the consolidated financial statements

We conducted our audit in accordance with professional standards applicable in France; those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit involves performing procedures, using sampling techniques or other methods of selection, to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made, as well as the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

In our opinion, the consolidated financial statements give a true and fair view of the assets and liabilities and of the financial position of the Group as at 31 December 2012 and of the results of its operations for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

#### II - Justification of our assessments

In accordance with the requirements of article L. 823-9 of the French Commercial Code (*Code de Commerce*) relating to the justification of our assessments, we bring to your attention the following matters:

- your company accounts for depreciations to cover the credit and counterparty risks inherent to its activities (Note 2 g to the consolidated financial statements). We have reviewed the control procedures relating to credit and counterparty risk monitoring, the assessment of risks of non-recoverability and the calculation of the corresponding individual and collective impairment;
- your company holds positions in securities and financial instruments (Notes 1 a, 2 d, 2 j, 2 l and 28 to the consolidated financial statements). We have examined the control procedures for the accounting classification of these positions and for determining the parameters used to value them. We have verified the appropriateness of the accounting policies selected by your company and have satisfied ourselves that they are applied correctly;
- your company assessed the impact of changes in its own credit risk with respect to the valuation of issuances measured at fair value through profit and loss (Note 28 to the consolidated financial statements). We have assessed the appropriateness of the parameters used for this purpose;
- your company recognizes provisions to cover risks and litigations related to its activity (Notes 2 w and 36 to the consolidated financial statements). We have examined the methodology used to measure these provisions, as well as the main assumptions applied.

These assessments were made as part of our audit of the consolidated financial statements taken as a whole, and therefore contributed to the opinion we formed which is expressed in the first part of this report.

### **III - Specific verification**

As required by law we have also verified, in accordance with professional standards applicable in France, the information presented in the group's management report.

We have no matters to report as to its fair presentation and its consistency with the consolidated financial statements.

Paris-La Défense and Paris, on 12 April 2013

KPMG Audit FS II  
Pascal Brouard  
*Partner*

BDO France – Léger & Associés  
Michel Léger  
*Partner*

## Parent company financial statements

### Balance sheets 2012-2011

#### ASSETS

(in thousands of euros)

|  | Notes | 31.12.2012         | 31.12.2011         |
|--|-------|--------------------|--------------------|
| Cash and amounts due from central banks and post office banks        |       | <b>960,421</b>     | 800,886            |
| Treasury bills and money-market instruments                          | 4     | <b>27,239,637</b>  | 23,884,006         |
| Loans and advances to banks  | 2     | <b>41,924,803</b>  | 48,598,101         |
| Loans and advances to customers                                      | 3     | <b>52,806,571</b>  | 62,173,195         |
| Bonds and other fixed income securities                              | 4     | <b>7,494,934</b>   | 8,846,010          |
| Equities and other variable income securities                        | 4     | <b>5,527</b>       | 163,967            |
| Investments in subsidiaries and equity securities held for long-term | 5     | <b>341,387</b>     | 334,322            |
| Interests in affiliated parties                                      | 5     | <b>1,142,123</b>   | 1,569,026          |
| Finance leases   | 7     | <b>77,383</b>      | –                  |
| Intangible fixed assets  | 6     | <b>245,016</b>     | 245,292            |
| Tangible fixed assets  | 7     | <b>243,583</b>     | 214,205            |
| Other assets   | 9     | <b>28,551,437</b>  | 29,336,900         |
| Prepayments and accrued income                                       | 10    | <b>171,867,881</b> | 140,863,450        |
| <b>TOTAL ASSETS</b>  |       | <b>332,900,703</b> | <b>317,029,360</b> |
| <b>Off-balance sheet items</b>                                       |       |                    |                    |
| Financing commitments received                                       | 21    | <b>18,763,982</b>  | 21,792,816         |
| Guarantees and endorsements  | 21    | <b>4,585,883</b>   | 6,154,402          |
| Securities commitments (other commitments received)                  |       | <b>30,572,301</b>  | 1,257,264          |

#### LIABILITIES

| (in thousands of euros)                          | Notes | 31.12.2012           |                                  | 31.12.2011          |
|--|-------|----------------------|----------------------------------|---------------------|
|  |       | Before appropriation | After appropriation <sup>1</sup> | After appropriation |
| Due to credit institutions                       | 11    | <b>41,161,835</b>    | <b>41,161,835</b>                | 46,421,709          |
| Customer accounts                                | 12    | <b>52,238,221</b>    | <b>52,238,221</b>                | 56,575,935          |
| Debt securities                                  | 13    | <b>15,290,578</b>    | <b>15,290,578</b>                | 17,381,034          |
| Other liabilities                                | 15    | <b>46,089,164</b>    | <b>46,089,164</b>                | 49,796,974          |
| Accruals and deferred income                     | 16    | <b>172,803,315</b>   | <b>172,803,315</b>               | 142,015,101         |
| Provisions for liabilities and charges           | 14    | <b>322,405</b>       | <b>322,405</b>                   | 437,291             |
| Subordinated liabilities                         | 17    | <b>181,362</b>       | <b>181,362</b>                   | 181,554             |
| Share capital                                    | 18    | <b>337,189</b>       | <b>337,189</b>                   | 337,189             |
| Additional paid-in capital                       |       | <b>16,139</b>        | <b>16,139</b>                    | 16,139              |
| Reserves   |       | <b>1,047,616</b>     | <b>1,047,616</b>                 | 1,047,843           |
| Special tax-allowable reserves                   |       | <b>26,221</b>        | <b>26,221</b>                    | 33,124              |
| Retained earnings                                |       | <b>2,785,468</b>     | <b>3,386,658</b>                 | 2,785,467           |
| <b>Net profit of the year</b>                    |       | <b>601,190</b>       |                                  |                     |
| Interim dividend                                 |       |                      |                                  |                     |
| <b>TOTAL LIABILITIES</b>                         |       | <b>332,900,703</b>   | <b>332,900,703</b>               | <b>317,029,360</b>  |
| <b>Off-balance sheet items</b>                   |       |                      |                                  |                     |
| Financing commitments given                      | 21    | <b>360,066</b>       | <b>360,066</b>                   | 6,510,185           |
| Guarantees and endorsements                      | 21    | <b>7,818,611</b>     | <b>7,818,611</b>                 | 6,750,678           |
| Securities commitments (other commitments given) |       | <b>26,449,398</b>    | <b>26,449,398</b>                | 2,452,615           |

<sup>1</sup> Proposed appropriation.

## Profit and loss accounts 2012-2011

| <i>(in thousands of euros)</i>                            | <i>Notes</i> | <b>31.12.2012</b>  | 31.12.2011  |
|---|--------------|--------------------|-------------|
| <b>Income/(Expenses)</b>                                  |              |                    |             |
| Interest and similar income                               | 23           | <b>1,474,200</b>   | 2,340,916   |
| Interest and similar expenses                             | 23           | <b>(740,187)</b>   | (1,605,561) |
| Finance leases income                                     |              | <b>4,520</b>       | –           |
| Finance leases expenses                                   |              | <b>(4,669)</b>     | –           |
| Income from equities and other variable instruments       | 24           | <b>142,899</b>     | 188,553     |
| Commissions received                                      | 25           | <b>794,743</b>     | 808,119     |
| Commissions paid  | 25           | <b>(197,364)</b>   | (201,254)   |
| Dealing profits   | 26           | <b>539,620</b>     | 9,062       |
| Gains or losses on available-for-sale securities          | 27           | <b>299,222</b>     | (67,430)    |
| Other banking operating income                            |              | <b>13,116</b>      | 37,175      |
| Other banking operating expenses                          |              | <b>(11,574)</b>    | (15,005)    |
| <b>Net banking operating income</b>                       |              | <b>2,314,526</b>   | 1,494,575   |
| General operating expenses                                | 28           | <b>(1,424,504)</b> | (1,421,175) |
| Depreciation, amortisation and impairment of fixed assets |              | <b>(51,518)</b>    | (53,598)    |
| <b>Gross operating income</b>                             |              | <b>838,503</b>     | 19,802      |
| Cost of risk  | 8            | <b>(51,545)</b>    | (111,997)   |
| <b>Net operating income</b>                               |              | <b>786,958</b>     | (92,195)    |
| Gains or losses on disposals of long term investments     | 29           | <b>15,092</b>      | (36,454)    |
| <b>Profit before tax</b>                                  |              | <b>802,050</b>     | (128,649)   |
| Exceptional items   |              | <b>(94)</b>        | –           |
| Income tax  | 30           | <b>(207,670)</b>   | 148,039     |
| Gains and losses from regulated provisions                |              | <b>6,904</b>       | 7,114       |
| <b>Net income</b>   |              | <b>601,190</b>     | 26,504      |

## Statement of reported net profit and movements in shareholders' funds and the reserve for general banking risks

*(Recommendation of the Stock Exchange Commission – Bulletin no. 79 of February 1976)*

| <i>(in thousands of euros)</i>   | <b>31.12.2012</b> | 31.12.2011  |
|--|-------------------|-------------|
| <b>Net profit for the year</b>   |                   |             |
| – total  | <b>601,190.0</b>  | 26,504.4    |
| – per share <i>(in euros)</i> <sup>1,2</sup>   | <b>8.91</b>       | 0.39        |
| <b>Movements in shareholders' funds and the reserve for general banking risks</b><br>(after appropriation of 2011 net profit and proposed appropriation for 2012 net profit) |                   |             |
| – change in revaluation difference   | <b>(227.3)</b>    | (27.2)      |
| – transfer to reserves and change in retained earnings   | <b>–</b>          | (95,890.8)  |
| – change in revaluation reserve and special tax-allowable reserves   | <b>(6,902.6)</b>  | (7,126.0)   |
| <b>Change in shareholders' funds</b>   | <b>(7,129.9)</b>  | (103,044.0) |
| – per share <i>(in euros)</i> <sup>1,2</sup>   | <b>(0.1)</b>      | (1.5)       |
| <b>Proposed dividend</b>   |                   |             |
| – total  | <b>240,079.0</b>  | 118,016.2   |
| – per share <i>(in euros)</i> <sup>1,2</sup>   | <b>3.56</b>       | 1.75        |

<sup>1</sup> Number of shares outstanding at year end (excluding own shares held): 67,437,827 in 2012, 67,437,827 in 2011 and 67,437,820 in 2010.

<sup>2</sup> Based on the weighted average number of shares outstanding (excluding own shares held), dividend per share amounted to EUR 3.56 in 2012 (67,437,827 shares) and EUR 1.75 in 2011 (67,437,827 shares).

## Parent company financial statements (continued)

### Appropriation of net profit

| <i>(in millions of euros)</i>                   | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| <b>Results available for distribution</b>       |                   |            |
| – retained earnings .....                       | <b>2,785,467</b>  | 2,876,979  |
| – transition adjustment in respect of EIR ..... | <b>–</b>          | –          |
| <b>Subtotal</b> .....                           | <b>2,785,467</b>  | 2,876,979  |
| Net profit for the year .....                   | <b>601,190</b>    | 26,504     |
| <b>TOTAL (A)</b> .....                          | <b>3,386,657</b>  | 2,903,483  |
| <b>Appropriation of income</b>                  |                   |            |
| – dividends .....                               | <b>240,079</b>    | 118,016    |
| – legal reserve .....                           | <b>–</b>          | –          |
| – free reserve .....                            | <b>–</b>          | –          |
| <b>TOTAL (B)</b> .....                          | <b>240,079</b>    | 118,016    |
| <b>Retained earnings (A - B)</b> .....          | <b>3,146,578</b>  | 2,785,467  |

### Information on supplier payable amounts schedule

*(Articles L. 441-6-1 and D. 441-4 of the French Commercial Code)*

At 31 December 2012, amounts payable to suppliers of HSBC France were EUR 104.4 million, of which 49.5 per cent with a due date less than 30 days.

At 31 December 2011, amounts payable to suppliers of HSBC France were EUR 69 million, of which 73 per cent with a due date less than 45 days.

Except for specific agreements with suppliers, payments are made within 45 days of invoice date.

### Five-year highlights

*(Articles R. 225-81 and R. 225-102 of the French Commercial Code)*

| <i>(in thousands of euros)</i>  | <b>2012</b>       | 2011       | 2010       | 2009       | 2008       |
|---|-------------------|------------|------------|------------|------------|
| <b>Share capital at year end</b>  |                   |            |            |            |            |
| Called up share capital .....   | <b>337,189</b>    | 337,189    | 337,189    | 337,189    | 337,189    |
| Number of issued shares .....   | <b>67,437,827</b> | 67,437,827 | 67,347,820 | 67,437,820 | 67,437,820 |
| Nominal value of shares in euros .....  | <b>5</b>          | 5          | 5          | 5          | 5          |
| <b>Results of operations for the year</b>   |                   |            |            |            |            |
| Sales .....   | <b>3,263,800</b>  | 3,316,395  | 3,402,924  | 4,304,312  | 7,002,038  |
| Profit before tax, depreciation and provisions .....                              | <b>799,099</b>    | 146,388    | 873,707    | 949,898    | 2,415,956  |
| Profit after tax, depreciation and provisions .....                               | <b>601,190</b>    | 26,504     | 819,731    | 550,167    | 1,985,603  |
| <b>Per share data</b> (in euros)  |                   |            |            |            |            |
| Profit after tax, but before depreciation<br>and provisions .....                 | <b>8.6</b>        | 4.4        | 12.2       | 11.9       | 37.7       |
| Profit after tax, depreciation and provisions .....                               | <b>8.9</b>        | 0.4        | 9.2        | 8.2        | 29.4       |
| Dividend paid per ordinary share,<br>eligible as of 1 January .....               | <b>3.56</b>       | 1.75       | 10.67      | 9.94       | –          |
| <b>Employees</b> (France)   |                   |            |            |            |            |
| Number of employees <sup>1</sup> .....  | <b>9,424</b>      | 9,860      | 9,694      | 9,731      | 10,218     |
| Average number of employees<br>(excluding employees available) <sup>2</sup> ..... | <b>9,645</b>      | 9,748      | 9,615      | 9,872      | 8,940      |
| Salaries and wages .....  | <b>559,888</b>    | 577,016    | 535,533    | 564,619    | 459,067    |
| Employee benefits .....   | <b>289,322</b>    | 244,808    | 247,908    | 252,768    | 231,279    |
| Payroll and other taxes .....   | <b>62,784</b>     | 72,650     | 96,763     | 63,502     | 65,481     |
| Incentive schemes and/or employee<br>profit-sharing scheme <sup>3</sup> .....     | <b>–</b>          | 29,560     | 39,500     | 17,695     | 27,610     |

<sup>1</sup> Banking status employees, registered as at 31 December of each year.

<sup>2</sup> Of which 6,402 executives and 3,243 non-executives in 2012; of which 6,116 executives and 3,499 non-executives in 2011; of which 6,067 executives and 3,805 non-executives in 2010; of which 5,462 executives and 3,478 non-executives in 2009; of which 4,894 executives and 3,209 non-executives in 2008.

<sup>3</sup> Based on previous year's profits.

## List of equity shares and debt securities held at 31 December 2012 (excluding trading securities)

Held-on maturity, available-for-sale and portfolio activity securities

(in thousands of euros)

|   |                  |
|---|------------------|
| <b>A – Held-to-maturity securities</b>  | <b>184,413</b>   |
| <b>Debt securities</b>  | <b>184,413</b>   |
| Treasury bills and other eligible bills   | –                |
| Other public sector securities  | –                |
| Money market instruments  | –                |
| Negotiable certificates of deposit  | –                |
| Negotiable medium-term notes  | –                |
| Bonds and similar assets  | 184,224          |
| Accrued interest  | 189              |
| <b>B – Available-for-sale and portfolio activity securities</b>                     | <b>7,507,560</b> |
| <b>Debt securities</b>  | <b>7,502,033</b> |
| Treasury bills and other eligible bills   | 935,631          |
| Other public sector securities  | 4,412,071        |
| Money market instruments  | –                |
| Commercial paper  | –                |
| Negotiable certificates of deposit  | 14,028           |
| Negotiable medium-term notes  | –                |
| Asset-backed securities   | 134,131          |
| Bonds and similar   | 1,939,268        |
| Negotiable medium-term notes issued by banks  | –                |
| Accrued interest  | 66,904           |
| <b>Equity shares</b>  | <b>5,527</b>     |
| Equity shares and similar   | 4,894            |
| Mutual fund units   | 633              |
| <b>TOTAL HELD-TO-MATURITY, AVAILABLE-FOR-SALE AND PORTFOLIO ACTIVITY SECURITIES</b> | <b>7,691,973</b> |

Interests in related parties, other participating interests and long-term securities

(in thousands of euros)

|   |                  |
|---|------------------|
| <b>A – Other participating interest and long-term securities</b>                                  | <b>341,179</b>   |
| Securities listed on a recognized French exchange   | 1,847            |
| Unlisted French securities  | 339,332          |
| Foreign securities listed on a recognised French exchange   | –                |
| Foreign securities listed elsewhere   | –                |
| Unlisted foreign securities   | –                |
| Accrued income  | –                |
| <b>B – Interests in related parties</b>   | <b>1,142,123</b> |
| Listed French securities  | –                |
| Unlisted French securities  | 1,124,680        |
| Listed foreign securities   | –                |
| Unlisted foreign securities   | 17,443           |
| Accrued income  | –                |
| <b>TOTAL INTERESTS IN RELATED PARTIES, OTHER PARTICIPATING INTERESTS AND LONG-TERM SECURITIES</b> | <b>1,483,302</b> |

## Parent company financial statements (continued)

### Interests in subsidiaries and related parties at 31 December 2012

In accordance with the CNC opinion (*Avis no. 2009-11*) for the application of article L. 511-45 of the French Monetary and Financial Code, HSBC France does not hold direct or indirect investments in non cooperative countries or territories.

| <i>(in thousands of currency units)</i>   | Business                         | Share capital | Reserves + retained earnings before appropriation of net profit | Ownership interest % |
|---|----------------------------------|---------------|---|----------------------|
| <b>A – Information on companies whose book value at cost exceeds 1% of HSBC France’s share capital</b>  |                                  |               |   |                      |
| <b>1 – Subsidiaries (over 50%)</b>  |                                  |               |   |                      |
| HSBC SFH (France) (ex- HSBC Covered Bonds (France) . . . . .<br>15, rue Vernet – 75008 Paris (France)   | Financial company                | EUR54,750     | EUR395  | 100.00               |
| HSBC Factoring (France) . . . . .<br>103, avenue des Champs-Élysées – 75008 Paris (France)  | Financial company                | EUR9,240      | EUR16,164   | 100.00               |
| COPARI Société de Constructions. . . . .<br>et de Participations Immobilières<br>184, avenue Frédéric & Irène Joliot-Curie<br>92000 Nanterre (France) | Real estate                      | EUR50         | EUR1,137  | 99.96                |
| Société Française et Suisse . . . . .<br>64, rue Galilée – 75008 Paris (France)   | Investment company               | EUR599        | EUR9,846  | 100.00               |
| FDM 6 . . . . .<br>39, rue Bassano – 75008 Paris (France)   | Investment and portfolio company | EUR139,052    | EUR4,735  | 100.00               |
| SAPC UFIPRO Recouvrement . . . . .<br>186, avenue Frédéric & Irène Joliot-Curie<br>92000 Nanterre (France)  | Debt collecting company          | EUR7,619      | EUR1,497  | 99.98                |
| HSBC Epargne Entreprise (France) . . . . .<br>15, rue Vernet – 75008 Paris (France)   | Financial company                | EUR16,000     | EUR22,005   | 100.00               |
| HSBC Global Asset Management (France) . . . . .<br>4, place de la Pyramide – La Défense 9<br>92800 Puteaux (France)                                   | Investment company               | EUR8,050      | EUR81,618   | 95.66                |
| HSBC Service (France) (ex- HSBC Securities (France)) . . . . .<br>103, avenue des Champs-Élysées – 75008 Paris (France)                               | Financial company                | EUR12,626     | EUR14,934   | 100.00               |
| Eurofin Capital Partners . . . . .<br>109, avenue des Champs-Élysées – 75008 Paris (France)   | Investment company               | EUR3,044      | EUR2,516  | 100.00               |
| Valeurs Mobilières Elysées (ex- Nobel) . . . . .<br>1, avenue Franklin Roosevelt – 75008 Paris (France)   | Investment company               | EUR104,000    | EUR28,720   | 100.00               |
| SAF Palissandre . . . . .<br>64, rue Galilée – 75008 Paris (France)   | Financial company                | EUR42,033     | EUR785  | 100.00               |

