

## REPORT OF THE DIRECTORS

The Directors have pleasure in presenting their report together with the audited accounts for the year ended 31 December 2004.

### PRINCIPAL ACTIVITIES

The Bank and its subsidiary and associated companies are engaged in the provision of banking and related financial services.

### PROFITS

The consolidated profit of the Bank and its subsidiary and associated companies for the year is set out on page 117 together with particulars of dividends which have been paid or declared.

### MAJOR CUSTOMERS

The Directors believe that the five largest customers of the Bank accounted for less than 30% of the total of interest income and other operating income of the Bank in the year.

### SUBSIDIARIES

Particulars of the Bank's principal subsidiaries at 31 December 2004 are set out on page 169.

### SHARE CAPITAL

No change in either the authorised or issued share capital took place during the year.

### DONATIONS

Charitable donations made by the Bank and its subsidiaries during the year amounted to HK\$18 million.

### DIRECTORS

The Directors of the Bank who were in office at the end of the year were Mr D G Eldon, Mr Vincent H C Cheng, Mr John C C Chan, Dr Y T Cheng, Dr Marvin K T Cheung,

Mr S J Glass, Mr Jenkin Hui, Mr Peter T C Lee, Dr Eric K C Li, Dr Vincent H S Lo, Mr W K Mok, Mr Raymond C F Or, Mr Joseph C Y Poon, Dr David W K Sin and Mr Richard Y S Tang.

Dr Lee Quo-Wei and Dr Ho Tim retired as Directors with effect from the conclusion of the Bank's Annual General Meeting held on 22 April 2004 and, in recognition of their contributions to the Bank, were then appointed Honorary Senior Advisors to the Bank. It is with regret that the Directors report the loss of Dr Ho, who passed away on 6 November 2004 at the age of 95. Dr Ho joined the Bank in 1933 and had made important contributions to the Bank particularly in the formative years. He was appointed Director and General Manager in 1953 and Vice-Chairman from 1967 to 1979.

Mr Roger K H Luk resigned from the Board with effect from 6 December 2004 and would retire on 1 May 2005 after 30 years of service with the Bank.

Dr Marvin K T Cheung and Mr Joseph C Y Poon were appointed Directors of the Bank with effect from 25 May 2004 and 7 December 2004 respectively. Both of them retire under the provisions of the Bank's Articles of Association and, being eligible, offer themselves for re-election.

The Directors retiring by rotation in accordance with the Bank's Articles of Association are Mr John C C Chan, Dr Y T Cheng and Dr Vincent H S Lo, who, being eligible, offer themselves for re-election.

No Director proposed for re-election at the forthcoming Annual General Meeting has a service contract with the Bank which is not determinable by the Bank within one year without payment of compensation (other than statutory compensation).

No contract of significance, to which the Bank or any of its holding companies or any of its subsidiaries or fellow subsidiaries was a party and in which a Director of the Bank had a material interest, subsisted at the end of the year or at any time during the year.

## **STATUS OF INDEPENDENT NON-EXECUTIVE DIRECTORS**

The Bank has received from each independent non-executive Director an annual confirmation of his independence pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("the Listing Rules") and the Bank still considers the independent non-executive Directors to be independent.

## **BOARD COMMITTEES**

The Board has set up three committees, namely the Executive Committee, Audit Committee and Remuneration Committee.

### **Executive Committee**

The Executive Committee meets regularly and operates as a general management committee under the direct authority of the Board. The current members of the Executive Committee include Mr Vincent H C Cheng (Chairman), Mr Raymond C F Or, Mr Joseph C Y Poon, Mr W K Mok (Directors) and Mr William W Leung (General Manager).

### **Audit Committee**

The Audit Committee meets regularly with the senior financial, internal audit and compliance management and the external auditors to consider the Bank's financial reporting, the nature and scope of audit reviews and the effectiveness of the systems of internal control and compliance. The current members of the Audit Committee are Dr Eric K C Li (Chairman), Mr Richard Y S Tang and Dr Marvin K T Cheung, all of whom are independent non-executive Directors of the Bank.