1 Loans, advances and guarantees granted outside the framework of normal banking business.

2 Net operating income in the case of banks.



| Book value<br>of securities held |            | Loans and<br>advances<br>granted by<br>HSBC France <sup>1</sup> | Guarantees<br>given by<br>HSBCFrance <sup>1</sup> | Last year's<br>sales <sup>2</sup> | Last year's<br>net profit<br>or loss | Dividends<br>received by<br>HSBC France<br>in the last<br>financial year | Comments |
|----------------------------------|------------|---|---|-----------------------------------|--------------------------------------|--|----------|
| Cost                             | Net        |   |   |                                   |                                      |  |          |
| EUR54,739                        | EUR54,739  | -   | -   | EUR635                            | EUR150                               | -  | -        |
| EUR39,236                        | EUR39,236  | -   | -   | EUR27,429                         | EUR8,426                             | -  | -        |
| EUR36,370                        | EUR1,186   | -   | -   | EUR7                              | EUR2                                 | -  | -        |
| EUR60,384                        | EUR10,219  | -   | -   | EUR68                             | EUR39                                | -  | -        |
| EUR128,916                       | EUR128,916 | -   | -   | EUR12                             | EUR667                               | -  | -        |
| EUR16,260                        | EUR9,164   | -   | -   | EUR84                             | EUR48                                | -  | -        |
| EUR15,148                        | EUR15,148  | -   | -   | EUR11,640                         | EUR(1,442)                           | EUR5,000   | -        |
| EUR134,546                       | EUR134,546 | -   | -   | EUR184,706                        | EUR14,457                            | EUR41,937  | -        |
| EUR55,988                        | EUR25,859  | -   | -   | EUR159                            | EUR(1,324)                           | -  | -        |
| EUR4,689                         | EUR4,689   | -   | -   | -                                 | EUR24                                | -  | -        |
| EUR168,099                       | EUR168,099 | -   | -   | EUR17,266                         | EUR9,795                             | EUR38,070  | -        |
| EUR41,617                        | EUR41,617  | -   | -   | -                                 | EUR1,683                             | EUR36,966  | -        |

## Parent company financial statements (continued)

### Interests in subsidiaries and related parties at 31 December 2012 (continued)

| <i>(in thousands of currency units)</i>   | Business           | Share capital | Reserves + retained earnings before appropriation of net profit | Ownership interest % |
|---|--------------------|---------------|---|----------------------|
| <b>A – Information on companies whose book value at cost exceeds 1% of HSBC France’s share capital</b>                    |                    |               |   |                      |
| <b>1 – Subsidiaries (over 50%) (continued)</b>  |                    |               |   |                      |
| HSBC Leasing (France) . . . . .<br>39, rue Bassano – 75008 Paris (France)   | Financial company  | EUR281,760    | EUR(69,358)   | 100.00               |
| Société Financière et Immobilière . . . . .<br>103, avenue des Champs-Élysées – 75008 Paris (France)                      | Financial company  | EUR40,000     | EUR7,173  | 100.00               |
| Foncière Elysées S.A. . . . .<br>103, avenue des Champs-Élysées – 75008 Paris (France)                                    | Holding company    | EUR14,043     | EUR21,662   | 100.00               |
| Société Immobilière Malesherbes Anjou . . . . .<br>103, avenue des Champs-Élysées – 75008 Paris (France)                  | Holding company    | EUR13,412     | EUR36,017   | 100.00               |
| Charterhouse Management Services Ltd . . . . .<br>8 Canada Square – London E14 5HQ (United Kingdom)                       | Investment company | GBP10,000     | GBP(235)  | 100.00               |
| HSBC Real Estate Leasing (France) . . . . .<br>15, rue Vernet – 75008 Paris (France)                                      | Financial company  | EUR38,255     | EUR27,603   | 80.98                |
| CCF & Partners Asset Management Ltd . . . . .<br>8 Canada Square – London E14 5HQ (United Kingdom)                        | Financial company  | GBP5,000      | GBP412  | 100.00               |
| <b>2 – Associated companies (10-50%)</b>  |                    |               |   |                      |
| Lafarge Finance Limited . . . . .<br>Seaton House, 17 Seaton Place<br>St Helier, Jersey (United Kingdom)                  | Financial company  | GBP400,000    | –   | 16.67                |
| <b>B – Aggregate data concerning companies whose book value at cost does not exceed 1% of HSBC France’s share capital</b> |                    |               |   |                      |
| <b>1 – Subsidiaries not included in paragraph<sup>1</sup></b>   |                    |               |   |                      |
| a) French subsidiaries (aggregated) . . . . .   | –                  | –             | –   | –                    |
| b) Foreign subsidiaries (aggregated) . . . . .  | –                  | –             | –   | –                    |
| <b>2 – Related party companies not included in paragraph<sup>2</sup></b>  |                    |               |   |                      |
| a) French companies (aggregated) . . . . .  | –                  | –             | –   | –                    |
| b) Foreign companies (aggregated) . . . . .   | –                  | –             | –   | –                    |

<sup>1</sup> Loans, advances and guarantees granted outside the framework of normal banking business.

<sup>2</sup> Net operating income in the case of banks.

| Book value of securities held |            | Loans and advances granted by HSBC France <sup>1</sup> | Guarantees given by HSBC France <sup>1</sup> | Last year's sales <sup>2</sup> | Last year's net profit or loss | Dividends received by HSBC France in the last financial year | Comments |
|-------------------------------|------------|--|--|--------------------------------|--------------------------------|--|----------|
| Cost                          | Net        |  |  |                                |                                |  |          |
| EUR281,756                    | EUR281,756 | -  | -  | EUR(49,521)                    | EUR(11,339)                    | -  | -        |
| EUR84,053                     | EUR84,053  | -  | -  | EUR(3,916)                     | EUR11,571                      | EUR3,500   | -        |
| EUR44,478                     | EUR36,026  | -  | -  | EUR465                         | EUR415                         | -  | -        |
| EUR49,385                     | EUR49,385  | -  | -  | EUR10,931                      | EUR2,072                       | EUR2,000   | -        |
| EUR12,253                     | EUR12,253  | -  | -  | N/A                            | GBP(1,068)                     | -  | -        |
| EUR37,190                     | EUR37,190  | -  | -  | EUR152,883                     | EUR7,214                       | -  | -        |
| EUR5,190                      | EUR5,190   | -  | -  | -                              | GBP6                           | -  | -        |
| EUR245,068                    | EUR245,068 | -  | -  | -                              | -                              | GBP6,760   | -        |
| EUR760                        | EUR754     | -  | -  | -                              | -                              | EUR3,607   | -        |
| EUR1,821                      | EUR1,232   | -  | -  | -                              | -                              | -  | -        |
| EUR4                          | EUR4       | -  | -  | -                              | -                              | -  | -        |
| -                             | -          | -  | -  | -                              | -                              | -  | -        |

**Parent company financial statements** (continued)**Notes to the parent company financial statements**

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## 2012 Highlights

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### Business review

The eurozone sovereign debt crisis was preeminent in 2012, although there were reasons for cautious optimism towards the end of the year.

In this uneven environment, Banking and Wealth Management activities resisted well, whereas Market activities, benefitted from financial markets stabilisation.

HSBC France reported a profit before tax of EUR 802 million in 2012, compared with EUR -129 million the previous year in 2011.

Net operating income amounted to EUR 2,315 million, up by + 55 per cent over 2011. This performance is achieved with a strong increase in Markets activities mainly rates business.

Loan Impairment Charges at EUR 52 million display a 54 per cent fall over one year. This drop is due to a EUR 63 million release in country risk provision. Excluding this, credit risk provisions rose by 2 per cent in a deteriorated environment.

Operating expenses were stable at EUR 1,476 million reflecting the non recurring restructuring costs recognised in 2011 and the increase in certain taxes and performance-related expenses.

Profit attributable to shareholders therefore amounted to EUR 601 million in 2012; the distribution of a EUR 240 million dividend for 2012 is proposed.

Moreover, the average eligible loans to *Livret A* and *Livret de Développement Durable* funds assignment stands at EUR 823.5 million. This exceeds the non-centralised part of deposits on such products.

Finally, the simplification of the HSBC France group legal structure has continued. Particularly, in 2012, a merger took place between two HSBC France subsidiaries, HSBC Private Wealth Managers and HSBC Global Asset Management (France), without any significant consequence on the bank's accounts.

### Credit risk concentration

The group provides a diverse range of financial services predominantly in France. Its portfolio of financial instruments generating credit risk is highly diversified and without exposure to individual industries or economic groupings totalling more than 10 per cent of consolidated total assets, except as follows:

- the majority of the group's exposure to credit risk is concentrated in France. Within France, the group's credit risk is diversified over a wide range of industrial and economic groupings; and
- the group's position as part of a major international banking group means that it has a significant concentration of exposure to banking counterparties. The majority of credit risk to the banking industry is concentrated in Europe.

There are no special collateral requirements relating to industrial concentrations, with the exception of exposure to the real estate sector. The majority of exposure to the real estate and construction industry and the residential mortgage market is secured on the underlying property.

HSBC France is exposed to the sovereign risk of the eurozone regarding its market maker activity and its expertise in Treasury bond dealing for the HSBC Group concerning the sovereign debt of the eurozone countries. Some detailed information on the exposition concerning some eurozone countries selection is shown in Note 33 of the Consolidated financial statements included in the Annual Report and Accounts.

### Liquidity and funding management

HSBC France maintains a diversified and stable funding base comprising core retail and corporate customer deposits, portfolios of highly liquid assets, and debt instruments.

HSBC France adapts its liquidity and funding management policy framework in response to changes in the range of businesses that the group undertakes and to changes in the markets in which HSBC France operates.

HSBC France also complies with the HSBC Group's policy of matching all bank and professional deposits due in under one month plus a percentage of all other deposits with liquid assets, all currencies combined. In the event of crisis, the group would therefore be able to meet its obligations as they fall due, for a period of at least one month, without having to go to the markets. This rule is in addition to and reinforces the regulatory requirements.

## Parent company financial statements (continued)

### 1 Principal accounting policies

The principles adopted are those set out in the regulations of the *Comité de la Réglementation Bancaire et Financière* (CRBF), those of the *Comité de la Réglementation Comptable* (CRC), the *Conseil National de la Comptabilité* (CNC) opinions and French *Autorité de contrôle prudentiel* rulings. Transactions on which these various bodies have not given opinions are treated in accordance with generally accepted accounting principles in France.

The presentation of the HSBC France financial statements complies with the provisions of CRC regulation 2000-03, as amended relating to the individual financial reports of companies that are regulated by the *Comité de la Réglementation Bancaire et Financière*.

#### a Recognition and depreciation/amortisation of fixed assets

Since 1 January 2005, HSBC France applies CRC regulation 2002-10 of 12 December 2002 on the depreciation, amortisation and impairment of assets, as modified by CRC regulation 2003-07 of 12 December 2003.

This regulation makes the component approach mandatory in recognising, depreciating and amortising fixed assets. The details of the method are given in the French Urgent Issues Committee CNC opinion 2003-E of 9 July 2003.

Regarding recognition of the impact of first time adoption of the regulation, HSBC France opted for the prospective method of reallocating carrying amounts at 1 January 2005.

This method involves first breaking down the carrying amounts of fixed assets at 1 January 2005, among the new components that were identified, and then depreciating the carrying amounts thus calculated, less their residual values, over their remaining useful lives.

#### *Operating and investment fixed assets*

For operating and investment fixed assets, HSBC France adopted the components approach as a minimum floor using the following components, methods and useful lives:

| Components                                 | Depreciation and amortisation methods and periods |
|--|---|
| <b>Infrastructure</b>                      |   |
| Building .....                             | 25 and 50 years on a straight-line basis          |
| Civil engineering works .....              | 25 years on a straight-line basis                 |
| <b>Technical installations</b>             |   |
| Air conditioning Ventilation Heating ..... | 10 years on a straight-line basis                 |
| Electrical installations .....             | 10 years on a straight-line basis                 |
| Telephone and electrical fittings .....    | 10 years on a straight-line basis                 |
| Security fittings .....                    | 10 years on a straight-line basis                 |
| <b>Fittings</b>                            |   |
| Improvements and internal fittings .....   | 10 years on a straight-line basis                 |

#### *Fixed assets acquired on realising collateral on impaired lending facilities*

The accounting treatment of repossessed fixed assets that came into HSBC France's ownership on default by debtors depends on whether the company plans to continue to hold them or not.

Properties that the bank intends to resell quickly are treated as inventories. As a result, they are not amortised, but impairment is recognised if necessary. They are recorded in the "Other Assets" account, with corresponding impairment appearing in miscellaneous impairment.

Fixed assets that are expected to be held long-term, and that the bank has leased, constitute non-operating fixed assets and are depreciated over the same periods as for operating fixed assets with similar characteristics. In compliance with instructions from the supervisory bodies, impairment is recognised when the market value of the non-operating properties falls below their carrying amount.

#### *Goodwill*

Purchased goodwill, if not made up of separately identifiable assets, is not amortised. Instead, impairment is recognised if necessary on the basis of objective indicators.

## 1 Principal accounting policies (continued)

### *Other fixed assets*

For other fixed assets, depreciation periods are determined according to the remaining useful lives of the assets concerned, which usually fall into the following brackets:

- office equipment: 5 years;
- furniture: 5 to 10 years;
- IT hardware: 3 to 5 years;
- software: 3 to 5 years.

### *Assets held under finance lease*

The assets leased under the activity of leasing have a gross value of EUR 81.3 million, which corresponds to the input value of the goods plus expenses necessary for the implementation status of use of such property.

Depreciation is calculated using the straight-line method over the estimated useful life of the assets.

In accordance with French Urgent Issues Committee CNC Opinion n° 2006.C of 4 October 2006, CRC regulations 2002-10 and 2004-06 have not been applied to the assets leased.

The depreciation periods are as follows:

- furniture and office equipment: 5 years;
- computer equipment: 3 years;
- tools and equipment: 5 to 7 years.

Depreciation and amortisation of fixed assets leased under operating leases are recognised as an expense on finance lease or operating lease.

In financial accounting, the financial contracts outstanding is substituted to net fixed assets leased. The difference between the outstanding amounts of financial assets and the net book value of fixed assets is represented by the unearned finance income. At 31 December 2012, the financial outstanding amounts to EUR 73.4 million and the unearned finance income before deferred tax to EUR 4 million.

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## **b** *Securities portfolio*

In accordance with the provisions of CRC 90-01 as amended, securities are categorised as follows:

- trading account securities;
- available-for-sale securities;
- held-to-maturity securities;
- portfolio activity securities;
- other long-term securities;
- interests in subsidiaries and associates.

### *Trading account securities*

Trading securities are securities that are tradable on a liquid market and which are originally acquired or sold with the intention that they should be resold or bought back within a short timescale.

Trading securities are stated at cost (including accrued interest for fixed-income securities). At the balance sheet date, the securities are valued at market price, and changes in value are recognised through profit or loss.

### *Available-for-sale securities*

Securities acquired for purposes of income but intended in principle to be resold within a relatively short timescale are recorded under the heading “Available-for-sale securities”.

On the date of acquisition, they are recorded at cost price (excluding accrued income for fixed-income securities).

At the closing of the period, available-for-sale securities are valued individually at the lowest of their cost price or market value. The market value of equity and similar securities is represented by quoted prices at 31 December for listed securities and by probable trading prices for unlisted securities. The market value of fixed-income securities is the quoted price on the last working day of the period.

## Parent company financial statements (continued)

### 1 Principal accounting policies (continued)

Realised or unrealised gains or losses on hedging instruments are taken into account by instrument for the calculation of any impairment.

#### *Held-to-maturity securities*

Fixed-income securities that were acquired for holding long-term, and in principle to maturity, are categorised as held-to-maturity securities.

Held-to-maturity securities are valued at historical cost, with the premium or discount amortised over their residual life. Impairment may, however, be charged in the event of counterparty risk.

Securities acquired for income or held for regulatory reasons in certain foreign subsidiaries are categorised as held-to-maturity securities.

#### *Portfolio activity securities*

This category regroup investments made under normal arrangements with the sole objective of making medium-term capital gains with no intention of investing long-term in the business of the issuing entity, nor of taking an active part in the management of its operations. This is particularly the case for securities held in venture capital businesses.

Portfolio activity securities are recognised individually at the lower of their historical cost or value-in-use, determined with regard to the issuer's general prospects and the anticipated holding period.

The methods for assessing value-in-use are set out below.

#### *Other long-term securities*

"Other long-term securities" are equity shares and similar securities that HSBC France intends to hold long-term to derive a satisfactory return within an undefined period of time, without however taking any part in managing the businesses in which the shares are held, but with the intention of fostering long-term business relationships by creating a special link with the issuing companies. These securities are recorded individually at the lowest of their acquisition value or their value-in-use.

The methods for assessing value-in-use are set out below.

#### *Interests in subsidiaries and associates*

The heading "Interests in subsidiaries and associates" regroup securities held long-term (equity interests) and holdings in subsidiaries (shares in group companies).

Interests in subsidiaries and associates are valued individually at the lowest of their cost and their value-in-use, as determined below.

The assessment of the value-in-use of portfolio activity securities, other long-term securities and interests in subsidiaries and associates is carried out using a comprehensive approach based on the combination of a number of criteria:

- economic and financial assessment of the company based mainly on the value of its revalued net assets;
- market appraisal based on research by financial analysts;
- movements in market prices for listed companies, and for interests in subsidiaries and associates consideration of the specific relationships that may exist between HSBC France and each of the companies involved.

#### **Recognition of gains and losses**

Gains or losses on sale and impairment charges are recognised under the heading "Net gains on fixed assets" in the income statement, except for capital gains realised as part of restructuring operations, which are recognised as exceptional items.

#### **Presentation of the portfolio in the published statements**

The European Directive 86/635 as amended, aiming at harmonising the presentation and content of the annual accounts of all financial institutions within the European Union, did not recognise the concept of intention as a criterion for categorising portfolios. This breakdown is shown in Notes 4 and 5.



## 1 Principal accounting policies *(continued)*

In the balance sheet, the portfolio is broken down according to the legal nature of instruments:

- treasury bills and other eligible bills: tradable securities issued by governments irrespective of type (treasury bills, bonds, etc.);
- bonds and other fixed-income securities: securities issued by the private sector or by public bodies, where these are not admitted to the central bank refinancing facilities of the country of issue;
- equities and similar securities, including portfolio activity securities;
- interests in subsidiaries and associates and other long-term securities;
- shares in group companies.

### *Sale and repurchase agreements*

Stock lending or temporary acquisition, governed for legal purposes by law no. 93-1444 of 31 December 1993, amended by law no. 2003-1311 of 30 December 2003, referred to as stock repurchase agreements, have no effect on the composition and valuation of the securities portfolio. For accounting purposes, in accordance with article 5 of regulation 89-07, amended by regulation 94-05 of the CRBF, they are treated as financing transactions, with the counter-entries to cash movements being receivables or payables, depending on whether they involve stock lending or borrowing. Income and expenses received or borne by the transferee or transferor are recognised as interest.

### *Securities received or given under repurchase agreements*

Repurchase transactions that do not fall within the scope of law no. 93-1444 are categorised under this heading in the balance sheet. Their treatment for accounting purposes is similar to that described above for securities under sale and repurchase agreements.

Similar treatment is applied to “Buy and sell back” transactions.

### *Stock borrowed/lent against cash collateral*

Stock borrowing/lending against cash collateral is similar, for accounting purposes, to repurchase agreements.

### *Off-balance sheet repos and reverse repos*

At 31 December 2012, in accordance with article 15 of CRB 90-01 regulation, repo transactions recorded in off-balance sheet between the trade date and the settlement/delivery date are now shown under “Securities Commitments”. They were not reported in the previous financial statements.

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## c *Loans and advances*

### *Loans assessed individually*

Charges for impairment against non-performing and impaired loans, included in the calculation of the banking result, are determined annually on the basis of the risk of non-recovery assessed by analysing each loan individually. Since 1 January 2005, impairment on non-performing and impaired loans has been calculated on the basis of the present value of expected future recoveries.

Non-performing loans include all types of receivables, even receivables with collateral, with a probable or certain risk of non-recovery, in full or in part.

The following are therefore categorised as non-performing loans:

- receivables overdue for more than three months for all types of loans and equipment leases, with this period rising to more than six months for property loans or leases and more than nine months for loans to local government bodies;
- receivables with known risk criteria;
- receivables which, before expiry of these time limits, appear to be at risk (insolvent administration, liquidation or personal bankruptcy, etc.);
- receivables deriving from debt restructuring for which the debtor is again in default.

## Parent company financial statements (continued)

### 1 Principal accounting policies (continued)

HSBC France applies the provisions of CNC ruling 2007-06 on identifying overdrafts at risk of default. For overdrafts, the overdue period starts when:

- the debtor exceeds an authorised limit that has been notified to him by HSBC France;
- or the debtor is notified that the amount outstanding exceeds a limit set by HSBC France under its internal control system;
- or the debtor withdraws amounts without overdraft authorisation.

For lending granted to real estate industry borrowers, any categorisation to non-performing loans is decided upon, development by development, on the basis of criteria reflecting: project potential completion, the ability of shareholders/partners to provide the necessary equity, and also their financial standing.

The downgrade to non-performing loans immediately applies to all amounts outstanding and commitments for that debtor that are in the same category, on the contagion principle and, if applicable, the downgrade of counterparties belonging to the same group to non-performing debtors, on a case-by-case assessment.

In application of CRC regulation 2005-03 amending CRC 2002-03 on the accounting treatment of credit risk in entities covered by the French Banking and Financial Regulation Committee, HSBC France has introduced a specific system for dealing with restructured debt and impaired loans.

Impaired loans are those for which the prospect of recovery is very remote and for which a write-off is being considered. These include receivables which are long overdue or for which the contract has been terminated in case of leasing, and also receivables that have been categorised as non-performing for more than one year, unless final write off is not being considered because of information on the prospects for recovery available at that stage. Interests on impaired loans are not recognised through profit or loss until the date of actual payment.

Furthermore, in line with banking industry practice, the bank raises provisions to cover the risks incurred in certain countries considered as high risk by the banking industry.

In the income statement, charges and releases of provisions, losses on irrecoverable receivables and recoveries on receivables that had been written off are recognised in the “Cost of risk” line.

#### *Loans assessed on a portfolio basis*

In application of IFRS standards, impairment on a portfolio basis is recognised in HSBC France consolidated accounts to reflect known credit risks, where these risks cannot be allocated to individual receivables at the year end.

Impairment of this type is not recorded in individual company accounts as there is no regulatory basis for it.

#### *Discount on restructured debt*

In application of CRC regulation 2002-03 as amended on the accounting treatment of credit risk in entities covered by the French Banking and Financial Regulation Committee, HSBC France applies a specific system for dealing with restructured debt, when they have a significant impact.

On restructuring, any waived principal and interest, accrued or due, is written off.

Moreover, at the time of restructuring, a discount is provided for on the restructured debt for the difference between the present value of initially anticipated contractual cash flows and the present value of future flows of capital and interest arising from the restructuring plan. The discount rate used is the original effective interest rate for fixed interest loans, or the most recent effective rate before the restructuring calculated in accordance with contractual terms for floating-rate loans.

This discount is recognised in the net cost of risk on restructuring and is then written back through net interest income over the remainder of the period that the debt has to run.

#### *Application of the effective interest rate*

HSBC France has applied the CRC ruling 2009-03 of 3 December 2009. HSBC France has recognised lending fees and costs on a time-apportioned basis, with effect to 1 January 2010.

## 1 Principal accounting policies (continued)

### d Provisions

In accordance with CRC 2000-06, provisions are registered where it is probable that an outflow of resources, without an at least equivalent inflow being expected from the beneficiary (whether known or not), will be required to extinguish a legal or implicit obligation arising from past events and where the amount of the obligation can be reliably estimated.

#### *Retirement benefit liabilities*

As of 1 January 2004, HSBC France has opted to adopt CNC recommendation 2003-R01 on the rules for recognising and measuring obligations for retirement and similar benefits.

HSBC France provides some of its employees with long term and post-employment benefits such as pension plans, termination payments and loyalty bonuses.

The costs recognised for funding these defined-benefit plans are determined using the projected unit credit method, with annual actuarial valuations being performed on each plan.

Actuarial gains or losses are recognised through profit or loss.

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 period until the benefits are vested. The current service costs and any past service costs, together with the expected return on scheme assets less the unwinding of the discount on the scheme liabilities, are charged to operating expenses.

The net defined-benefit liability recognised in the balance sheet represents the present value of the defined-benefit obligations adjusted for unrecognised past service costs and reduced by the fair value of the scheme's 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.

Payments to defined-contribution plans and state-managed retirement benefit plans, where HSBC France's obligations under the plans are equivalent to a defined-contribution plan, are charged as an expense as they fall due.

#### *Provisions for French PEL and CEL home ownership plans and accounts*

CEL home ownership accounts and PEL home ownership plans are special financial instruments introduced by law no. 65-554 of 10 July 1965. They combine a savings phase and a lending phase which are inextricably linked, the lending phase being contingent to the savings phase.

In accordance with CNC regulation 2007-01 on the accounting treatment of CEL and PEL home ownership plans and accounts with banks and institutions authorised to receive home ownership funds and to grant home ownership loans, HSBC France has provided against the adverse consequences of PEL/CEL commitments in its individual company accounts.

PEL commitments are measured by series, without any offset between series. CEL commitments are considered as one single series, distinct from the PEL series.

Provisions for the adverse consequences of these commitments are calculated using a model which takes into account:

- an estimate of future customer savings and credit behaviour, based on historical data;
- the value of various market parameters, particularly interest rates and volatility, determined from data available at the date of assessment.

#### *Provision for share-based payments*

### **HSBC Group share plan**

The HSBC Group share plan is a performance reward plan for retaining high-achieving employees.

HSBC France has not entered into any specific arrangements for share-based payments. It benefits from HSBC Holdings plc stock option plans (hereafter referred to as "HSBC share plans"), which set up awards of options and shares.

In 2005, the HSBC Group conducted an in-depth review of its policy for awarding options and shares to its employees. The new arrangements for free option and share plans were submitted to its Annual General Meeting in May 2005. These arrangements introduced a French sub-plan (Schedule 3 of the general rule), which respected the legal and tax regulations applicable in France. This regulation was revised in 2011 firstly, to take into account the regulatory changes impacting the plan and, secondly, to formalise the rules of the "Group Performance Share Plan", which aim the Senior Executives. In this context, the French sub-plan (Schedule 5 of the new rules) has also been subject to a review to comply with local social and tax rules.

## Parent company financial statements (continued)

### 1 Principal accounting policies (continued)

Since 2006, the HSBC Group set up free share award plans for certain employees, under which a fixed number of HSBC Holdings plc shares are awarded. The shares vest in the employees' ownership two or three years after they are awarded, conditional on continued employment within the HSBC Group.

No cover arrangements were put in place for the plans granted in 2009 and onwards by HSBC France. Delivery of the shares is therefore made by purchasing the shares on the market, at the plan expiry date at the latest.

In accordance with CRC regulation 2008-15:

- the expense is recognised on a straight-line basis over the vesting period with the counter-entry going to a provision account which is cleared on final employee vesting. The measurement of the expense is based on assumptions on the number of beneficiaries leaving and on performance conditions;
- the provision recognised is based on the closing quoted price of the HSBC Holdings plc stock.

#### HSBC Group share option plans

The HSBC Group Share Option Plan was a long-term incentive plan available to certain Group employees between 2000 and 2005. The aim of the plan was to raise awareness of the best-performing employees about value-creation objectives for shareholders. The options were awarded at market value and could normally be exercised from the third year and up to the tenth anniversary of being awarded, subject to vesting conditions.

HSBC Group share options without performance conditions were granted between 2001 and 2005 to certain HSBC Group employees.

Finally, share options with performance conditions were granted in 2005 under the HSBC Group Share Plan to Senior Executives in France. The award of these options is combined with a bonus to be paid at the exercise date of the options for an amount equal to the exercise price of the options awarded. These share options are subject to a double Corporate Performance Condition, which consists of an absolute Earnings Per Share measure and a Total Shareholder Return measure, based on the HSBC Group's ranking against a comparative group of 28 major banks. The options vest on expiry of a period of three years and can be exercised up to the fourth anniversary of the date of grant, after which they become void.

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#### e Reserve for general banking risks

No reserve for general banking risks is held in the accounts of HSBC France at 31 December 2012.

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#### f Foreign exchange position

With the exception of structural foreign exchange positions valued at historical cost, the asset and liability foreign exchange positions are restated at the exchange rates applicable at the period end. The resulting gains or losses are included in operating banking income or expenses.

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#### g Forward foreign exchange contracts

Forward exchange contracts that are open at the closing of the period and hedged with spot transactions are valued at the spot rate at the period end. Differences between spot and forward rates calculated on close out are recorded on a time-apportioned basis in the income statement. Outright forward exchange contracts and those hedged by forward instruments are restated at the rate for the remaining period.

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#### h Financial derivatives

The HSBC France group operates on all new financial instruments markets, whether on behalf of its customers or for the purposes of hedging balance sheet items or for arbitration purposes.

The accounting principles applied vary according to the instruments and the intentions of the operators at the outset, either hedging or market operations. However, some general rules apply to all market positions. Other general rules are specific to certain instrument categories.

## 1 Principal accounting policies (continued)

### *Interest-rate and currency options*

Options are contracts entered into between two parties by which one, the buyer, is granted the right to buy or to sell an actual asset or another financial instrument called an “underlying asset” at the expiry of a certain time period, at a price agreed at the time the contract was concluded.

Option contracts result in a premium being paid by the buyer to the seller.

HSBC France has interest rate and currency options.

The basic accounting treatment principles for these various products are identical.

On closing out the contract, the notional amount of the “underlying asset”, which is the subject of the option, is recorded as an off-balance-sheet item.

For income and expenses, a distinction is made between contracts for hedging, contracts entered into for market operations or for arbitration purposes:

- the income and expenditure on hedging operations is reported symmetrically to the income and expenditure of the item being hedged;
- for market transactions, the positions are revalued at each period end. For transactions quoted on an organised market or similar within the meaning of CRBF regulation 88-02 as amended, changes in the value of positions are recognised through profit or loss, either by means of margin calls, or directly by means of a mathematical calculation where the options are not quoted.

### *Options on indexes or on equities*

Transactions involving index and equity contracts are entered into for purposes of market operations: changes in the value of contracts that have not been closed out at the balance sheet date are recognised directly through profit or loss.

### *Interest-rate futures (Tradable futures)*

The accounting treatment is identical to that set out above for options, in compliance with ruling 94-04 as amended by ruling 2003-03 of the French Banking Commission.

### *Currency swaps and/or interest terms (swaps, FRAs)*

In application of CRBF regulation 90-15 as amended, and the Ministry of the Economy, Finances and Industry decree of 20 February 2007, the contracts are recorded separately depending whether their purpose is to:

- hold stand-alone open positions to take advantage of any beneficial changes in interest rates;
- hedge, demonstrably from the outset, in accordance with the above-mentioned article 4 of CRBF regulation 88-02 as amended, interest-rate risk affecting an item or a group of similar items or credit risk in the case of Credit Default Swaps (CDS);
- hedge and manage the entity’s overall interest rate risk on assets, liabilities and off-balance-sheet items;
- to provide for specialist investment management of trading portfolios (trading business).

On the accounting side, methodology varies depending on whether the transactions are for hedging or trading business purposes.

The gains or losses on asset or liability hedges are recognised in the appropriate accounting period, unless the items hedged are themselves stated at market value in the balance sheet. This is particularly the case for swaps entered into for purposes of asset-liability management of overall interest rate risk.

Gains or losses on positions managed as part of a trading swaps portfolio are valued at current value after allowing for a discount to reflect counterparty risk and future portfolio management expenses.

In market activities, the contracts negotiated by HSBC France are revalued at market conditions after the date of the trade; the corresponding commitments are shown as off-balance-sheet items between the trade date and the value date. As a general rule, that second date is the date the cash flows are swapped and then recognised in the ordinary way in the balance sheet.

The notionals are recorded as off-balance-sheet items, whether they are actually to be swapped or are simply to serve a benchmark.

Forward foreign exchange contracts that are not hedged through treasury operations are valued at market value, at the rate for the period remaining to run.

## Parent company financial statements (continued)

### 1 Principal accounting policies (continued)

#### i Recognition of income and expenses

All income and expenses are time-apportioned to the appropriate accounting period, except for most commissions and dividends which are recognised when the right to receive them arises.

At 31 December 2012, HSBC France chose the accounting option to align to the IFRS using for the determination of the market value of trading instruments, Bid prices for long positions and Ask prices for short positions. Some very specific derivatives, generally produced by combining several simple products, are measured by modelling using market data. However, their value always reflects the lower liquidity of these positions which, because of their specific features, could probably not be closed out at mid-spread prices.

Following the review of the implementation of CRBF 90-15, regarding the definition of market value of financial instruments, HSBC France released EUR 30 million provisions as at 31 December 2011 for value adjustments covering liquidity restrictions and potentials errors due to valuation models and parameters.

The calculation of accrued interest recognised through profit or loss complies with the statutory rules for each instrument. Fixed-income securities, for example, are marked to market based on the coupon at the deal date through to that at the sale date. Interest is recognised for so long as the entity holds the instruments, that is from the purchase delivery date through to the sales delivery date. On the Paris market, for paper of this type, there is an interval of three days between the deal date and the delivery date.

At 31 December 2012, HSBC France made the choice to review the calculation methods of the country risk provision which had, until then, a general provision nature: countries depreciation rates, previously fixed, now reflect the economic risk appreciation. This estimation change resulted in a provision release of EUR 63 million.

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#### j Exceptional items

Items which are generated by or derive from exceptional circumstances, and not from ordinary operations, are recognised as exceptional items.

Gains or losses on disposals of holdings in subsidiaries and associates are categorised through pre-tax profit on ordinary operations.

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#### k Deferred taxation

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the 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 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.

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#### l Segment reporting

This information is not available on the parent company accounts but details are given in the Notes to the consolidated financial statements.

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#### m Combating tax evasion and avoidance

In compliance with CNC recommendation 2009-11 and the decree of 6 October 2009 on the application of article L. 511-45 of the French Financial and Monetary Code, HSBC France does not have a direct or indirect presence in any of the specified states or territories.

## 2 Loans and advances to banks

| (in millions of euros)  | 31.12.2012                | 31.12.2011                |
|---|---------------------------|---------------------------|
| <b>On demand deposits</b> <sup>1</sup>                          | <b>23,974.6</b>           | 26,823.2                  |
| <b>Term deposits</b>  | <b>17,935.7</b>           | 21,726.4                  |
| < 3 months  | 10,622.8                  | 16,589.1                  |
| > 3 months < 1 year   | 2,708.7                   | 2,244.1                   |
| > 1 year < 5 years  | 3,494.4                   | 2,047.2                   |
| > 5 years   | 1,109.9                   | 846.0                     |
| Accrued interest  | 14.5                      | 48.5                      |
| <b>Overall total</b>  | <b>41,924.8</b>           | 48,598.1                  |
| <i>Of which securities received under repurchase agreements</i> | <i>28,031.5</i>           | <i>37,700.1</i>           |
| <i>Of which subordinated loans</i>                              | <i>725.8</i> <sup>2</sup> | <i>718.3</i> <sup>2</sup> |

<sup>1</sup> Including overnight stock lending.

<sup>2</sup> Including subordinated debt granted in 2008 to HSBC Bank plc for EUR 650 million.

## 3 Customers loans

*Outstanding at 31 December*

### Breakdown of outstanding loans by type

| (in millions of euros)                          | 31.12.2012      | 31.12.2011 |
|---|-----------------|------------|
| Commercial loans                                | 151.1           | 217.0      |
| Ordinary accounts – debit balances              | 1,681.8         | 1,993.4    |
| Other customer facilities <sup>1</sup>          | 50,973.7        | 59,962.8   |
| <b>Total</b>                                    | <b>52,806.6</b> | 62,173.2   |
| <sup>1</sup> Including unspecified term lending | 20.3            | 25.5       |

### Breakdown of outstanding loans by quality

| (in millions of euros)                                   | 31.12.2012      | 31.12.2011   |
|--|-----------------|--------------|
| Retail loans   | 9,606.7         | 8,969.5      |
| Financial customer loans                                 | 358.2           | 830.0        |
| Non-financial customer loans                             | 19,091.7        | 19,521.5     |
| Securities received under repurchase agreements          | 23,668.3        | 32,715.4     |
| Accrued interest   | 81.7            | 136.8        |
| <b>Total</b>   | <b>52,806.6</b> | 62,173.2     |
| <i>Of which subordinated loans</i>                       | <i>55.0</i>     | <i>59.5</i>  |
| <i>Of which gross non-performing loans</i>               | <i>649.1</i>    | <i>665.3</i> |
| <i>Of which gross impaired loans</i>                     | <i>790.4</i>    | <i>766.8</i> |
| <i>Of which impairment on gross non-performing loans</i> | <i>148.1</i>    | <i>143.4</i> |
| <i>Of which impairment on gross impaired loans</i>       | <i>519.8</i>    | <i>533.6</i> |
| <i>Of which restructured loans</i>                       | <i>192.5</i>    | <i>106.2</i> |

**Parent company financial statements** (continued)**3 Customers loans** (continued)**Breakdown of outstanding loans by remaining contractual maturity**

| (in millions of euros)                        | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| <b>Repayable on demand</b> <sup>1</sup> ..... | <b>6,899.5</b>    | 2,616.3    |
| <b>Term deposits</b> .....                    | <b>45,825.4</b>   | 59,420.1   |
| < 3 months .....                              | <b>20,631.7</b>   | 31,303.1   |
| > 3 months < 1 year .....                     | <b>5,515.1</b>    | 8,273.0    |
| > 1 year < 5 years .....                      | <b>9,975.6</b>    | 10,707.1   |
| > 5 years .....                               | <b>9,702.9</b>    | 9,136.9    |
| Accrued interest .....                        | <b>81.7</b>       | 136.8      |
| <b>Total</b> .....                            | <b>52,806.6</b>   | 62,173.2   |

<sup>1</sup> Including overnight stock lending

**Breakdown by business sector**

| (in millions of euros)        | <b>31.12.2012</b> | 31.12.2011 |
|-------------------------------|-------------------|------------|
| Retail .....                  | <b>10,231.8</b>   | 9,565.7    |
| Industrial .....              | <b>1,443.4</b>    | 1,420.6    |
| Commercial and Services ..... | <b>8,211.7</b>    | 8,259.1    |
| Real estate .....             | <b>6,332.8</b>    | 6,041.3    |
| Finance .....                 | <b>25,109.6</b>   | 34,596.0   |
| Others .....                  | <b>1,477.3</b>    | 2,290.5    |
| <b>Total</b> .....            | <b>52,806.6</b>   | 62,173.2   |



#### 4 Portfolio of trading, available-for-sale securities and held-to-maturity securities

| (in millions of euros)   | <u>31.12.2012</u>      | <u>31.12.2011</u>      |
|--|------------------------|------------------------|
|  | <i>Carrying amount</i> | <i>Carrying amount</i> |
| <b>Treasury bills and other eligible bills</b> .....                             | <b>27,239.6</b>        | 23,884.0               |
| Trading account securities .....   | <b>21,848.3</b>        | 18,594.8               |
| Available-for-sale securities .....  | <b>5,347.7</b>         | 5,230.8                |
| Held-to-maturity securities .....  | –                      | –                      |
| Accrued interest .....   | <b>43.6</b>            | 58.4                   |
| <b>Debt securities</b> .....   | <b>7,494.9</b>         | 8,846.0                |
| Trading account securities .....   | <b>5,199.8</b>         | 7,292.9                |
| – bonds and other quoted securities .....  | <b>5,199.8</b>         | 7,292.9                |
| – unquoted bonds, interbank market securities and tradable debt securities ..... | –                      | –                      |
| Available-for-sale securities .....  | <b>2,087.4</b>         | 1,328.3                |
| – quoted bonds .....   | <b>2,073.4</b>         | 1,308.1                |
| – unquoted bonds, interbank market securities and tradable debt securities ..... | <b>14.0</b>            | 20.2                   |
| Held-to-maturity securities .....  | <b>184.2</b>           | 205.8                  |
| – quoted bonds .....   | <b>184.2</b>           | 205.8                  |
| – unquoted bonds, interbank market securities and tradable debt securities ..... | –                      | –                      |
| Accrued interest .....   | <b>23.5</b>            | 19                     |
| <i>Of which restructured loans</i> .....   | <b>208.2</b>           | 188.4                  |
| <b>Equity shares and similar &amp; portfolio equities</b> .....                  | <b>5.5</b>             | 164.0                  |
| Trading account securities .....   | –                      | –                      |
| – quoted shares .....  | –                      | –                      |
| – unquoted shares and similar .....  | –                      | –                      |
| Available-for-sale securities .....  | <b>0.6</b>             | 149.8                  |
| – quoted shares .....  | –                      | –                      |
| – unquoted shares and similar .....  | <b>0.6</b>             | 149.8                  |
| Portfolio activity securities .....  | <b>4.9</b>             | 14.2                   |
| – quoted portfolio activity shares .....   | –                      | –                      |
| – unquoted portfolio activity shares .....                                       | <b>4.9</b>             | 14.2                   |
| <b>Total</b> .....   | <b>34,740.0</b>        | 32,894.0               |

#### Breakdown by remaining contractual maturity of Treasury bills and government bonds

| Type of security<br>(in millions of euros)     | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| <b>Treasury bills and other eligible bills</b> |                   |                   |
| < 3 months .....                               | <b>836.1</b>      | 377.5             |
| > 3 months < 1 year .....                      | <b>4,111.4</b>    | 2,826.0           |
| > 1 year < 5 years .....                       | <b>10,344.2</b>   | 9,118.6           |
| > 5 years .....                                | <b>11,904.3</b>   | 11,503.6          |
| Accrued interest .....                         | <b>43.6</b>       | 58.4              |
| <b>Total</b> .....                             | <b>27,239.6</b>   | 23,884.0          |
| <b>Debt securities</b>                         |                   |                   |
| < 3 months .....                               | <b>142.2</b>      | 469.7             |
| > 3 months < 1 year .....                      | <b>560.0</b>      | 872.4             |
| > 1 year < 5 years .....                       | <b>4,573.6</b>    | 4,603.7           |
| > 5 years .....                                | <b>2,195.6</b>    | 2,881.2           |
| Accrued interest .....                         | <b>23.5</b>       | 19.0              |
| <b>Total</b> .....                             | <b>7,494.9</b>    | 8,846.0           |

**Parent company financial statements** (continued)**4 Portfolio of trading, available-for-sale securities and held-to-maturity securities** (continued)**Estimated value of the portfolio of available-for-sale and portfolio business securities**

| Type of security<br>(in millions of euros)  | 31.12.2012                 |                        | 31.12.2011                 |                        |
|---|----------------------------|------------------------|----------------------------|------------------------|
|   | <i>Net carrying amount</i> | <i>Estimated value</i> | <i>Net carrying amount</i> | <i>Estimated value</i> |
| Treasury bills and other eligible bills .....   | 5,347.7                    | 5,655.1                | 5,230.8                    | 5,374.8                |
| Debt securities .....   | 2,087.4                    | 2,200.2                | 1,328.3                    | 1,379.4                |
| Equity shares and similar and other portfolio equities .....  | 5.5                        | 5.8                    | 164.0                      | 169.5                  |
| <b>Total available-for-sale and portfolio activity securities<br/>(excluding related receivables) .....</b> | <b>7,440.6</b>             | <b>7,861.1</b>         | <b>6,723.1</b>             | <b>6,923.7</b>         |

The available-for-sale securities portfolio is made up mainly of fixed income securities for which the interest-rate risk is usually hedged. The portfolio valuation rules are given in Note 1 b on pages 197 to 199.

| (in millions of euros)  | 31.12.2012               |                   |                   |
|---|--------------------------|-------------------|-------------------|
|   | <i>Before provisions</i> | <i>Provisions</i> | <i>Net amount</i> |
| <b>Unrealised gains in available-for-sale securities<sup>1</sup> .....</b>  | <b>417.1</b>             | <b>4.7</b>        | <b>421.8</b>      |
| – treasury bills and other eligible bills .....                             | 304.6                    | 2.8               | 307.4             |
| – bonds and other fixed-income securities .....                             | 112.2                    | 1.9               | 114.1             |
| – equity shares and similar & portfolio equities .....                      | 0.3                      | –                 | 0.3               |
| <b>Unrealised losses in available-for-sale securities<sup>1</sup> .....</b> | <b>10.7</b>              | <b>9.4</b>        | <b>1.3</b>        |
| – treasury bills and other eligible bills .....                             | –                        | –                 | –                 |
| – bonds and other fixed-income securities .....                             | 6.1                      | 4.8               | 1.3               |
| – equity shares and similar & portfolio equities .....                      | 4.6                      | 4.6               | –                 |

<sup>1</sup> Available derivatives of partners cover EUR -349 million.