### **Remuneration Committee**

The Remuneration Committee, which has recently been set up, will meet regularly to consider human resource issues and to make recommendations to the Board on, among others, the Bank's policy and structure for all remuneration of Directors and senior management in order to attract, motivate and retain them. The current members of the Remuneration Committee are Mr John C C Chan (Chairman), Mr Jenkin Hui and Mr Peter T C Lee, all of whom are independent non-executive Directors of the Bank.

## **CODE OF BEST PRACTICE AND SUPERVISORY POLICY MANUAL ON CORPORATE GOVERNANCE OF LOCALLY INCORPORATED AUTHORISED INSTITUTIONS**

The Bank has complied throughout the year with the Code of Best Practice adopted by the Bank, which includes all the guidelines set out in Appendix 14 of the Listing Rules in force during 2004, and has followed the module on "Corporate Governance of Locally Incorporated Authorised Institutions" under the Supervisory Policy Manual issued by the Hong Kong Monetary Authority in September 2001. Information about the Bank's Corporate Governance is given on pages 8 to 13.

## **THE CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS**

In relation to securities transactions by Directors, the Bank has revised its code of conduct and has since 31 March 2004 adopted in it terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers (ie Appendix 10 of the Listing Rules) as then in force.

## **DIRECTORS' COMPLIANCE WITH THE CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS**

Specific enquiry has been made of all Directors (including those who have ceased to be Directors or who have become Directors during the year ended 31 December 2004) who have confirmed that they complied with the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers (ie Appendix 10 of the Listing Rules) and the Bank's code of conduct regarding securities transactions by Directors (both as in force at the material times) at the applicable times for the period from 1 January 2004 to 31 December 2004 (both dates inclusive).

## DIRECTORS' INTERESTS

At the end of the financial year, the interests of the Directors in the shares, underlying shares of equity derivatives and

debentures of the Bank and its associated corporations (all within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) disclosed in accordance with the Listing Rules were detailed below.

	Personal Interests (held as beneficial owner)	Family Interests (Interests of spouse or child under 18)	Corporate Interests (Interests of controlled corporation)	Other Interests	Total Interests	Total Interests as % of the relevant issued share capital
<b>Number of Ordinary Shares of HK\$5 each in the Bank</b>						
Mr D G Eldon	300	–	–	–	300	0.00
Mr John C C Chan	–	–	–	1,000 <sup>(1)</sup>	1,000	0.00
Mr W K Mok	1,625	–	–	–	1,625	0.00
<b>Number of Ordinary Shares of US\$0.50 each in HSBC Holdings plc</b>						
Mr D G Eldon	98,904 <sup>(2)</sup>	942	–	341,571 <sup>(6)</sup>	441,417	0.00
Mr Vincent H C Cheng	37,030	77,488	–	194,769 <sup>(6)</sup>	309,287	0.00
Mr John C C Chan	14,283	–	–	3,000 <sup>(1)</sup>	17,283	0.00
Mr S J Glass	278	8,532	–	66,740 <sup>(6)</sup>	75,550	0.00
Mr Jenkin Hui	9,732	24,342	1,078,368 <sup>(3)</sup>	–	1,112,442	0.01
Dr Eric K C Li	–	18,132	79,622 <sup>(4)</sup>	–	97,754	0.00
Mr W K Mok	18,960	–	–	60,729 <sup>(6)</sup>	79,689	0.00
Mr Raymond C F Or	91,086	33,851	–	164,423 <sup>(6)</sup>	289,360	0.00
Mr Joseph C Y Poon	22,599 <sup>(5)</sup>	54,916	–	38,533 <sup>(6)</sup>	116,048	0.00

Notes:

<sup>(1)</sup> 1,000 shares in the Bank and 3,000 shares in HSBC Holdings plc were held by a trust of which Mr and Mrs John C C Chan were beneficiaries.

<sup>(2)</sup> These shares are jointly held by Mr and Mrs D G Eldon.