**Additional information on the securities given in compliance with article 16 of Banking Regulation Committee regulation 90-01 of 23 February 1990***Total of held-to-maturity securities sold during the period*

This information is not material.

*Unamortised difference between the acquisition price and the redemption price of held-to-maturity securities*

This information is not material.

## 5 Investments in subsidiaries and equity securities held for long-term

| (in millions of euros)  | <b>31.12.2012</b>          | 31.12.2011                 |
|---|----------------------------|----------------------------|
|   | <i>Net carrying amount</i> | <i>Net carrying amount</i> |
| <b>Interests in subsidiaries and associates</b> .....         | <b>330.8</b>               | 323.8                      |
| <b>Listed securities</b> .....                                | <b>1.8</b>                 | 1.9                        |
| – banks .....   | –                          | –                          |
| – others .....  | <b>1.8</b>                 | 1.9                        |
| <b>Non-listed securities</b> .....                            | <b>329.0</b>               | 321.9                      |
| – banks .....   | <b>49.7</b>                | 48.3                       |
| – others .....  | <b>279.3</b>               | 273.6                      |
| <b>Other long-term securities</b> .....                       | <b>10.6</b>                | 10.5                       |
| <b>Listed securities</b> .....                                | –                          | –                          |
| – banks .....   | –                          | –                          |
| – others .....  | –                          | –                          |
| <b>Non-listed securities</b> .....                            | <b>10.6</b>                | 10.5                       |
| – banks .....   | –                          | –                          |
| – others .....  | <b>10.6</b>                | 10.5                       |
| <b>Interests in group companies</b> .....                     | <b>1,142.1</b>             | 1,569.0                    |
| <b>Listed securities</b> .....                                | –                          | –                          |
| – banks .....   | –                          | –                          |
| – others .....  | –                          | –                          |
| <b>Non-listed securities</b> .....                            | <b>1,142.1</b>             | 1,569.0                    |
| – banks .....   | <b>512.1</b>               | 471.4                      |
| – others .....  | <b>630.0</b>               | 1,097.6                    |
| <b>Accrued interests</b> .....                                | –                          | –                          |
| <b>Total (including the 1976 statutory revaluation)</b> ..... | <b>1,483.5</b>             | 1,903.3                    |

| (in millions of euros)   | <b>31.12.2012</b> |
|--|-------------------|
| <b>Gross amounts at 1 January (excluding advances and accrued interests)</b> .....   | <b>2,086.9</b>    |
| Changes in the year .....  | <b>(457.6)</b>    |
| Acquisitions of securities/share issues <sup>1</sup> .....                           | <b>53.3</b>       |
| Disposals/capital reductions <sup>2</sup> .....                                      | <b>(458.7)</b>    |
| Effect of foreign exchange differences .....   | <b>6.0</b>        |
| Other movements / Merger <sup>3</sup> .....  | <b>(58.3)</b>     |
| <b>Gross amounts at 31 December (excluding advances and accrued interests)</b> ..... | <b>1,629.3</b>    |
| <b>Impairments at 1 January</b> .....  | <b>(183.6)</b>    |
| Changes in the year .....  | <b>37.6</b>       |
| New allowances <sup>4</sup> .....  | <b>(1.9)</b>      |
| Release of allowances no longer required <sup>5</sup> .....                          | <b>39.5</b>       |
| Other movements .....  | –                 |
| Effect of foreign exchange differences .....   | –                 |
| <b>Impairment at 31 December</b> .....   | <b>(146.0)</b>    |
| Accrued interests .....  | –                 |
| <b>Net book value including accrued interests</b> .....                              | <b>1,483.3</b>    |

1 Relates mainly to share capital increase for HSBC Factoring (France) for EUR 34 million, HSBC SFH (France) for EUR 6.75 million, as well as the OSEO securities acquisitions for EUR 1.3 million and the merger of HSBC Private Wealth Managers to HSBC Global Asset Management (France) for EUR 10.9 million.

2 Relates mainly to SAF Palissandre capital reduction of EUR 458.4 million.

3 Relates mainly to the exit of HSBC Private Wealth Managers following the merger with HSBC Global Asset Management (France) for EUR 49.7 million and transmission of the entire assets and liabilities of Vernet expansion for EUR 8.5 million.

4 Relates mainly to the allowance of EUR 1.7 million to HSBC Services (France).

5 Relates mainly to HSBC Private Wealth Managers reversal of provisions for EUR 38.78 million following the merger to HSBC Global Asset Management (France).

## Parent company financial statements (continued)

### 6 Intangible fixed assets

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Gross amounts at 1 January</b> .....                               | <b>485.4</b>      | 387.0             |
| Changes in the year:  |                   |                   |
| Transfers and other movements <sup>1</sup> .....                      | –                 | 91.6              |
| Fixed asset acquisitions .....  | 7.4               | 8.5               |
| Fixed asset disposals and other changes .....                         | <u>(1.9)</u>      | <u>(1.7)</u>      |
| <b>Gross amounts value at 31 December</b> .....                       | <b>490.9</b>      | 485.4             |
| <b>Amortisation at 1 January</b> .....                                | <b>240.1</b>      | 227.4             |
| Changes in the year:  |                   |                   |
| Charges for the period for amortisation and impairment .....          | 5.9               | 5.8               |
| Transfers and other movements (including Private bank transfer) ..... | –                 | 8.1               |
| Fixed asset sales, disposals and other changes .....                  | <u>(0.1)</u>      | <u>(1.2)</u>      |
| <b>Amortisation at 31 December</b> .....                              | <b>245.9</b>      | 240.1             |
| <b>Net book value of fixed assets at 31 December</b> .....            | <b>245.0</b>      | 245.3             |

<sup>1</sup> HSBC Private Bank France merger impact in 2011.

According to 2004-01 CRC regulation, a goodwill, corresponding to the difference between the net current value shares of the merged company and the net asset value transferred, was recognised on the merger of HSBC Hervet with HSBC France in 2008 and on the merger of HSBC Private Bank France with HSBC France in 2011.

Goodwill on merger is written back through profit or loss as the assets to which it was attributed are realised.

Goodwill on merger is considered to be impaired when the current value of one or more underlying assets, to which a portion of it was attributed, falls below the carrying amount of the asset(s) plus the attributed goodwill. The current value is the higher of the market value and the value-in-use (see article 322-1 of CRC regulation 99-03 as amended by regulation 02-10).

#### Concerning HSBC Hervet

The goodwill on merger, amounting initially to EUR 139.5 million, was attributed proportionately to the unrealised gains (net of tax), without being reflected in the accounting records, to the following items:

| (in millions of euros)  |              |
|---|--------------|
| The unrealised gain on the Baecque Beau HSBC securities ..... | 47.7         |
| Unrealised gains in fixed assets .....                        | 9.6          |
| Unrealised gains in securities .....                          | 0.2          |
| Purchased goodwill (no attribution) .....                     | <u>82.0</u>  |
|   | <b>139.5</b> |

At the end of 2012, following the realisation of part of the assets (mainly the merger of HSBC de Baecque Beau with HSBC France in 2008), and in the absence of depreciation, the goodwill on merger stood at EUR 89.5 million.

#### Concerning HSBC Private Bank France

The goodwill on merger, initially amounting to EUR 72.0 million, is fully attributed to purchased goodwill.

## 7 Tangible fixed assets

| (in millions of euros)  | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| <b>Gross amounts at 1 January</b> .....                               | <b>707.0</b>      | 667.3      |
| Changes in the year:  |                   |            |
| Transfers and other movements (including Private bank transfer) ..... | –                 | 4.8        |
| Fixed asset acquisitions .....  | <b>77.6</b>       | 83.0       |
| Fixed asset disposals and other changes <sup>1</sup> .....            | <b>(28.7)</b>     | (48.1)     |
| <b>Carrying amount at 31 December</b> .....                           | <b>755.9</b>      | 707.0      |
| <br>  |                   |            |
| <b>Depreciation at 1 January</b> .....                                | <b>492.8</b>      | 486.4      |
| Changes in the year:  |                   |            |
| Charges for the period for depreciation and impairment .....          | <b>44.9</b>       | 47.7       |
| Transfers and other movements (including Private bank transfer) ..... | <b>(6.5)</b>      | 3.5        |
| Fixed asset disposals and other changes <sup>1</sup> .....            | <b>(18.9)</b>     | (44.8)     |
| <b>Depreciation at 31 December</b> .....                              | <b>512.3</b>      | 492.8      |
| <b>Carrying amount at 31 December</b> .....                           | <b>243.6</b>      | 214.2      |
| <br>  |                   |            |
| Operating land and buildings .....                                    | <b>13.5</b>       | 14.5       |
| Non-operating land and buildings .....                                | <b>0.7</b>        | 1.3        |
| Other tangible assets .....   | <b>229.4</b>      | 198.4      |
| <b>Carrying amount at 31 December</b> .....                           | <b>243.6</b>      | 214.2      |

<sup>1</sup> Mainly due to write off of fixed assets in the context of the 2011 Strategic Plan.

|  | <b>31.12.2012</b> |
|--|-------------------|
| <b>Leasing and renting with buy option<sup>1</sup></b> |                   |
| Assets under construction .....                        | <b>0.7</b>        |
| Gross values <sup>2</sup> .....                        | <b>81.3</b>       |
| Amortisation .....                                     | <b>(4.7)</b>      |
| Related loans .....                                    | –                 |
| <b>Total</b> .....                                     | <b>77.4</b>       |

<sup>1</sup> In 2012 launch of the leasing activity for Commercial Banking customers.

<sup>2</sup> Main financed assets: Road assets EUR 35.5 million, Public buildings and construction EUR 10 million, Machine tool EUR 6.9 million.

## 8 Loan impairment

| (in millions of euros)  | <i>Balance at<br/>31.12.2011</i> | <i>Charges</i> | <i>Utilised<br/>releases</i> | <i>Available<br/>releases</i> | <i>Other<br/>changes</i> | <b>Balance at<br/>31.12.2012</b> |
|---|----------------------------------|----------------|------------------------------|-------------------------------|--------------------------|----------------------------------|
| Impairment on interbank and customer non-performing loans (excluding doubtful interest) ..... | 677.1                            | 238.0          | (89.9)                       | (143.6)                       | (14.0) <sup>1</sup>      | <b>667.6</b>                     |
| Impairment on securities .....  | 4.3                              | –              | –                            | –                             | –                        | <b>4.3</b>                       |
| Provisions for commitments by signature and disputes ....                                     | 12.3                             | 13.4           | (4.0)                        | (1.8)                         | –                        | <b>19.9</b>                      |
| <b>Total of impairment and provisions recognised in cost of risk</b> .....                    | <b>693.7</b>                     | <b>251.4</b>   | <b>(93.9)</b>                | <b>(145.4)</b>                | <b>(14.0)</b>            | <b>691.8</b>                     |

<sup>1</sup> Of which discounting effect on impaired loans recognised in net operating income .....

(7.9)

## Parent company financial statements (continued)

### 8 Loan impairment (continued)

#### Loan impairment

| (in millions of euros)   | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| Net impairment charge for the period   |                   |                   |
| Interbank and customer non-performing and impaired receivables<br>(excluding doubtful interest) <sup>1</sup> ..... | (111.3)           | (105.0)           |
| Counterparty risk on securities .....  | -                 | -                 |
| Commitments by issuer and disputes <sup>2</sup> .....  | (16.2)            | 0.8               |
| Recoveries of amounts previously written off .....   | 13.6              | 1.5               |
| <b>Total cost of risk excluding country risk</b> .....   | <u>(113.9)</u>    | <u>(102.7)</u>    |
| Country risk <sup>3</sup> .....  | 62.4              | (9.3)             |
| <b>Total cost of risk</b> .....  | <u>(51.5)</u>     | <u>(112.0)</u>    |
| 1 Of which unprovided losses on doubtful receivables .....   | (23.1)            | (11.8)            |
| 2 Of which unprovided losses .....   | (5.0)             | (0.5)             |
| 3 Country risk provision - see comments in Note 1 i.   |                   |                   |

### 9 Other assets

| (in millions of euros)                            | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Securities transactions settlement accounts ..... | 226               | 150               |
| Sundry debtors and other receivables .....        | 28,325            | 29,187            |
| <b>Total</b> .....                                | <u>28,551</u>     | <u>29,337</u>     |

### 10 Prepayments and accrued income

| (in millions of euros)                                  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Items in course of collection from other banks .....    | 809               | 806               |
| Other prepayments and accrued assets <sup>1</sup> ..... | 171,059           | 140,057           |
| <b>Total</b> .....                                      | <u>171,868</u>    | <u>140,863</u>    |

1 Including mark-to-market on derivatives instruments for EUR 164,758 million.

### 11 Treasury and interbank transactions

#### Deposits by banks

| (in millions of euros)                                      | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>On demand deposits</b> .....                             | 9,411.4           | 8,095.8           |
| <b>Term deposits</b> .....                                  | 31,645.9          | 38,236.0          |
| < 3 months .....  | 20,584.0          | 27,152.3          |
| > 3 months < 1 year .....                                   | 3,544.9           | 3,570.1           |
| > 1 year < 5 years .....                                    | 7,155.7           | 5,654.5           |
| > 5 years .....   | 361.3             | 1,859.1           |
| Accrued interest .....                                      | 104.5             | 90.0              |
| <b>Overall total</b> .....                                  | <u>41,161.8</u>   | <u>46,421.7</u>   |
| Of which securities given under repurchase agreements ..... | 28,923.3          | 32,336.5          |

## 12 Customer accounts

*Outstanding at 31 December*

### Breakdown of customer credit balances by type of deposit

| (in millions of euros)  | <b>31.12.2012</b> | 31.12.2011 |
|---|-------------------|------------|
| On demand deposits .....  | <b>16,756.3</b>   | 15,816.9   |
| Special demand accounts .....   | <b>7,327.8</b>    | 6,659.7    |
| Special term accounts .....   | <b>713.4</b>      | 770.5      |
| Term accounts .....   | <b>5,806.2</b>    | 8,015.7    |
| Certificates of deposit and savings certificates <sup>1</sup> .....   | <b>0.2</b>        | –          |
| <b>Total customer deposits (excluding repurchase agreements and including certificates of deposit and savings certificates) .....</b> | <b>30,603.9</b>   | 31,262.7   |
| <b>Total deposits excluding certificates of deposit and savings certificates .....</b>  | <b>30,603.7</b>   | 31,262.8   |
| Securities given under repurchase agreements .....  | <b>21,495.4</b>   | 25,135.6   |
| Accrued interest .....  | <b>139.1</b>      | 177.4      |
| <b>Total customer credit balance accounts .....</b>   | <b>52,238.2</b>   | 56,575.9   |

<sup>1</sup> Certificates of deposit are categorised in the balance sheet under the heading "Debt securities".

### Breakdown of customer credit balances by remaining contractual maturities

| (in millions of euros)          | <b>31.12.2012</b> | 31.12.2011 |
|---------------------------------|-------------------|------------|
| <b>On demand deposits .....</b> | <b>35,540.0</b>   | 22,549.9   |
| <b>Term deposits .....</b>      | <b>16,559.2</b>   | 33,848.6   |
| < 3 months .....                | <b>14,527.8</b>   | 23,246.0   |
| > 3 months < 1 year .....       | <b>1,777.6</b>    | 9,961.1    |
| > 1 year < 5 years .....        | <b>202.3</b>      | 416.7      |
| > 5 years .....                 | <b>51.5</b>       | 224.7      |
| Accrued interest .....          | <b>139.1</b>      | 177.4      |
| <b>Total .....</b>              | <b>52,238.2</b>   | 56,575.9   |

## 13 Bonds and other fixed income securities

| (in millions of euros)   | <b>31.12.2012</b> | 31.12.2011 |
|--|-------------------|------------|
| Certificates of deposit (including accrued interest) .....     | –                 | –          |
| Interbank market securities and tradable debt securities ..... | <b>6,385</b>      | 6,559      |
| Bonds .....  | <b>8,784</b>      | 10,678     |
| Accrued interest .....   | <b>122</b>        | 144        |
| <b>Total .....</b>   | <b>15,291</b>     | 17,381     |

### Breakdown of debt securities by maturity

| (in millions of euros)        | <b>31.12.2012</b> | 31.12.2011 |
|-------------------------------|-------------------|------------|
| <b>Debt securities .....</b>  | <b>15,169</b>     | 17,237     |
| < 1 year .....                | <b>9,403</b>      | 8,794      |
| of which up to 3 months ..... | <b>5,752</b>      | 6,876      |
| from 3 months to 1 year ..... | <b>3,651</b>      | 1,918      |
| > 1 year < 5 years .....      | <b>4,571</b>      | 7,070      |
| > 5 years .....               | <b>1,195</b>      | 1,373      |
| <b>Accrued interest .....</b> | <b>122</b>        | 144        |
| <b>Total .....</b>            | <b>15,291</b>     | 17,381     |

**Parent company financial statements** (continued)**14 Provisions**

| (in millions of euros)                              | <i>Balance at<br/>31.12.2011</i> | <i>Charges</i> | <i>Release for<br/>write off</i> | <i>Available<br/>releases</i> | <i>Other<br/>movements</i> | <i>Balance at<br/>31.12.2012</i> |
|---|----------------------------------|----------------|----------------------------------|-------------------------------|----------------------------|----------------------------------|
| Provisions for commitments                          |                                  |                |                                  |                               |                            |                                  |
| by signature and disputes...                        | 12.4                             | 13.4           | (4.0)                            | (1.9)                         | –                          | <b>19.9</b>                      |
| Provision for country risk...                       | 62.7                             | –              | –                                | (62.7)                        |                            | –                                |
| Provision on forward<br>financial instruments ..... | 81.6                             | –              | –                                | –                             | (81.6) <sup>2</sup>        | –                                |
| Other provisions <sup>1</sup> .....                 | 280.7                            | 129.2          | (57.2)                           | (50.1)                        | (0.1)                      | <b>302.5</b>                     |
| <b>Total</b> .....                                  | <b>437.4</b>                     | <b>142.6</b>   | <b>(61.2)</b>                    | <b>(114.7)</b>                | <b>(81.7)</b>              | <b>322.4</b>                     |

<sup>1</sup> Including employee benefits provision (see Note 20 "Pensions and post-employment benefits"), for share based payments and on 2012-2014 Strategic Plan.

<sup>2</sup> Reclassification from provisions to actual value of derivatives products.

**Provision on PEL/CEL home ownership products**

Provision at 31 December 2012, by age group:

- PEL: EUR 11.7 million (of which EUR 7 million of provision for over 10 years; EUR 0.4 million of provision between 4 and 10 years and EUR 4.4 million of provision under 4 years);
- CEL: EUR 0.4 million.

The movements on provisions recognised through profit or loss in 2012 relate to a charge of EUR 2.2 million (including a release of allowance of EUR 0.4 million more than 10 years old, EUR 0.5 million between 4 and 10 years old and EUR 2.3 million under 4 years old).

Amounts collected at 31 December 2012, by age group:

- PEL: EUR 690.6 million, aged as follows:
  - 0-4 years: EUR 170.3 million,
  - 4-10 years: EUR 251.4 million,
  - more than 10 years: EUR 268.9 million;
- CEL: EUR 125.8 million.

Outstandings collected at 31 December 2012, by age group:

- PEL: EUR 5.2 million:
  - 0-4 years: EUR 2.3 million,
  - 4-10 years: EUR 0.1 million,
  - more than 10 years: EUR 2.8 million;
- CEL: EUR 13.4 million.

**15 Other liabilities**

| (in millions of euros)   | <b>31.12.2012</b> | 31.12.2011 |
|--|-------------------|------------|
| Securities transactions settlement accounts .....  | <b>33</b>         | 226        |
| Sundry creditors .....   | <b>12,541</b>     | 12,843     |
| Short position and securities received under repurchase<br>agreements confirmed resold ..... | <b>33,515</b>     | 36,728     |
| <b>Total</b> .....   | <b>46,089</b>     | 49,797     |



## 16 Accruals and deferred income

| (in millions of euros)                               | <b>31.12.2012</b> | 31.12.2011 |
|--|-------------------|------------|
| Items in course of collection from other banks ..... | <b>702</b>        | 757        |
| Accruals and deferred income <sup>1</sup> .....      | <b>172,101</b>    | 141,258    |
| <b>Total</b> .....                                   | <b>172,803</b>    | 142,015    |

<sup>1</sup> Including mark-to-market on derivatives instruments for EUR 165,276 million.

## 17 Subordinated debt

| (in millions of euros)           | <b>31.12.2012</b> | 31.12.2011 |
|----------------------------------|-------------------|------------|
| Subordinated notes .....         | <b>165</b>        | 165        |
| Undated subordinated notes ..... | <b>16.2</b>       | 16.2       |
| Accrued interest .....           | <b>0.2</b>        | 0.4        |
| <b>Total</b> .....               | <b>181.4</b>      | 181.6      |

### Securities issued by HSBC France

Subordinated securities issued by HSBC France, in euros and other currencies, are liabilities which, in the event of liquidation, will only be repaid after the interests of other creditors have been extinguished but before repayment of the holders of participating securities or equity.

The main issues are listed below:

### Redeemable subordinated securities

| (in millions of euros)   | <u>Date<br/>of issue</u> | <u>Date of<br/>maturity</u> | <u>Interest<br/>type</u> | <u>Currency<br/>of issue</u> | <b>31.12.2012</b> | 31.12.2011 |
|--|--------------------------|-----------------------------|--------------------------|------------------------------|-------------------|------------|
| Redeemable subordinated securities .....   | 25.03.2004               | 25.03.2014                  | Floating rate            | EUR                          | <b>150.0</b>      | 150.0      |
| Redeemable subordinated securities .....   | 15.12.2000               | 15.12.2015                  | Floating rate            | EUR                          | <b>15.0</b>       | 15.0       |
| Accrued interest .....   |                          |                             |                          |                              | <b>0.2</b>        | -          |
| <b>Total for securities issued by HSBC France (including accrued interest)</b> ..... |                          |                             |                          |                              | <b>165.2</b>      | 165.0      |

### Participating securities: undated subordinated securities and debt

| (in millions of euros)                          | <u>Date of<br/>issue</u> | <u>Nominal<br/>rate</u>            | <u>Issue<br/>currency</u> | <b>31.12.2012</b> | 31.12.2011 |
|---|--------------------------|------------------------------------|---------------------------|-------------------|------------|
| Undated subordinated securities .....           | 22.07.1985               | Effective<br>monthly<br>rate -0.25 | FRF                       | <b>16.2</b>       | 16.2       |
| Accrued interest .....                          |                          |                                    |                           | -                 | 0.4        |
| <b>Total (including accrued interest)</b> ..... |                          |                                    |                           | <b>16.2</b>       | 16.6       |

**Parent company financial statements** (continued)**18 Share capital**

|  | 31.12.2012                  |  | 31.12.2011                  |  |
|--|-----------------------------|--|-----------------------------|--|
|  | <i>Number<br/>of shares</i> | <i>Total<br/>(in thousands<br/>of EUR)</i> | <i>Number<br/>of shares</i> | <i>Total<br/>(in thousands<br/>of EUR)</i> |
| (shares of 5 euros)                    |                             |  |                             |  |
| At 1 January .....                     | <b>67,437,827</b>           | <b>337,189</b>                             | 67,437,820                  | 337,189                                    |
| – Subscription options exercised ..... | –                           | –  | –                           | –  |
| – New capital issued – Merger .....    | –                           | –  | 7                           | –  |
| – Reduction of capital .....           | –                           | –  | –                           | –  |
| <b>At 31 December</b> .....            | <b>67,437,827</b>           | <b>337,189</b>                             | <b>67,437,827</b>           | <b>337,189</b>                             |

**Voting rights**

At 31 December 2012, the total of voting rights stood at 67,437,827; shares with double voting rights disappeared with the tender offer and the minority buyout launched by HSBC Holdings plc.

## 19 Equity

|   | 31.12.2012                            |                                      | 31.12.2011                            |                                      |
|---|---------------------------------------|--------------------------------------|---------------------------------------|--------------------------------------|
|   | <i>Before appropriation of profit</i> | <i>After appropriation of profit</i> | <i>Before appropriation of profit</i> | <i>After appropriation of profit</i> |
| (in millions of euros)                  |                                       |                                      |                                       |                                      |
| Called-up share capital .....           | 337.2                                 | 337.2                                | 337.2                                 | 337.2                                |
| Share premium account .....             | 16.1                                  | 16.1                                 | 16.1                                  | 16.1                                 |
| Reserves .....                          | 1,047.6                               | 1,047.6                              | 1,047.9                               | 1,047.9                              |
| Legal reserve .....                     | 38.1                                  | 38.1                                 | 38.1                                  | 38.1                                 |
| – Long-term gains reserve .....         | 405.5                                 | 405.5                                | 405.5                                 | 405.5                                |
| – Revaluation reserve .....             | 5.2                                   | 5.2                                  | 5.5                                   | 5.5                                  |
| – Extraordinary and other reserve ..... | 304.7                                 | 304.7                                | 304.7                                 | 304.7                                |
| – Free reserve .....                    | 294.1                                 | 294.1                                | 294.1                                 | 294.1                                |
| Revaluation reserve .....               | –                                     | –                                    | –                                     | –                                    |
| Retained earnings .....                 | 2,785.5                               | 3,386.7                              | 2,877.0                               | 2,785.5                              |
| Interim dividend .....                  | –                                     | –                                    | (118.0)                               | –                                    |
| Special tax-allowable reserves .....    | 26.2                                  | 26.2                                 | 33.1                                  | 33.1                                 |
| Net Profit for the year .....           | 601.2                                 | –                                    | 26.5                                  | –                                    |
| <b>Equity .....</b>                     | <b>4,813.8</b>                        | <b>4,813.8</b>                       | <b>4,219.8</b>                        | <b>4,219.8</b>                       |

### Changes in equity in 2012

(in millions of euros)

|  |                |
|--|----------------|
| <b>Balance at 1 January 2012 .....</b>   | <b>4,219.8</b> |
| Net Profit for the year .....  | 601.2          |
| New shares issued upon exercise of stock options .....   | –              |
| Reduction of capital .....   | –              |
| Interim dividend .....   | –              |
| Others <sup>1</sup> .....  | (7.2)          |
| Retained earnings – first-time adoption of the new accounting policy of effective rate of interest ..... | –              |
| <b>Balance at 31 December 2012 .....</b>   | <b>4,813.8</b> |

<sup>1</sup> Changes connected with regulated provisions and revaluation surplus.

### Legal reserve

This reserve is built up by appropriating at least one-twentieth of the year's profit. This appropriation ceases to be mandatory once this reserve reaches one-tenth of share capital. It is not distributable.

### Net long-term gains reserve

Distributing this reserve would lead to an additional tax charge equal to the difference between standard tax rate and reduced tax rate.

### Revaluation reserve (1976 revaluation)

This reserve could be incorporated into capital, but it cannot be distributed or used to offset losses.

### Other reserves

Amounts put into reserves over five years ago would be subject to a levy if they were to be distributed.

For distributions paid on or after 1 January 2000, HSBC France can charge the dividends against profits liable to corporate income tax for accounting periods ended at most five years ago, starting with the oldest, in application of the decree of 21 December 1999.

**Parent company financial statements** (continued)**20 Pensions, post-employment benefits**

|   |                   |            |
|---|-------------------|------------|
| (in millions of euros)  | <b>31.12.2012</b> | 31.12.2011 |
| Provision for employee-related commitments <sup>1</sup> ..... | <b>149.5</b>      | 115.0      |

<sup>1</sup> Including defined benefits pension plans for Executive Directors for EUR 3.4 million in 2011 and for EUR 4.8 million in 2012.

**Principal actuarial assumptions of the post-employment defined benefit plans**

The main actuarial assumptions used for measuring pension plan commitments and post-employment healthcare benefits, which serve as the basis for calculating the expense for the relevant accounting periods, are as follows:

| (in %)                           | <i>Discount<br/>rate</i> | <i>Expected<br/>rate of<br/>return on<br/>plan assets</i> | <i>Inflation<br/>assumption</i> | <i>Rate of<br/>increase for<br/>pensions in<br/>payment<br/>and<br/>deferred<br/>pensions</i> | <i>Rate of pay<br/>increase</i> | <i>Mortality<br/>rate</i> |
|----------------------------------|--------------------------|---|---------------------------------|---|---------------------------------|---------------------------|
| <b>At 31 December 2012</b> ..... | <b>2.75</b>              | - <sup>1</sup>  | <b>2</b>                        | <b>2</b>  | <b>3</b>                        | - <sup>2</sup>            |
| At 31 December 2011 .....        | 4.5                      | - <sup>1</sup>  | 2                               | 2   | 3                               | - <sup>2</sup>            |

<sup>1</sup> The expected rate of return on bonds was 3.5% in 2012 and 4% in 2011.

<sup>2</sup> HSBC France uses "mortality tables TV88-90" for retirement compensation and long-service awards and TGH/TGF05 for pension obligations.

HSBC France determines discount rates in consultation with its actuaries based on the current average yield of high quality (AA-rated) debt instruments, with maturities consistent with that of the pension obligation. The expected rate of return on plan assets is determined in consultation with HSBC's actuaries, based on historical market returns, adjusted for additional factors such as the current rate of inflation and interest rates.

**Provision recognised**

|  |                   |            |
|--|-------------------|------------|
| (in millions of euros)                     | <b>31.12.2012</b> | 31.12.2011 |
| Present value of benefit obligations ..... | <b>161.3</b>      | 128.1      |
| Fair value of plan assets .....            | <b>(11.9)</b>     | (13.0)     |
| <b>Net liability recognised</b> .....      | <b>149.5</b>      | 115.0      |

## 21 Off-balance-sheet items

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Loan commitments</b>   |                   |                   |
| Commitments given   |                   |                   |
| Refinancing agreements and other financing commitments          |                   |                   |
| in favour of banks .....  | 2,094             | 2,159             |
| In favour of customers .....                                    | 16,670            | 19,634            |
| – confirmed credit facilities .....                             | 16,611            | 19,573            |
| – acceptances payable and similar instruments .....             | <u>59</u>         | <u>59</u>         |
| <b>Total</b> .....  | <u>18,764</u>     | <u>21,792</u>     |
| <i>Of which transactions with group companies</i> .....         | 820               | 820               |
| Commitments received  |                   |                   |
| Refinancing agreements and other financing commitments          |                   |                   |
| in favour of banks <sup>1</sup> .....                           | 360               | 6,510             |
| <b>Guarantee commitments</b>                                    |                   |                   |
| Commitments given   |                   |                   |
| Guarantees, acceptances and other security to banks .....       | 1,159             | 2,097             |
| Guarantees, acceptances and other securities to customers ..... | <u>3,427</u>      | <u>4,057</u>      |
| <b>Total</b> .....  | <u>4,586</u>      | <u>6,154</u>      |
| <i>Of which transactions with group companies</i> .....         | 79                | 121               |
| Commitments received  |                   |                   |
| Guarantees, acceptances and other security from banks .....     | 7,819             | 6,751             |

<sup>1</sup> Decrease of the funding commitment received from the French Bank for EUR -4,300 million.

### Loans pledged for Covered Bonds issues

|   | <u>31.12.2012</u> |
|---|-------------------|
| Covered bonds .....                           | 3,997             |
| Loans pledged on guarantee 3G and TRICP ..... | 4,115             |
| Securities pledged on guarantee .....         | <u>1,851</u>      |
| <b>Total</b> .....                            | <u>9,963</u>      |

## Parent company financial statements (continued)

|                                   | 31.12.2012               |                                   |                                   | 31.12.2011         |                          |                                  |                                   |                    |
|-----------------------------------|--------------------------|-----------------------------------|-----------------------------------|--------------------|--------------------------|----------------------------------|-----------------------------------|--------------------|
|                                   | Fair value<br>31.12.2012 | Hedging<br>contracts <sup>1</sup> | Trading<br>contracts <sup>1</sup> | Total <sup>1</sup> | Fair value<br>31.12.2011 | Hedging<br>contract <sup>1</sup> | Trading<br>contracts <sup>1</sup> | Total <sup>1</sup> |
| <b>22 Derivatives</b>             |                          |                                   |                                   |                    |                          |                                  |                                   |                    |
| <b>Exchanges rate contracts</b>   |                          |                                   |                                   |                    |                          |                                  |                                   |                    |
| (in billions of euros)            |                          |                                   |                                   |                    |                          |                                  |                                   |                    |
| <b>Unconditional transactions</b> |                          |                                   |                                   |                    |                          |                                  |                                   |                    |
| Exchange traded                   |                          |                                   |                                   |                    |                          |                                  |                                   |                    |
| – interest rate                   | (5.5)                    | 5.5                               | 4,636.5                           | 4,442.0            | (4.6)                    | 8.0                              | 4,675.7                           | 4,683.7            |
| – exchange rate                   | –                        | –                                 | 93                                | 93                 | –                        | –                                | 117.8                             | 117.8              |
| – equity                          | –                        | –                                 | 93.0                              | 93.0               | –                        | –                                | 117.8                             | 117.8              |
| Non-exchange traded               | (5.5)                    | 5.5                               | 4,343.5                           | 4,349.0            | (4.6)                    | 8.0                              | 4,557.9                           | 4,565.9            |
| – futures                         | –                        | –                                 | 403.2                             | 403.2              | –                        | –                                | 396.5                             | 396.5              |
| – interest rate                   | 0.3                      | 0.6                               | 3,758.5                           | 3,759.1            | 1                        | 1.7                              | 3,961.2                           | 3,962.9            |
| – exchange rate                   | (6.1)                    | 0.1                               | 53.7                              | 53.8               | (5.5)                    | 0.3                              | 66.1                              | 66.4               |
| – other contracts                 | 0.3                      | 4.8                               | 128.1                             | 132.9              | (0.1)                    | 6.0                              | 134.1                             | 140.1              |
| <b>Conditional transactions</b>   | (4)                      | 0.4                               | 492.8                             | 493.2              | (3.7)                    | 2.1                              | 564.4                             | 566.5              |
| Exchange traded                   | –                        | –                                 | 40.1                              | 40.1               | –                        | –                                | 54.6                              | 54.6               |
| Interest rate                     | –                        | –                                 | 3.8                               | 3.8                | –                        | –                                | 4.6                               | 4.6                |
| Exchange rate                     | –                        | –                                 | 36.3                              | 36.3               | –                        | –                                | 50.0                              | 50.0               |
| Other contracts                   | –                        | –                                 | –                                 | –                  | –                        | –                                | –                                 | –                  |
| Non-exchange traded               | (4)                      | 0.4                               | 452.7                             | 453.1              | (3.7)                    | 2.1                              | 509.8                             | 511.9              |
| Caps and floors                   | –                        | 0.3                               | 166.2                             | 166.5              | –                        | 1.3                              | 214.4                             | 215.7              |
| Swaptions and options             | (4)                      | –                                 | –                                 | –                  | (3.7)                    | –                                | –                                 | –                  |
| – bought                          | –                        | 0.1                               | 137.6                             | 137.7              | –                        | 0.8                              | 138.7                             | 139.5              |
| – sold                            | –                        | –                                 | 148.9                             | 148.9              | –                        | –                                | 156.7                             | 156.7              |
| <b>Total derivatives</b>          | <b>5.9</b>               | <b>5.9</b>                        | <b>4,929.3</b>                    | <b>4,935.2</b>     | <b>(3.7)</b>             | <b>10.1</b>                      | <b>5,240.1</b>                    | <b>5,250.2</b>     |

1 Notional contract amounts.

## 22 Derivatives (continued)

### Other information on derivatives

|                           |                   |            |
|---------------------------|-------------------|------------|
| (in billions of euros)    | <b>31.12.2012</b> | 31.12.2011 |
| Microhedge contract ..... | <b>0.6</b>        | 1.7        |
| Macrohedge contract ..... | –                 | –          |
| Trading .....             | <b>3,758.5</b>    | 3,961.2    |
| Other .....               | –                 | –          |

### Derivatives: maturity analysis

|                               |                       |                       |                       |                       |
|-------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
|                               | <b>31.12.2012</b>     |                       |                       |                       |
| (in billions of euros)        | <u>&lt;= 1 year</u>   | <u>&lt;= 5 years</u>  | <u>&gt; 5 years</u>   | <u>Total</u>          |
| Derivatives:                  |                       |                       |                       |                       |
| Exchange contracts .....      | <b>10.1</b>           | <b>30.4</b>           | <b>13.2</b>           | <b>53.7</b>           |
| Interest rate contracts ..... | <b>834.8</b>          | <b>1,417.7</b>        | <b>1,508.1</b>        | <b>3,760.6</b>        |
| Others .....                  | <b>677.5</b>          | <b>315.5</b>          | <b>127.9</b>          | <b>1,120.9</b>        |
| <b>Total</b> .....            | <b><u>1,522.4</u></b> | <b><u>1,763.6</u></b> | <b><u>1,649.2</u></b> | <b><u>4,935.2</u></b> |

### Risk-weighted assets

Amount of Exposure At Default (EAD) for derivatives contracts

|  |                       |                       |
|--|-----------------------|-----------------------|
| (in millions of euros)   | <b>31.12.2012</b>     | 31.12.2011            |
| <b>A – Contracts concluded under Master agreement with close-out netting</b> ..... | <b>4,841.7</b>        | 5,129.2               |
| 1. Transactions with banks from OECD countries .....                               | <b>4,841.1</b>        | 5,125.6               |
| 2. Transactions with customers and banks localised outside OECD countries .....    | <b>0.5</b>            | 3.6                   |
| <b>B – Other contracts</b> .....   | <b>475.3</b>          | 633.4                 |
| 1. Transactions with banks from OECD countries .....                               | <b>474.8</b>          | 632.8                 |
| – interest rate contracts .....  | <b>416.8</b>          | 120.1                 |
| – exchange contracts .....   | <b>58.0</b>           | 512.8                 |
| – equity derivatives contracts .....   | –                     | –                     |
| – commodities contracts .....  | –                     | –                     |
| 2. Transactions with customers and banks localised outside OECD countries .....    | <b>0.6</b>            | 0.6                   |
| – interest rate contracts .....  | –                     | –                     |
| – exchange contracts .....   | <b>0.6</b>            | 0.6                   |
| – equity derivatives contracts .....   | –                     | –                     |
| <b>Total Exposure At Default</b> .....   | <b><u>5,317.0</u></b> | <b><u>5,762.6</u></b> |
| <i>Corresponding risk-weighted assets (RWA)</i> .....                              | <b><u>1,063.7</u></b> | <b><u>1,701.7</u></b> |

**Parent company financial statements** (continued)**23 Net interest income**

| (in millions of euros)                        | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Interest and similar income</b>            |                   |                   |
| Banks and financial institutions .....        | 250.6             | 648.1             |
| Customers .....                               | 1,087.5           | 1,438.8           |
| Bonds and other fixed-income securities ..... | 136.1             | 254.0             |
| <b>Total</b> .....                            | <u>1,474.2</u>    | <u>2,340.9</u>    |
| <b>Interest and similar expenses</b>          |                   |                   |
| Banks and financial institutions .....        | 207.2             | 509.6             |
| Customers .....                               | 344.9             | 626.0             |
| Subordinated liabilities .....                | 3.1               | 3.1               |
| Other bonds and fixed-income securities ..... | 185.0             | 466.9             |
| <b>Total</b> .....                            | <u>740.2</u>      | <u>1,605.6</u>    |

**24 Fixed-income securities**

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| <b>Income</b>   |                   |                   |
| Available-for-sale and similar & portfolio activity securities .....          | –                 | –                 |
| Interests in subsidiaries and associates and other long-term securities ..... | 0.1               | 38.7              |
| Interests in group companies .....  | 142.8             | 149.9             |
| <b>Total</b> .....  | <u>142.9</u>      | <u>188.6</u>      |

**25 Breakdown of fees**

| <b>Breakdown of fees recorded as such in the published income statement</b> |                   |                   |
|---|-------------------|-------------------|
| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
| <b>Fees</b>   |                   |                   |
| <b>Income</b> .....   | 794.7             | 808.1             |
| On transactions with banks .....  | 3.8               | 5.9               |
| On transactions with customers .....  | 109.7             | 123.0             |
| On foreign exchange transactions .....                                      | 2.8               | 2.8               |
| On primary securities market activities .....                               | 37.9              | 65.2              |
| On provision of services for third parties .....                            | 470.4             | 472.5             |
| On commitments .....  | 124.4             | 99.9              |
| Other commission .....  | 45.7              | 38.8              |
| <b>Expenses</b> .....   | <u>(197.4)</u>    | <u>(201.2)</u>    |
| On transactions with banks .....  | (6.6)             | (9.0)             |
| On corporate actions .....  | (21.2)            | (24.8)            |
| On forward financial instrument activities .....                            | (9.8)             | (12.0)            |
| On provision of services for third parties .....                            | (142.1)           | (147.1)           |
| On commitments .....  | (12.7)            | (0.4)             |
| Other commission .....  | (5.0)             | (7.9)             |
| <b>Total fees</b> .....   | <u>597.3</u>      | <u>606.9</u>      |



## 26 Gains and losses on portfolio business transactions

| (in millions of euros)              | <u>31.12.2012</u> | <u>31.12.2011</u> |
|-------------------------------------|-------------------|-------------------|
| <b>Gains or losses</b>              |                   |                   |
| Trading securities .....            | 427.8             | 301.8             |
| Foreign exchange transactions ..... | 82.1              | 9.8               |
| Forward financial instruments ..... | 29.7              | (302.6)           |
| <b>Total</b> .....                  | <u>539.6</u>      | <u>9.0</u>        |

## 27 Gains or losses on available-for-sale securities

| (in millions of euros)                           | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| <b>Results for available-for-sale securities</b> |                   |                   |
| Gains or losses .....                            | 190.6             | 19.5              |
| Impairment .....                                 | 104.7             | (86.8)            |
| <b>Results for portfolio activity securities</b> |                   |                   |
| Gains or losses .....                            | 4.9               | –                 |
| Impairment .....                                 | (1.0)             | (0.1)             |
| <b>Total</b> .....                               | <u>299.2</u>      | <u>(67.4)</u>     |

## 28 General operating expenses

| (in millions of euros)   | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--|-------------------|-------------------|
| <b>Employee compensation and benefits</b>  |                   |                   |
| Salaries and wages, social security, taxes and levies on compensation <sup>1</sup> ..... | (813.7)           | (797.9)           |
| Pension expense .....  | (98.3)            | (96.9)            |
| Profit sharing .....   | (7.3)             | 2.5               |
| Incentive plan .....   | (26.3)            | 2.3               |
| <b>Compensation expense subtotal</b> .....   | <u>(945.6)</u>    | <u>(890.0)</u>    |
| <b>Other administrative expenses</b> .....   | <u>(478.9)</u>    | <u>(531.2)</u>    |
| <b>Total operating expenses</b> .....  | <u>(1,424.5)</u>  | <u>(1,421.2)</u>  |

<sup>1</sup> Including EUR 15 million for Executive Committee compensation and EUR 0.4 million in Directors' fees paid to Directors for 2012 and EUR 15.7 million for Executive Committee compensation and EUR 0.4 million in Directors' fees paid to Directors for 2011.

### 2010 share award plan

Allowance for this plan was 50 per cent released for a total amount of EUR 20.4 million against shares attribution for EUR 22.4 million.

### 2011 and 2012 share award plans

The final charge for HSBC France is not yet known as the attributed shares were not bought by the Trust. The allowance defined is hence accounted on a linear basis on the employees' grant acquisition period based on the quoted price as at 31 December 2012.

At 31 December 2012, allowance stood at EUR 18.5 million for the 2010 plan, at EUR 19 million on the 2011 plan and at EUR 5.6 million on the 2012 plan.

### 2013 share award plan

The allowance defined is hence accounted on a linear basis on the employees' grant acquisition period based on awarding hypothesis.

At 31 December 2012, allowance stood at EUR 4 million.

**Parent company financial statements** (continued)**29 Gains or losses on disposals of fixed assets**

| (in millions of euros)  | <u>31.12.2012</u> | <u>31.12.2011</u> |
|---|-------------------|-------------------|
| Gains or losses on held-to-maturity securities .....  | –                 | –                 |
| Gains or losses on tangible and intangible fixed assets <sup>1</sup> .....  | 9.4               | (1.3)             |
| Gains or losses on investments in subsidiaries and associates,<br>long-term securities and other group companies <sup>2</sup> ..... | 5.7               | (35.2)            |
| <b>Total</b> .....  | <u>15.1</u>       | <u>(36.5)</u>     |

1 In 2012, gains on disposal of 95 rue Réaumur, 75002 Paris for EUR 9.1 million. Non significant items in 2011.

2 In 2012, mainly a provision complement for HSBC Service (France) for EUR 1.66 million. In 2011, mainly an impairment on HSBC Private Wealth Managers for EUR 38.1 million.

**30 Corporate income tax**

| (in millions of euros)         | <u>31.12.2012</u> | <u>31.12.2011</u> |
|--------------------------------|-------------------|-------------------|
| <b>Current tax</b>             |                   |                   |
| At standard rate .....         | (116.5)           | 66.8              |
| At reduced rate .....          | –                 | –                 |
| <b>Deferred taxation</b> ..... | (91.1)            | 81.2              |
| <b>Total</b> .....             | <u>(207.6)</u>    | <u>148.0</u>      |

Note: Deferred tax is calculated according to the principles set out in Note 1 k on page 204.

The rates used for calculating taxes are:

| (in %)   | <u>Payable<br/>2013</u> | <u>Payable<br/>2012</u> | <u>Payable<br/>2011</u> |
|--|-------------------------|-------------------------|-------------------------|
| Standard rate .....  | 33.33                   | 33.33                   | 33.33                   |
| Reduced rate (PVL T gains rate) .....                      | 4.00                    | 3.33                    | 1.67                    |
| Reduced rate (gains on disposal of property to SIIC) ..... | 19.00                   | 19.00                   | 19.00                   |
| Reduced rate (common funds on risk placement) .....        | 15.00                   | 15.00                   | 15.00                   |
| <b>Tax contribution</b>                                    |                         |                         |                         |
| CSB .....  | 3.3                     | 3.3                     | 3.3                     |
| Exceptional contribution .....                             | 5                       | 5                       | –                       |
| <b>Deferred Taxation</b>                                   |                         |                         |                         |
| Standard rate on DT .....                                  | 33.33                   | 33.33                   | 33.3                    |
| Reduced rate on DT .....                                   | 4.00                    | 3.33                    | 1.67                    |
| <b>Tax contribution</b>                                    |                         |                         |                         |
| CSB .....  | 3.3                     | 3.3                     | 3.3                     |

A deferred tax asset for the carryforward of unused tax losses of EUR 88,9 million was recognised in 2011.

This deferred tax asset has been released in 2012 as associated tax losses have been fully matched with 2012 tax gains.

### **30 Corporate income tax (continued)**

#### **Tax group**

Since 2001, the parent company of the tax group has been HSBC Bank plc Paris branch.

In 2012, tax benefits allowed by HSBC Bank plc to the HSBC France group amounted to EUR 62.2 million. The proportion of benefits passed on to HSBC France was EUR 8.9 million.

In 2011, tax benefits allowed by HSBC Bank plc to the HSBC France group amounted to EUR 60.4 million. The proportion of benefits passed on to HSBC France was EUR 60.4 million.

These benefits are recognised in their entirety under the heading “Taxes”.

#### **Deferred tax in the balance sheet**

The net deferred tax receivable recognised in the balance sheet at 31 December 2012 was EUR 114.9 million compared with EUR 206 million at 31 December 2011.

At 31 December 2012 this receivable is made up of deferred tax assets of EUR 139.1 million against EUR 220 million at 31 December 2011 and a deferred tax liability of EUR 24.2 million compared with EUR 14 million at 31 December 2011.

### **31 Litigation**

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Various regulators and competition and enforcement authorities around the world including in the UK, the US, Canada, the EU, Switzerland and Asia, are conducting investigations and reviews related to certain past submissions made by panel banks and the processes for making submissions in connection with the setting of London interbank offered rates (“Libor”), European interbank offered rates (“Euribor”) and other benchmark interest and foreign exchange rates. Several of these panel banks have reached settlements with various regulatory authorities.

As a member of such panel for “Euribor”, HSBC France has been the subject of regulatory demands for information and is cooperating with those investigations and reviews. Based on the facts currently known, there is a high degree of uncertainty as to the resolution of these regulatory investigations and reviews, including the timing. The potential impact and size of any fines or penalties that could be imposed on HSBC France cannot be measured reliably.

As at 31 December 2012, there were no other litigation or arbitration proceedings likely to have a material impact on HSBC France’s financial position, its activities nor results.

## Parent company financial statements (continued)

### Statutory Auditors' report on the annual financial statements

*This is a free translation into English of the Statutory Auditors' report on the financial statements issued in French and it is provided solely for the convenience of English-speaking users. The Statutory Auditors' report includes information specifically required by French law in such reports, whether modified or not. This information is presented below the audit opinion on the financial statements and includes an explanatory paragraph discussing the Auditors' assessments of certain significant accounting and auditing matters. These assessments were considered for the purpose of issuing an audit opinion on the financial statements taken as a whole and not to provide separate assurance on individual account balances, transactions, or disclosures. This report also includes information relating to the specific verification of information given in the management report. This report should be read in conjunction with, and construed in accordance with, French law and professional auditing standards applicable in France.*

*Year ended 31 December 2012*

To the shareholders,

In compliance with the assignment entrusted to us by your Annual General Meeting, we hereby report to you, for the year ended 31 December 2012, on:

- the audit of the accompanying annual financial statements of HSBC France;
- the justification of our assessments;
- the specific verifications and information required by law.

These annual financial statements have been approved by the Board of Directors. Our role is to express an opinion on these annual financial statements based on our audit.

#### I - Opinion on the financial statements

We conducted our audit in accordance with professional standards applicable in France; those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit involves performing procedures, using sampling techniques or other methods of selection, to obtain audit evidence about the amounts and disclosures in the financial statements. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made, as well as 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 audit opinion.

In our opinion, the annual financial statements give a true and fair view of the assets and liabilities and of the financial position of the company as at 31 December 2012 and of the results of its operations for the year then ended in accordance with French accounting principles.

#### II - Justification of our assessments

In accordance with the requirements of article L. 823-9 of the French Commercial Code (*Code de Commerce*) relating to the justification of our assessments, we bring to your attention the following matters:

- your company accounts for impairment losses to cover the credit and counterparty risks inherent to its activities (Note 1 c to the company financial statements). We have reviewed the control procedures relating to credit and counterparty risk monitoring, the assessment of risks of non-recoverability and the calculation of the individual impairment;
- your company holds positions in securities and financial instruments (Notes 1 b, 1 h and 1 i to the company financial statements). We have examined the control procedures for the accounting classification of these positions and for determining the parameters used to value them. We have verified the appropriateness of the accounting policies selected by your company and have satisfied ourselves that they are applied correctly;
- your company recognizes provisions to cover risks and litigations related to its activity (Notes 1 d and 3 1 to the company financial statements). We have examined the methodology used to measure these provisions, as well as the main assumptions applied.

These assessments were made as part of our audit of the annual financial statements taken as a whole, and therefore contributed to the opinion we formed which is expressed in the first part of this report.

### III - Specific verifications and information

We have also performed, in accordance with professional standards applicable in France, the specific verifications required by French law.

We have no matters to report as to the fair presentation and the consistency with the annual financial statements of the information given in the management report of the Board of Directors, and in the documents addressed to shareholders with respect to the financial position and the annual financial statements.

Concerning the information given in accordance with the requirements of article L. 225-102-1 of the French Commercial Code (“*Code de commerce*”) relating to remunerations and benefits received by the directors and any other commitments made in their favour, we have verified its consistency with the annual financial statements or with the underlying information used to prepare these annual financial statements and, where applicable, with the information obtained by your company from companies controlling your company or controlled by it. Based on this work, we attest the accuracy and fair presentation of this information.

Paris-La Défense and Paris, on 12 April 2013

KPMG Audit FS II  
Pascal Brouard  
*Partner*

BDO France – Léger & Associés  
Michel Léger  
*Partner*

## HSBC France's principal subsidiaries and investment policy

### HSBC France group's principal subsidiaries at 31 December 2012

#### Commercial Banking

**Distribution** HSBC Factoring (France) (100%)

#### Global Banking and Markets

**Real estate** Foncière Elysées SA (100%)  
HSBC Real Estate Leasing (France) (100%)

**Structures financing  
and Global Banking** HSBC SFH (France) (100%)  
Société Financière et Mobilière (100%)  
HSBC Leasing (France) (100%)  
HSBC Leasing (Belgium) (100%)  
CCF Charterhouse GmbH (100%)

**Markets** Financière d'Uzès (34%)

#### Asset Management

**France** HSBC Global Asset Management (France) (100%)  
HSBC Epargne Entreprise (France) (100%)  
HSBC REIM (France) (100%)

**Outside France** HSBC Global Asset Management (Switzerland) (50%)

#### Subsidiaries and equity investments

**France** Valeurs Mobilières Elysées (100%)  
Société Française et Suisse (100%)  
Société Immobilière Malesherbes Anjou (100%)  
Excofina (100%)

**Outside France** Charterhouse Management Services Ltd (100%)

- Stated percentages indicate the group's percentage of control.
- The subsidiaries are classified in the area where they principally operate.

## Summary business activities of HSBC France group's principal subsidiaries at 31 December 2012

### Commercial Banking

(in thousands of euros)

|                                | Total assets   |           | Shareholders' funds* |        | Net profit   |       | HSBC France group's percentage holding |       |
|--------------------------------|--|-----------|----------------------|--------|--------------|-------|--|-------|
|                                | 2012   | 2011      | 2012                 | 2011   | 2012         | 2011  | 2012                                   | 2011  |
| <b>HSBC Factoring (France)</b> | <b>1,658,809</b>   | 1,115,984 | <b>62,512</b>        | 20,086 | <b>8,426</b> | 5,708 | <b>100.0</b>                           | 100.0 |
|                                | <p>HSBC Factoring (France) saw growth of 37 per cent in 2012, with gross turnover of EUR 7.7 billion, corresponding to the amount of factored receivables. Net operating income rose by 17 per cent to EUR 27.6 million, the Risk Weighted Assets amounted to EUR 611 million, costs were reduced by 7 per cent between 2011 and 2012, the provision rate was below the standards of the profession to 0.020 per cent and the pre-tax contribution to group profit came to EUR 12.9 million. HSBC Factoring (France) benefited, in particular, from the following growth drivers in 2012:</p> <ul style="list-style-type: none"> <li>- market share of 4.1 per cent in France at end of 2012;</li> <li>- strengthening international activity (import and export), cross-border revenue generated within the Group and coordination;</li> <li>- obtaining ISO 9001 certification in 2012, which became effective in May 2012;</li> <li>- continuing work on optimising Return on Risk Weighted Assets (RoRWA), to reach 2 per cent at 31 December 2012;</li> <li>- improving profitability, with a target of reducing the cost efficiency ratio;</li> <li>- stepping up business development with major clients;</li> <li>- rolling out the "Risks and Structured Products" division;</li> <li>- making a share capital increase, in accordance with the ACP's recommendation;</li> <li>- launching the "Pegasus" financial back office project (Group Service Centre in Poland);</li> <li>- completing the implementation of all recommendations made as a result of the ACP audit.</li> </ul> <p>At 31 December 2012, the cost efficiency ratio amounted to 47 per cent compared with 59 per cent in 2011.</p> |           |                      |        |              |       |  |       |

### Global Banking and Markets

(in thousands of euros)

|  |   |           |                |         |                 |          |              |       |
|--|---|-----------|----------------|---------|-----------------|----------|--------------|-------|
| <b>HSBC SFH (France)</b>                 | <b>2,137,616</b>  | 2,126,424 | <b>55,296</b>  | 48,395  | <b>150</b>      | 254      | <b>100.0</b> | 100.0 |
|  | <p>HSBC SFH (France) is a company dedicated to refinancing HSBC France by issuing covered bonds secured by home loans (cover pool). HSBC SFH (France) launched its first issue on 20 January 2010 for an amount of EUR 1.5 billion, followed by three issues of CHF 200 million each, in the same year. At 31 December 2012, issues totalled EUR 1.9 billion against a cover pool of EUR 3.9 billion.</p> |           |                |         |                 |          |              |       |
| <b>HSBC Leasing (France)</b>             | <b>1,911,015</b>  | 1,899,309 | <b>189,066</b> | 200,405 | <b>(11,339)</b> | (13,172) | <b>100.0</b> | 100.0 |
|  | <p>HSBC Leasing (France) specialises in lease finance for major corporates. The company holds subsidiaries intended for leasing activities with a call option. It operates more particularly in the aeronautics sector by financing assets on behalf of airlines. The equity interests in 2012 totalling EUR 1.79 billion, on a par with 2011.</p>  |           |                |         |                 |          |              |       |
| <b>HSBC Real Estate Leasing (France)</b> | <b>1,182,360</b>  | 1,015,540 | <b>73,073</b>  | 65,858  | <b>7,214</b>    | 5,681    | <b>100.0</b> | 100.0 |
|  | <p>In 2012, the gross lending of this real estate leasing specialist subsidiary amounts to EUR 372 million. This gross lending, the control of cost of risk and the operating expenses reduction, allow a significant increase in net profit.</p>   |           |                |         |                 |          |              |       |

### Asset Management

(in thousands of euros)

|  |  |         |               |         |               |        |              |       |
|--|--|---------|---------------|---------|---------------|--------|--------------|-------|
| <b>HSBC Global Asset Management (France)</b> | <b>164,399</b>   | 186,664 | <b>90,259</b> | 108,848 | <b>15,048</b> | 66,128 | <b>100.0</b> | 100.0 |
|  | <p>In 2012, the reorganisation of the legal entities comprising the Asset Management business continued, in line with the strategy defined for the global business line aiming to leverage the HSBC brand. HSBC Global Asset Management (France), HSBC Private Wealth Managers and HSBC Global Asset Management Financial Services were merged on 31 October, effective retroactively from 1 January 2012.</p> <p>In addition, the difficult economic environment in the past few years has revealed the limitations of the current organisation of HSBC's Asset Management business in France, which has had to reorganise in order to pursue its development. This reorganisation of the Asset Management activities and support functions was the subject of a social process in July 2012.</p> <p>The sharp decrease in statutory net profit was due mainly to mergers and disposals made during 2011, which had led to significant non-recurring income in that year.</p> <p>Excluding these exceptional items, profit before tax was nonetheless down significantly, reflecting the full year impact of the decline in new inflows and the fall in the markets due to the eurozone crisis, which has put a strong brake on assets under management and therefore revenue since mid-2011. Assets managed and distributed amounted to EUR 67.6 billion compared with EUR 69.9 billion at end 2011, a decrease of 12 per cent. The decrease was due to net outflows of EUR 7.7 billion which was partially offset by a positive value effect of EUR 5.4 billion.</p> <p>In the institutional customer segment, money market funds (EUR 3.9 billion) and the termination of two mandates (EUR 2.0 billion) accounted for most of the net outflows whilst fixed-income funds continued to grow, especially credit, high yield and emerging debt funds. In the retail customer segment, Wealth Management, through the Retail Banking and Wealth Management network, made a positive contribution to growth, whilst the external distribution networks proved more restrained in terms of equity-based products but enjoyed some major inflows in European and emerging fixed-income products. All retail customer segments, both in terms of distribution networks (Retail Banking and Wealth Management, Private Banking, Commercial Banking and external distribution networks) and geographical areas (France, Benelux, Southern and Northern Europe), continued to make sustained efforts.</p> <p>In 2012, HSBC Global Asset Management (France) continued to invest in making its systems and processes more robust and mutualised, as well as improving its risk control.</p> |         |               |         |               |        |              |       |

\* Before net profit appropriation.

## HSBC France's principal subsidiaries and investment policy (continued)

### Asset Management (continued)

(in thousands of euros)

|   | Total assets  |        | Shareholders' funds* |        | Net profit     |       | HSBC France group's percentage holding |       |
|---|---|--------|----------------------|--------|----------------|-------|--|-------|
|   | 2012  | 2011   | 2012                 | 2011   | 2012           | 2011  | 2012                                   | 2011  |
| <b>HSBC Epargne Entreprise (France)</b> | <b>59,464</b>   | 75,623 | <b>38,005</b>        | 42,316 | <b>(1,442)</b> | 689   | <b>100.0</b>                           | 100.0 |
|   | <p>HSBC Epargne Entreprise (France), a credit institution specialising for the HSBC Group in France in holding employee savings accounts and a wholly-owned subsidiary of HSBC France, has a clientele of 9,200 companies and manages 560,000 personal accounts. The employee savings funds it offers are managed by HSBC Global Asset Management (France), with assets under management totalling EUR 3.9 billion at 31 December 2012. At 30 June 2012, assets under management stood at EUR 3.7 billion, making the Group the seventh-largest employee savings company. Its products are distributed either directly or via the HSBC Group distribution network in France and partner networks, covering the needs of companies of all sizes.</p>   |        |                      |        |                |       |  |       |
| <b>HSBC REIM (France)</b>               | <b>16,436</b>   | 13,474 | <b>10,066</b>        | 7,094  | <b>4,972</b>   | 3,824 | <b>100.0</b>                           | 100.0 |
|   | <p>HSBC REIM (France) is the Asset Management subsidiary specialising in real estate management for third parties. At 31 December 2012, the market value of assets under management was EUR 1.4 billion. The main fund managed, Elysées Pierre, with 124 properties, is a SCPI real estate investment trust invested primarily in offices in the Paris region. The fund has a yield-based strategy, which over the last five years has resulted in a growing or steady annual dividend. Net inflows reached a record EUR 244 million in 2012, reflecting investor confidence.</p> <p>Net profit of HSBC REIM (France) grew by 30 per cent compared with 2011. 59 per cent of its net operating income of EUR 13.8 million came from recurring commission income for property management services and 41 per cent from commission income within the framework of the capital increases of its non-trading property company (SCPI) Elysées Pierre, now an investment company with variable capital.</p> |        |                      |        |                |       |  |       |

### Own investments

(in thousands of euros)

|  |   |         |                |         |              |        |              |       |
|--|---|---------|----------------|---------|--------------|--------|--------------|-------|
| <b>Société Française et Suisse (SFS)</b>           | <b>10,492</b>   | 10,474  | <b>10,484</b>  | 10,445  | <b>39</b>    | 868    | <b>100.0</b> | 100.0 |
|  | <p>In 2012, Société Française et Suisse posted a profit of EUR 38,516.67, sharply down compared with 2011 (which had been marked by the sale of the entire line of Swiss Life Holding shares and the complete transfer of the assets and liabilities of S.G.E.F.F.). The profit in 2012 is largely due to the investment of cash. The balance, amounting to EUR 10,492 thousand, is mainly composed of two assets: cash (almost EUR 8,700 thousand) and financial assets (just over EUR 1,800 thousand).</p>  |         |                |         |              |        |              |       |
| <b>Valeurs Mobilières Elysées (Formerly Nobel)</b> | <b>172,153</b>  | 202,563 | <b>154,780</b> | 183,055 | <b>9,795</b> | 23,285 | <b>100.0</b> | 100.0 |
|  | <p>Valeurs Mobilières Elysées is a subsidiary in which are registered investments for own account of the HSBC Group in France. These investments include listed midcaps and private equity funds. The HSBC Group has decided in 2009 not to take new operations, therefore Valeurs Mobilières Elysées manages a portfolio gradually declining. The total assets of the Private Equity and listed securities totalised EUR 150 million in January 2012 and account for only EUR 125 million at the end of December 2012. Capital gains realised amount to EUR 6.2 million on the funds and EUR 6.8 million on the listed values.</p> |         |                |         |              |        |              |       |

### Other subsidiary of the HSBC Group in France

(in thousands of euros)

|                                     |  |            |                |         |               |        |                          |                    |
|-------------------------------------|--|------------|----------------|---------|---------------|--------|--------------------------|--------------------|
| <b>HSBC Assurances Vie (France)</b> | <b>19,608,962</b>  | 18,498,839 | <b>615,358</b> | 576,468 | <b>46,643</b> | 40,966 | <b>100.0<sup>1</sup></b> | 100.0 <sup>1</sup> |
|                                     | <p>HSBC Assurances Vie (France)'s gross reinsurance premiums amounted to EUR 2.2 billion, down 8 per cent compared with 2011. The gross technical reserves in euros rose 3.6 per cent (EUR 15 billion), and those in unit-linked products increased by 9 per cent (EUR 2.6 billion). Estimated net profit totalled EUR 46.6 million at 31 December 2012 (up 13.9 per cent compared to 2011).</p> |            |                |         |               |        |                          |                    |

\* Before net profit appropriation.

<sup>1</sup> 100% held by HSBC Bank plc Paris Branch.



## Investment policy

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### 2008

- Disposal by HSBC France of its regional banking subsidiaries (Société Marseillaise de Crédit, Banque de Savoie, Banque Chaix, Banque Marze, Banque Dupuy, de Parseval, Banque Pelletier and Crédit Commercial du Sud-Ouest).  
Proceeds: EUR 2,100 million.
- Disposal by HSBC France of its participation in Altadis.  
Proceeds: EUR 66.3 million.
- Subscription by HSBC France to capital increase made by HSBC Covered Bonds (France).  
Cost: EUR 28 million.
- Subscription by HSBC France of 9.43 per cent of Société de Financement de l'Economie Française capital.  
Cost: EUR 4.7 million.
- Subscription by HSBC France to capital increase made by HSBC Financial Products (France).  
Cost: EUR 75 million.
- Disposal by HSBC France of its participation in BIAT.  
Proceeds: EUR 8.6 million.

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### 2009

- Subscription by HSBC France to capital increase made by HSBC Financial Products (France).  
Cost: EUR 75 million.
- Disposal by HSBC France of its participation in Visa.  
Proceeds: EUR 2.8 million.
- Disposal of Swiss Life shares by SFS.  
Proceeds: EUR 13.6 million.

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### 2010

- Disposal by HSBC France of its fund depositary and custodial activities and its subsidiary HSBC Securities Services (France).  
Proceeds: EUR 8 million.
- Disposal by HSBC France of its participation in Servair.  
Proceeds: EUR 3.3 million.
- Capital decrease of Nobel.  
Proceeds: EUR 46.9 million.

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### 2011

- Acquisition by HSBC France of 5.26 per cent of Citizen Capital.  
Cost: EUR 1 million.
- Disposal by Sinopia Asset Management, a wholly-owned subsidiary of HSBC France, of 100 per cent of Sinopia Asset Management (Asia Pacific) Limited to HSBC Global Asset Management (Hong Kong) Limited.  
Proceeds: EUR 17.5 million.
- Disposal by Sinopia Asset Management, a wholly-owned subsidiary of HSBC France, of 100 per cent of Sinopia Asset Management (UK) Limited to HSBC Global Asset Management (UK) Limited.  
Proceeds: EUR 9.7 million.
- Subscription by HSBC France to capital increase made by HSBC Trinkaus Gesellschaft für Kapitalmarktinvestments oHG.  
Cost: EUR 145 million.
- Subscription by HSBC France to two capital increases made by HSBC Trinkaus Gesellschaft für Bankbeteiligungen oHG.  
Cost: EUR 135 million and EUR 35 million.
- Subscription by HSBC France to capital increase made by HSBC SFH (France).  
Cost: EUR 20 million.
- Capital decrease of Charterhouse Management Services Limited.  
Proceeds: GBP 15 million.

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### 2012

- Subscription by HSBC France to capital increase made by HSBC Factoring (France).  
Cost: EUR 34 million.
- Subscription by HSBC France to capital increase made by HSBC SFH (France).  
Cost: EUR 6.7 million.
- Capital decrease of SAF Palissandre.  
Proceeds: EUR 458.4 million.
- Increase by HSBC France of its participation in Oséo SA capital.  
Cost: EUR 1.3 million.

## Other legal documents relating to the Annual General Meeting to be held on 30 April 2013

### Agreements governed by article L. 225-38 of the French Commercial Code

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Article L. 225-38 of the French Commercial Code requires that any agreement entered into directly or indirectly between a company and one of its Directors or Chief Executives, or between a company and one of its shareholders owning at least 10 per cent of the voting rights, or, in the case of a corporate shareholder, the company which controls it, must first be authorised by the Board of Directors and subsequently approved at the Annual General Meeting of shareholders. It also prohibits certain types of agreement between those parties, such as loans or guarantees.

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#### Agreements entered into in 2012

A new agreement subject to the provisions of article L. 225-38 of the French Commercial Code and approved by the HSBC France's Board of Directors during its meeting on 10 January 2012, was entered into in 2012.

This agreement, between HSBC France and Mr Christophe de Backer, sets out the terms and conditions regarding the resignation of Mr de Backer from his position as Chief Executive Officer of HSBC France. In particular, it specifies, pursuant to the Group rules, that no bonus will be paid to Mr de Backer with respect of the 2011 year and that his pension rights, under the defined benefits supplementary pension scheme for the Executive Directors of HSBC France, are lost.

It also stipulates the retention of the benefit of unvested shares and stock-options not yet exercised at his resignation date, subject to the non-solicitation of HSBC France high-net-worth and Private Banking clients and critical staff, for a period of one year following his resignation.

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#### Agreements entered into in prior years and still in force and effect during 2012

Three agreements entered into in 2001 by HSBC France and its direct 99.99 per cent shareholder, HSBC Bank plc Paris Branch, remained in full force and effect during 2012. These were a pooling of resources agreement designed to provide the parties with various services relating to their activities at cost, an agreement for the provision of services covering various activities and a group tax relief agreement.

The agreement entered into in 2003 with HSBC Bank plc, regarding the invoicing of services covering market activities of the HSBC France group, remained in full force and effect during 2012.

The agreement entered into in 2005 with HSBC Holdings plc and HSBC Bank plc, regarding services provided by their central departments, also remained in full force and effect during 2012.

The "Group Software" agreement entered into in 2006 with HSBC Holdings plc, HSBC France and other companies of the HSBC Group, remained in full force and effect during 2012 regarding the share of the IT development expenses engaged by the HSBC Group.

The agreement renewed in 2007 between HSBC Holdings plc and HSBC France, giving HSBC France and its subsidiaries free use of the HSBC brand, remained in full force and effect during 2012.

The agreement entered into in 2009, and confirming decisions previously adopted by the Board of Directors, concerning the supplementary defined benefit pension scheme for Senior Executives of HSBC France, remained in full force and effect during 2012.

The agreement entered into in 2009 with HSBC Global Asset Management (France), regarding the delegation of financial management of asset management mandates allocated by clients of the HSBC France network to HSBC Global Asset Management (France), came into effect on 1 January 2010 and remained in full force and effect during 2012.

## **Statutory Auditors' report on regulated agreements and commitments**

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*This is a free translation into English of a report issued in French and provided solely for the convenience of English-speaking readers. This report should be read in conjunction with, and is construed in accordance with, French law and professional auditing standards applicable in France.*

*Year ended 31 December 2012*

To the shareholders,

In our capacity as Statutory Auditors of your company, we hereby report on certain related party agreements and commitments.

We are required to inform you, on the basis of the information provided to us, of the terms and conditions of those agreements and commitments indicated to us, or that we may have identified in the performance of our engagement. We are not required to comment as to whether they are beneficial or appropriate or to ascertain the existence of any such agreements and commitments. It is your responsibility, in accordance with article R. 225-31 of the French Commercial Code ("*Code de commerce*"), to evaluate the benefits resulting from these agreements and commitments prior to their approval.

In addition, we are required, where applicable, to inform you in accordance with article R. 225-31 of the French Commercial Code ("*Code de commerce*") concerning the implementation of the agreements and commitments already approved by the General Meeting of the Shareholders.

We performed those procedures which we considered necessary to comply with professional guidance issued by the National Auditing body ("*Compagnie nationale des Commissaires aux comptes*") relating to this type of engagement.

### **I - Agreements and commitments submitted for approval by the General Meeting of Shareholders**

#### **Agreements and commitments allowed during the fiscal year**

In accordance with the article R. 255-38 of the French Commercial Code ("*Code de commerce*"), we hereby inform you that we have been advised of the following agreements and commitments already approved by the General Meeting of the Shareholders.

*With Mr Christophe de Backer*

The agreement establishes the terms and conditions of Mr de Backer's resignation as Chief Executive Officer of HSBC France. It states, in particular, that in accordance with the Group's policies, Mr de Backer will not receive any bonuses for the year 2011 and will lose the supplementary defined benefit pension scheme for Senior Executive of HSBC France.

Furthermore, this agreement states that Mr de Backer preserves his shares and stock options not vested at the time of his resignation, as long as he does not, for one year from the date of his resignation, solicit any HSBC France Private Banking customers, as well as any individual occupying a critical position within HSBC France.

This agreement was approved by the Board of Directors on 10 January 2012.

### **II - Agreements and commitments already approved by the General Meeting of Shareholders**

#### **Continuing agreements and commitments which were entered in the prior years**

In accordance with article R. 225-30 of the French Commercial Code ("*Code de commerce*"), we were informed that the following agreements, which were entered into in prior years, have continued during the year.

*Agreements and commitments relating to the supplementary defined benefit pension scheme for Senior Executives*

The agreement, adopted in 2009, confirmed the decisions previously adopted by the Board of Directors concerning the updating of the rules governing the supplementary defined benefit pension scheme for four Senior Executives of CCF, subsequently HSBC France, as well as the payment of these supplementary pensions to Charles-Henri Filippi and Gilles Denoyel. Christophe de Backer has lost the benefit on 10 January 2012 as indicated above.

With respect to this agreement, an additional provision for pension commitments has been recorded in HSBC France accounts at 31 December 2012 for EUR 1.4 million.

## Other legal documents relating to the Annual General Meeting to be held on 30 April 2013 (continued)

### *With HSBC Holdings plc*

- Head-office costs agreement: services provided by central departments of HSBC Holdings plc are invoiced to HSBC France with respect to the agreement settled in 2005. With respect to this agreement, the invoices represented a charge of GBP 10.1 million in 2012.
- “Group Software” agreement: HSBC Holdings plc invoices the expenses engaged by the Group regarding IT developments, in accordance with the agreement entered into in 2006. With respect to this agreement, a charge of USD 19 million has been recorded in 2012.
- Agreement renewed in 2007 and giving HSBC France and its subsidiaries the free use of the HSBC brand.

### *With HSBC Bank plc*

- Head-office costs agreement: services provided by central departments of HSBC Bank plc are invoiced to HSBC France with respect to the agreement settled in 2005. This agreement had no financial impact in 2012.
- Service level agreement for all market activities of HSBC France group: HSBC Bank plc invoices to HSBC France services covering all the market activities in accordance with the agreement settled in 2003. This agreement had no financial impact in 2012.

### *With HSBC Bank plc Paris Branch*

Three agreements have been entered into during 2001 by HSBC France and HSBC Bank plc Paris Branch and remained in full force and effect during 2012:

- a group wide service agreement for the purpose of rendering services to its members at cost concerning diverse activities of the two entities;
- service level agreement issued by HSBC France to HSBC Bank plc Paris Branch concerning various activities.

With respect to these two agreements, the income recorded for 2012 amounted to EUR 17.2 million;

- tax integration agreement between HSBC Bank plc Paris Branch and HSBC France. With respect to this agreement, a tax income of EUR 8.9 million has been recorded in 2012.

### *With HSBC Global Asset Management (France)*

Agreement approved in 2009 and effective from 1 January 2010 regarding the delegation to HSBC Global Asset Management (France) of financial management of asset management mandates allocated by clients of the HSBC France network. With respect to this agreement, a charge of EUR 3.6 million has been recorded in 2012.

Paris-La Défense and Paris, on 12 April 2013

KPMG Audit FS II  
Pascal Brouard  
*Partner*

BDO France – Léger & Associés  
Michel Léger  
*Partner*

## Proposed resolutions to the Combined General Meeting

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### First resolution

Voting under the quorum and majority conditions to transact ordinary business, and having heard and considered the report of the Directors, the Statutory Auditors' report on the financial statements for the year ended 31 December 2012, and the Chairman's and the Statutory Auditors' reports on corporate governance, internal control and risk management procedures, the shareholders hereby approve the company's financial statements for that year as presented, together with the business operations reflected therein and summarised in the reports.

### Second resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby approve the following proposed distribution of net profit for the year:

|  |                     |
|--|---------------------|
| Net profit for the year .....                | EUR601,189,983.50   |
| Plus retained profits .....                  | EUR2,785,467,451.71 |
| Total sum available<br>for distribution..... | EUR3,386,657,435.21 |

To be distributed as follows:

|   |                     |
|---|---------------------|
| Dividend of EUR3.56<br>per share to be paid ..... | EUR240,078,664.12   |
| Retained earnings .....                           | EUR3,146,578,771.09 |

According to the decision of the Board of Directors on 27 February 2013, an interim dividend amounting to EUR 3.56 per share has already been paid to the 67,437,827 shares issued at that date, for a total amount of EUR 240,078,664.12. As this interim dividend is equal to the total amount of the dividend, no final payment will be made.

Dividend paid is eligible for the tax deduction referred to in article 158 paragraph 3.2 of the General Tax Code.

The shareholders duly note that dividends paid in respect of the three previous financial years were as follows:

| Year      | Net dividend per share |
|-----------|------------------------|
| 2009..... | EUR9.94                |
| 2010..... | EUR10.67               |
| 2011..... | EUR1.75                |

Dividends paid in respect of the three previous years are eligible for the tax deduction referred to in article 158 paragraph 3.2 of the General Tax Code.

### Third resolution

Voting under the quorum and majority conditions to transact ordinary business, and having heard and considered the report of the Directors and the report of the Statutory Auditors regarding the consolidated statements for the year ended 31 December 2012, the shareholders hereby approve the consolidated financial statements for that year as presented.

### Fourth resolution

Voting under the quorum and majority conditions to transact ordinary business, and having heard and considered the Statutory Auditors' report on regulated agreements governed by article L. 225-38 of the French Commercial Code, the shareholders hereby approve successively the agreements described therein under the conditions referred to in article L. 225-40 of said Code.

### Fifth resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby ratify the Board's co-optation on 22 November 2012 of Mr Samir Assaf to replace Mr Stuart Gulliver, who has resigned, for the remainder of the term of office of his predecessor, that is until the conclusion of the Annual General Meeting held to adopt the financial statements for the year ending 31 December 2015.

### Sixth resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby ratify the Board's co-optation on 27 February 2013 of Mr Lindsay Gordon to replace Mr Peter Boyles, who has resigned, for the remainder of the term of office of his predecessor, that is until the conclusion of the Annual General Meeting held to adopt the financial statements for the year ending 31 December 2012.

### Seventh resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby re-elect Mr Lindsay Gordon, who is retiring by rotation, as Director.

Subject to the adoption of the twelfth resolution setting three-year term of office of Directors elected or re-elected, the term of office of Mr Lindsay Gordon will end at the conclusion of the Annual General Meeting held to approve the financial statements for the year ending 31 December 2015.

### Eighth resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby re-elect Mr Thierry Moulouguet, who is retiring by rotation, as Director.

Subject to the adoption of the twelfth resolution setting three-year term of office of Directors elected or re-elected, the term of office of Mr Thierry Moulouguet will end at the conclusion of the Annual General Meeting held to approve the financial statements for the year ending 31 December 2015.

### Ninth resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby re-elect Mr Peter Shawyer, who is retiring by rotation, as Director.

Subject to the adoption of the twelfth resolution setting three-year term of office of Directors elected or re-elected, the term of office of Mr Peter Shawyer will end at the conclusion of the Annual General Meeting held to approve the financial statements for the year ending 31 December 2015.

## Other legal documents relating to the Annual General Meeting to be held on 30 April 2013 (continued)

### Tenth resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders hereby re-elect Mr Jacques Veyrat, who is retiring by rotation, as Director.

Subject to the adoption of the twelfth resolution setting three-year term of office of Directors elected or re-elected, the term of office of Mr Jacques Veyrat will end at the conclusion of the Annual General Meeting held to approve the financial statements for the year ending 31 December 2015.

### Eleventh resolution

Voting under the quorum and majority conditions to transact ordinary business, the shareholders duly note that Mr Marcel Roulet, who is retiring by rotation, is not standing for re-election.

### Twelfth resolution

Voting under the quorum and majority conditions required to transact special business, the shareholders decide to bring back to three-year term of office of Directors elected or re-elected in their mandates from 30 April 2013.

As a result, the shareholders decide to amend the last paragraph of article 10 of the Company's Articles of Association that will be drafted as follows, the rest of the article remaining unchanged:

*"ARTICLE 10 - BOARD OF DIRECTORS*

*(.../...)*

*Directors' term in office is three (3) years for Directors appointed or renewed in their duties as from 30 April 2013, the other terms in office of Directors underway on this date remaining unchanged to four years."*

### Thirteenth resolution

Voting under the quorum and majority conditions required to transact special business, the shareholders hereby authorise the Board of Directors to increase the share capital on one or more occasions at the time or times it deems appropriate up to a maximum amount of EUR 100 million, it being stipulated that this sum does not include capital increases made in respect of scrip dividend payments or upon exercise of stock options by employees.

Should the Board of Directors decide to use this authority, it may implement the capital increase at its discretion either by capitalising earnings, reserves or share premiums by means of an increase in the nominal value of existing shares or by means of a bonus issue of new shares identical in all respects to the existing shares, or by issuing new shares for cash or by way of a set-off, with pre-emptive rights in favour of existing shareholders, or by a combination of both procedures either successively or simultaneously.

In the event of a capital increase by issuing new shares for cash, the Board of Directors is specifically authorised to:

1. give those shareholders who applied for a greater number of shares than their entitlement as of right preference over any securities not taken up under the shareholders' pre-emptive rights, scaled back in the event that applications exceed the number of shares available;

2. limit the capital increase to the amount of applications received, provided that such amount represents at least three quarters of the initial proposed capital increase.

The shareholders hereby empower the Board of Directors to complete the capital increase or increases, if it deems appropriate, to fix the terms and conditions thereof and notably the issue price of the shares, the dividend entitlement date, which may be retrospective, and the opening and closing dates for applications, to officially record the capital increase and alter the Articles of Association accordingly, and, more generally, to take all measures and fulfil all formalities required to complete the operation.

This authority is valid for a period of 26 months with effect from the date of this meeting. It cancels and supersedes the authority granted at the Annual General Meeting held on 4 May 2011.

### Fourteenth resolution

Voting under the quorum and majority conditions to transact special business, and having heard and considered the report of the Directors and the special report of the Statutory Auditors, and in accordance with the provisions of article L. 225-129-6, indents 1 and 2 of the French Commercial Code, the shareholders hereby authorise the Board of Directors to increase the share capital, in one or several steps at its sole discretion, by issuing shares to be subscribed in cash reserved for participants in the company's employee share ownership plan in accordance with the provisions of article L. 3332-18 of the French Labour Code.

The shareholders set the maximum increase in the share capital at EUR 10 million.

The shareholders expressly renounce their pre-emptive subscription right with respect to new shares issued for the benefit of participants in the company's employee share ownership plan.

This authority shall extend for two years from the date of this General Meeting.

The shareholders grant full powers to the Board of Directors to decide all terms and conditions of the issuance transactions to be made, in particular the issue price of the new shares. The shareholders also grant the Board full powers to recognise the capital increase or increases effected under this authority, to amend the articles of association accordingly and generally to do what is necessary.

### Fifteenth resolution

Voting under the quorum and majority conditions to transact ordinary and special business, the shareholders hereby confer full powers on the bearer of an original, copy or abstract of the minutes of this meeting for the purpose of completing any formalities required by law.

## Information on HSBC France and its share capital

### Information on the company

#### Name

HSBC France.  
New name of CCF since 1 November 2005.

#### Commercial name

HSBC since 1 November 2005 and, for the Private Banking business, HSBC Private Bank since 31 October 2011.

#### Date of incorporation

1894.

#### Registered office

103 avenue des Champs-Élysées – 75008 Paris – France.

#### Legal Form

*Société Anonyme* incorporated under the laws of France, governed notably by the French Commercial Code. The company is a credit institution and authorised bank, and as such is also governed by the French Monetary and Financial Code.

#### Term

The company's term ends on 30 June 2043, unless previously wound up or extended.

#### Corporate purpose (article 3 of the Articles of Association)

The company's corporate purpose is the transaction in all countries of any and all banking, finance, lending, guarantee, trading, brokerage or fee-earning business together with the provision of any and all investment services and related services within the meaning of articles L. 321-1 and L. 321-2 of the Monetary and Financial Code, and more generally, to conduct within the limits permitted by law any and all commercial, industrial or agricultural, securities or real estate, financial or other operations as well as to provide any and all services directly or indirectly connected with or which may facilitate the achievement of the foregoing object.

#### Trade and companies Register and APE code

775 670 284 RCS Paris – APE 6419Z.

#### Legal and regulatory framework

Subject to the laws and regulations relating to credit institutions, including articles in the French Monetary and Financial Code applicable to them, the company is governed by commercial law, including articles L. 210-1 and following of the French Commercial Code and its Articles of Association.

HSBC France is a credit institution licensed as a bank. As such, the company may conduct all banking operations. It is, moreover, authorised to perform any services or related investment mentioned in articles L. 321-1 and L. 321-2 of the French Monetary and Financial Code, with the exception of operating a multilateral trading facility. In its capacity as provider of investment services, it is subject to the regulations applicable to them under the supervision

of the *Autorité des marchés financiers*. It is particularly subject to compliance with a number of prudential rules and controls by prudential authorities. Its Senior Management and all the people it employs are bound by professional secrecy, violation of which is punishable by law. It is also an insurance broker.

#### Documents and information on display

Any person requiring additional information on the HSBC France group may, without commitment, request documents by mail from:

HSBC France – 103, avenue des Champs-Élysées, 75419 Paris Cedex 08, France.

#### Financial year

From 1 January to 31 December.

#### Distribution of profits

A minimum of 5 per cent of the net profit for the year, less any prior year losses, is transferred to the legal reserve until such time as it has reached one tenth of the company's share capital and at any time after that should it fall back below the minimum requirement.

The balance, plus any retained earnings, less any sums which the shareholders deem expedient to transfer to new or existing reserves or to retained earnings, comprises the profit available for distribution among the shareholders.

However, except in the event of a reduction of the company's share capital, no distribution may be made if total shareholders' funds are, or would as a result, become lower than the amount of the company's share capital plus any non-distributable reserves.

By way of derogation to the provisions of this article, sums may be transferred to a special employee profit-sharing reserve, as provided for by law.

#### Form of shares

Shares have to be registered. They result in registration on an individual account pursuant to the conditions and according to the methods stipulated by the legal and regulatory provisions in force.

#### Voting rights

Each fully paid up share entitles the holder to one vote.

#### Transfer of shares

The transfer of shares takes place by way of a transfer from one account to another.

There are no restrictions on disposals of shares or negotiable securities giving access to the share capital in cases of inheritance or liquidation of matrimonial property, or on disposals to a spouse, descendant or ascendant.

Similarly, there are no restrictions on disposals of shares to natural or legal persons appointed as Directors, subject to the number of shares provided by article 11 of these Articles of Association.

## Information on HSBC France and its share capital (continued)

Any other disposals or transfers of shares or negotiable securities giving access to the capital, including between shareholders, whether free of charge or for valuable consideration, whether the said disposals or transfers take place by way of donation, exchange, disposal, capital contribution, merger, demerger, partial asset transfer, distribution following the liquidation of a shareholding company, universal asset transfer from a company, realisation of a security, or by way of compulsory or voluntary public tender, and whether they relate only to legal or beneficial ownership, shall be subject to the approval of the Board of Directors according to the conditions described below.

The transferor's request for approval, which must be served on the company, shall state the name, forenames, profession and address of the transferee, or the company name and registered office in the case of a company, the number of shares or negotiable securities giving access to the capital of which the disposal or transfer is envisaged, the price offered or an estimate of the value of the shares or negotiable securities giving access to the capital. This request for approval must be countersigned by the transferee.

Approval will be given in the form of a notice, or will be deemed to have been given, in the absence of a reply within three months of the date of the request for approval.

The approval decision will be made by the Board of Directors, by a majority of the Directors present or represented. The transferor shall be entitled to vote, if he is a Director. The decision will not be justified, and in the event of a refusal, shall never give rise to any claim.

If the proposed transferee is approved, the transfer will be completed in favour of the transferee upon presentation of the supporting documents, which must be supplied within one month of service of the decision of the Board of Directors, failing which a fresh approval will be required.

If the company does not approve the proposed transferee, the transferor will have a period of eight days from the date of service of the refusal to notify the Board whether or not he abandons his proposal.

If the transferor does not expressly abandon his proposal under the conditions set out above, the Board of Directors shall be obliged within a period of three months from the date of service of the refusal, to arrange for the purchase of the shares or negotiable securities giving access to the capital, by a shareholder, a third party, or, with the transferor's consent, by the company, with a view to a reduction of the capital.

In the event that the offered shares or negotiable securities giving access to the capital are purchased by shareholders or third parties, the Board of Directors shall inform the transferor of the names, forenames, profession and address of the purchasers, or of the company name and registered office in the case of a company. The sale price shall be fixed by agreement between the purchasers and the transferor.

In the event that the offered shares or negotiable securities giving access to the capital are purchased by the company, the Board of Directors must first ask for the transferor's consent. The transferor must give his answer within eight days of receiving this request.

In the absence of agreement between the parties, the price of the shares and negotiable securities giving access to the capital shall be determined by an expert valuation, under the conditions provided by article 1843-4 of the Civil Code.

If, upon the expiry of a period of three months, the purchase has not been completed, approval shall be deemed to have been given. However, this period may be extended by the courts on an application by the company.

The transferor may, at any time, and at the latest within a period of eight days of determination of the price by the expert, abandon the disposal of his shares or negotiable securities giving access to the capital.

Disposals to the purchaser or purchasers nominated by the Board of Directors shall be completed by means of a transfer order signed by the Chairman of the Board of Directors, who shall serve it to the transferor within eight days of its date, with an invitation to attend the registered office to receive the sale price, which shall not bear interest.

All notices, requests, answers, opinions, waivers, information and consents provided for by this article shall be validly given if sent by extrajudicial instrument or by registered letter with proof of receipt requested.

When an expert is used to determine the price of the shares or negotiable securities giving access to the share capital under the conditions provided by article 1843-4 of the Civil Code, the expert's fees shall be paid in equal shares by the assignor and assignee.

This approval clause, which is the purpose of this article, also applies to disposals of allocation rights in the event of capital increases by way of incorporation of reserves, profits or issue premiums, and disposals of subscription rights in respect of capital increases in cash or individual waivers of subscription rights in favour of named individuals.

In these cases, the rules governing approval and the buyback conditions shall apply to the securities subscribed, and the time given to the Board of Directors to notify the third party subscriber whether it accepts him as a shareholder shall be three months from the date of final completion of the capital increase.

In the event of a buyback, the price shall be equal to the value of the new shares or negotiable securities giving access to the capital determined under the conditions provided by article 1843-4 of the Civil Code.

**Custodian and financial service**  
HSBC France.



## History of the company

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1894: The Banque Suisse et Française (BSF) is founded. It will become the Crédit Commercial de France.

1965: First CCF advertising campaign.

CCF keeps growing, particularly on an international level. Its presence outside of France is strengthened with the opening of branches, subsidiaries and representative offices abroad.

From 1982 to 1987, CCF creates a European investment bank and the acquisition of interests in Union de Banque à Paris, Européenne de Banque and Banque Chaix is the basis of the future CCF group.

1987: CCF privatisation. Apart from its national network, CCF has progressively created a group of regional banks operating under their own brand.

1990: Crédit Commercial du Sud-Ouest is created with the CCF branches located in Gironde département.

1992: CCF acquires Banque Marze in Ardèche département.

1993: CCF acquires Banque de Savoie.

1994: Centenary of CCF.

CCF develops its activities in Investment Banking, International Private Banking, Asset Management, and French retail banking with the acquisition of other regional banks.

During the 90's, Asset Management activity becomes the third main activity in CCF group.

1995: CCF acquires Banque Dupuy, de Parseval.

1998: Société Marseillaise de Crédit joins CCF group.

1999: CCF acquires 100 per cent of Banque de Picardie.

April 2000: CCF joins the HSBC Group and becomes the European platform of the HSBC Group.

August 2000: CCF acquires Banque Pelletier.

2001: CCF acquires Banque Hervet.

June 2002: Crédit Commercial de France changes its legal name to CCF.

November 2005: CCF becomes HSBC France and certain of its subsidiaries change their legal name and adopt the HSBC brand. HSBC France, HSBC Hervet, HSBC UBP, HSBC Picardie and HSBC de Baecque Beau constitute the new HSBC network.

July 2008: Disposal by HSBC France of its regional banking subsidiaries (Société Marseillaise de Crédit, Banque de Savoie, Banque Chaix, Banque Marze, Banque Dupuy, de Parseval, Banque Pelletier and Crédit Commercial du Sud-Ouest).

July 2008: Merger of HSBC Hervet, HSBC de Baecque Beau, HSBC UBP and HSBC Picardie with HSBC France.

October 2011: Merger of HSBC Private Bank France with HSBC France.

## Material contracts

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HSBC France currently has no material contracts, other than those concluded as part of the normal course of its business, that gives any member of the Group a right or obligation having a material impact on the issuer's ability to fulfil its obligations to holders of issued securities.

## Information on the share capital

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At 31 December 2012, the share capital amounted to EUR 337,189,135 divided into 67,437,827 fully paid up shares, each with a nominal value of EUR 5.

## Authorities to increase the share capital

|   | <u>With pre-emptive rights</u> |
|---|--------------------------------|
| <b>Issue of shares for cash or by capitalising reserves</b> |                                |
| Date of authority . . . . .                                 | 4 May 2011                     |
| Expiry date . . . . .                                       | 4 July 2013                    |
| Maximum nominal amount . . . . .                            | EUR100 million                 |
| Used amount . . . . .                                       | EURO                           |

The renewal of this authority for EUR 100 million until 30 June 2015 will be proposed to the Combined General Meeting to be held on 30 April 2013.

**Information on HSBC France and its share capital** (continued)**Movements in share capital**

|   | 2012                |                              |                              | 2011                |                              |                              |
|---|---------------------|------------------------------|------------------------------|---------------------|------------------------------|------------------------------|
|   | Number<br>of shares | Share<br>capital<br>in euros | Share<br>premium<br>in euros | Number<br>of shares | Share<br>capital<br>in euros | Share<br>premium<br>in euros |
| At 1 January . . . . .  | <b>67,437,827</b>   | <b>337,189,135</b>           | –                            | 67,437,820          | 337,189,100                  | –                            |
| Exercise of share options <sup>1</sup> . . . . .                          | –                   | –                            | –                            | –                   | –                            | –                            |
| Reduction of share capital<br>by cancellation of own shares held. . . . . | –                   | –                            | –                            | –                   | –                            | –                            |
| Capital increase . . . . .  | –                   | –                            | –                            | 7 <sup>3</sup>      | 35 <sup>3</sup>              | –                            |
| At 31 December . . . . .  | <b>67,437,827</b>   | <b>337,189,135</b>           | –                            | 67,437,827          | 337,189,135                  | –                            |

1 *Of which:*

2 *Capital increase due to the approval by the Combined General Meeting held on 31 July 2008 of the mergers of HSBC Hermet and HSBC de Baecque Beau with HSBC France.*

3 *Capital increase due to the approval by the Combined General Meeting held on 31 October 2011 of the merger of HSBC Private Bank France with HSBC France.*

| 2010             |                        |                        | 2009             |                        |                        | 2008               |                        |                        |
|------------------|------------------------|------------------------|------------------|------------------------|------------------------|--------------------|------------------------|------------------------|
| Number of shares | Share capital in euros | Share premium in euros | Number of shares | Share capital in euros | Share premium in euros | Number of shares   | Share capital in euros | Share premium in euros |
| 67,437,820       | 337,189,100            | -                      | 67,437,820       | 337,189,100            | -                      | 75,963,895         | 379,819,475            | -                      |
|                  | -                      | -                      | -                | -                      | -                      | 221,154            | 1,105,770              | 16,138,604.17          |
| -                | -                      | -                      | -                | -                      | -                      | (8,750,000)        | (43,750,000)           | (834,122)              |
| -                | -                      | -                      | -                | -                      | -                      | 2,771 <sup>2</sup> | 13,855 <sup>2</sup>    | -                      |
| 67,437,820       | 337,189,100            | -                      | 67,437,820       | 337,189,100            | -                      | 67,437,820         | 337,189,100            | -                      |

100,379 shares issued at EUR 73.48  
120,775 shares issued at EUR 81.71

**Information on HSBC France and its share capital** (continued)**Share options**

Following the merger of HSBC Private Bank France on 31 October 2011, options over HSBC Private Bank France have been exchanged for options over shares HSBC France at a parity determined at the time of the merger.

| Year       | Exercise price | Options outstanding<br>at 31.12.2012 | Expiry date |
|------------|----------------|--------------------------------------|-------------|
| 2002 ..... | EUR142.84      | –                                    | 2012        |

**Ownership of share capital and voting rights at 31 December 2012**

HSBC Bank plc has owned 99.99 per cent of the share capital and voting rights since 31 October 2000. This percentage has not varied since then. HSBC Bank plc is a wholly-owned subsidiary of HSBC Holdings plc, a company quoted in London, Hong Kong, New York, Paris and Bermuda.

**Dividend and payout policy**

|   | 2012              | 2011       | 2010       | 2009       | 2008       |
|---|-------------------|------------|------------|------------|------------|
| Number of shares at 31 December . . .                             | <b>67,437,827</b> | 67,437,827 | 67,437,820 | 67,437,820 | 67,437,820 |
| Average number of shares<br>outstanding during the year . . . . . | <b>67,437,827</b> | 67,437,822 | 67,437,820 | 67,437,820 | 75,020,854 |
| EPS <sup>1</sup> . . . . .  | <b>EUR4.75</b>    | EUR1.83    | EUR6.73    | EUR5.15    | EUR23.51   |
| Net dividend . . . . .  | <b>EUR3.56</b>    | EUR1.75    | EUR10.67   | EUR9.94    | –          |
| Exceptional dividend . . . . .                                    | –                 | –          | –          | –          | –          |
| Dividend + tax credit . . . . .                                   | –                 | –          | –          | –          | –          |
| Payout <sup>2</sup> . . . . .                                     | <b>75%</b>        | 95.6%      | 158.5%     | 193%       | –          |

<sup>1</sup> Calculated on the weighted average number of shares outstanding after deducting own shares held.

<sup>2</sup> Dividend paid as a percentage of reported earnings.

At the Annual General Meeting to be held on 30 April 2013, the Board will propose a net dividend of EUR 3.56 per EUR 5 nominal share. As the proposed amount equals the interim dividend decided by the Board on 27 February 2013, there would be no new payment.

Dividends which are not claimed within five years of the payment date lapse and become the property of the French Treasury.

## Recent developments and outlook

### Post-balance sheet events

New products and services are frequently offered to the customers of the HSBC Group in France. Information is available on the group's websites, and particularly in the press releases that can be viewed on the [www.hsbc.fr](http://www.hsbc.fr) website.

There has been no significant change affecting the issuer's or its subsidiaries' financial or sales situation since 31 December 2012, the date of the last audited and published financial statements.

### Main post-balance sheet events

#### **HSBC enters 10-year bancassurance agreement with AIG in Continental Europe (extract of press release dated 28 January 2013)**

HSBC Bank plc ("HSBC Bank"), a wholly-owned subsidiary of HSBC Holdings plc ("HSBC"), has entered into a 10-year bancassurance agreement with AIG Europe Limited (the "AIG Agreement") through which HSBC Group companies will distribute AIG non-life insurance products to customers in Turkey, France, and other countries in Continental Europe as may be agreed. The arrangements for distribution of products in Turkey and France will be on an exclusive basis.

Total consideration of approximately USD 55 million in cash will be paid under the AIG Agreement by AIG Group companies to HSBC Group companies for the opportunity to be the exclusive providers of non-life insurance products distributed by HSBC Group companies to customers in Turkey and France.

HSBC Bank has also entered into a sale and purchase agreement to sell its French subsidiary, HSBC Assurances IARD (France) ("HAI"), to AIG for a consideration of up to approximately USD 14.5 million, subject to adjustment based upon the net asset value at 31 December 2012 and including a deferred payment of up to USD 1.2 million based upon written premiums in 2013.

The AIG Agreement and the sale and purchase agreement are conditional upon country-specific distribution agreements being entered into in respect of Turkey and France between HSBC Group companies and AIG Group companies.

Under the bancassurance arrangements AIG Group companies will pay commissions on product sales and make other payments to HSBC Group companies.

The bancassurance agreements, including the country-specific agreements, and the sale and purchase agreement, are all subject to regulatory approval. The AIG Agreement is expected to become unconditional, and the sale and purchase agreement is expected to complete, in the first half of 2013.

The bancassurance agreements and the sale of HAI represent further progress in the execution of the HSBC Group strategy.

### Outlook

There has been no significant deterioration affecting the issuer's or its subsidiaries' outlook since 31 December 2012, the date of the last audited and published financial statements.

HSBC France has a clear defined strategy, which was the subject of a presentation on 5 July 2011 and is consistent with that of the HSBC Group. The strategy has the following objectives:

- in Commercial Banking, to become the key banking partner for companies operating internationally;
- in Global Banking and Markets, to be the leading international bank for HSBC France clients and the HSBC Group's platform for eurozone equity derivatives and fixed-income activities;
- in Retail Banking and Wealth Management, to become the key banking partner for wealth management customers;
- in Private Banking, to build on an international range of investment products in order to achieve faster development.

HSBC France's growth model aims to balance the contribution of each business line and maintain a solid balance sheet.

## **Persons responsible for the Registration Document and for auditing the financial statements**

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### **Person responsible for the Registration Document**

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Mr Jean Beunardeau, Chief Executive Officer.

### **Statement by the person responsible for the Registration Document**

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I declare, after taking all reasonable measures for this purpose and to the best of my knowledge, that the information contained in this Reference Document is in accordance with the facts and that it makes no omission likely to affect its meaning.

I declare, to the best of my knowledge, that the accounts have been prepared in accordance with applicable accounting standards and are a fair reflection of the assets, liabilities, financial position and profit or loss of the company and all the undertakings included in the consolidation scope, and that the Management Report on pages 2 to 6 and on page 195 presents a fair view of the company's business, results and financial position and that of all the undertakings included in the consolidation scope, as well as a description of the main risks and uncertainties to which they are exposed.

I have received a completion letter from the Auditors stating that they have audited the information contained in this Document about the financial position and accounts and that they have read this Document in its entirety.

Paris, 24 April 2013

*Jean Beunardeau, CEO*

## Persons responsible for auditing the financial statements

|  | Date first<br>appointed | Date<br>re-appointed | Date term ends |
|--|-------------------------|----------------------|----------------|
| <b>Incumbents</b>  |                         |                      |                |
| KPMG Audit FS II <sup>1</sup><br>Represented by Pascal Brouard <sup>2</sup><br>3 cours du Triangle<br>92939 Paris-La Défense Cedex | 2001                    | –                    | 2018           |
| BDO France – Léger & Associés <sup>3</sup><br>Represented by Michel Léger <sup>4</sup><br>113 rue de l'Université<br>75007 Paris   | 2007                    | 2012                 | 2018           |
| <b>Alternates</b>  |                         |                      |                |
| KPMG Audit FS I <sup>1</sup><br>Represented by Jean-Luc Decornoy<br>3 cours du Triangle<br>92939 Paris-La Défense Cedex            | 2001                    | –                    | 2018           |
| François Allain <sup>1</sup><br>2 rue Hélène Boucher<br>78286 Guyancourt Cedex   | 2007                    | 2012                 | 2018           |

<sup>1</sup> Member of the Compagnie Régionale des Commissaires aux comptes of Versailles.

<sup>2</sup> KPMG represented by Pascal Brouard as of financial year 2009.

<sup>3</sup> Member of the Compagnie Régionale des Commissaires aux comptes of Paris.

<sup>4</sup> Fabrice Chaffois will replace Michel Léger as of the financial year 2013.

Statutory Auditors' fees paid in 2012 within the HSBC France group are available in Note 38 to the consolidated financial statements on page 183.

## Cross-reference table

This cross-reference table refers to the main headings required by the European Regulation 809/2004 (Annex XI) implementing the directive known as “Prospectus”.

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According to article 28 of the European Regulation 809/2004, are included by reference in this Registration Document:

- the consolidated financial statements for the year ended 31 December 2011 and the Statutory Auditors' report on the financial consolidated statements, presented on pages 83 to 169 and 170 to 171 of the Registration Document 2011 filed with the AMF on 25 April 2012 under reference number D12-0413; and
- the parent company financial statements for the year ended 31 December 2011 and the Statutory Auditors' report on the parent company financial statements, presented on pages 172 to 2012 and 213 to 214 of the Registration Document 2011 filed with the AMF on 25 April 2012 under reference number D12-0413.

This Registration Document includes the annual financial report:

- Parent company financial statements pages 186 to 225
- Consolidated financial statements pages 100 to 183
- Management report pages 2 to 7 and 195
- Corporate, social and environmental responsibility pages 52 to 74
- Statement by person responsible page 244
- Statutory Auditors' report pages 184 to 185 and 225 to 226

These documents are available on the website [www.hsbc.fr](http://www.hsbc.fr) and on the AMF's website [www.amf-france.org](http://www.amf-france.org).

## Network of offices

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### HSBC GROUP INTERNATIONAL NETWORK

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Group website: www.hsbc.com

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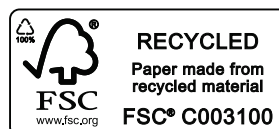
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