<sup>(3)</sup> Mr Jenkin Hui was entitled to fully control the voting power at general meetings of Parc Palais Incorporated, a private company, which beneficially held all of those shares referred to above as his corporate interests.

<sup>(4)</sup> Dr Eric K C Li was entitled to control no less than one-third of the voting power at general meetings of a private company which beneficially held all of those shares referred to above as his corporate interests.

<sup>(5)</sup> These shares are jointly held by Mr and Mrs Joseph C Y Poon.

<sup>(6)</sup> These represent interests in (i) options granted to Directors under the HSBC share plans to acquire ordinary shares of US\$0.50 each in HSBC Holdings plc and (ii) conditional awards of shares under the HSBC Holdings plc Restricted Share Plan made in favour of Directors and held by a trust for ordinary shares of US\$0.50 each in HSBC Holdings plc, as set against their respective names below:

	Options (please refer to the options table below for details)	Conditional awards of shares under the HSBC Holdings plc Restricted Share Plan (please refer to the awards table below for further information)	Total
Mr D G Eldon	–	341,571	341,571
Mr Vincent H C Cheng	3,070	191,699	194,769
Mr S J Glass	41,348	25,392	66,740
Mr W K Mok	2,526	58,203	60,729
Mr Raymond C F Or	2,634	161,789	164,423
Mr Joseph C Y Poon	32,334	6,199	38,533

At the end of the financial year, the undermentioned Directors held unlisted physically settled options to acquire the number of ordinary shares of US\$0.50 each in HSBC

Holdings plc set against their respective names. These options were granted for nil consideration by HSBC Holdings plc.

	Options held at 31 December 2004	Options exercised during the year (ordinary shares of US\$0.50 each)	Exercise price per share in pence	Date granted	Exercisable from	Exercisable until
Mr Vincent H C Cheng	3,070	–	534.96	8 May 2003	1 Aug 2008	31 Jan 2009
Mr S J Glass	17,550	–	637.54	29 Mar 1999	3 Apr 2002	29 Mar 2009
	6,500	–	746.00	3 Apr 2000	3 Apr 2003	3 Apr 2010
	7,500	–	871.20	23 Apr 2001	23 Apr 2004	23 Apr 2011
	7,000	–	840.50	7 May 2002	7 May 2005	7 May 2012
	2,798	–	602.99	10 Apr 2000	1 Aug 2005	31 Jan 2006
	<u>41,348</u>					
Mr W K Mok	–	3,126 <sup>(1)</sup>	539.80	1 Apr 1999	1 Aug 2004	31 Jan 2005
	2,526	–	647.20	10 May 2004	1 Aug 2009	31 Jan 2010
	<u>2,526</u>					
Mr Raymond C F Or	–	1,875 <sup>(1)</sup>	539.80	1 Apr 1999	1 Aug 2004	31 Jan 2005
	1,119	–	602.99	10 Apr 2000	1 Aug 2005	31 Jan 2006
	1,515	–	647.20	10 May 2004	1 Aug 2009	31 Jan 2010
	<u>2,634</u>					
Mr Joseph C Y Poon	3,750	–	501.60	24 Mar 1997	24 Mar 2000	24 Mar 2007
	9,000	–	637.54	29 Mar 1999	29 Mar 2002	29 Mar 2009
	4,750	–	746.00	3 Apr 2000	3 Apr 2003	3 Apr 2010
	2,750	–	871.20	23 Apr 2001	23 Apr 2004	23 Apr 2011
	4,400	–	840.50	7 May 2002	7 May 2005	7 May 2012
	5,050	–	691.00	2 May 2003	2 May 2006	2 May 2013
	1,119	–	602.99	10 Apr 2000	1 Aug 2005	31 Jan 2006
	1,515	–	647.20	10 May 2004	1 Aug 2009	31 Jan 2010
	<u>32,334</u>					

Note:

<sup>(1)</sup> At the date of exercise, 2 August 2004, the market value per share was 833.5p.

## REPORT OF THE DIRECTORS (continued)

At the end of the financial year, the interests of the Directors in the conditional awards of shares made in favour of them under the HSBC Holdings plc Restricted Share Plan and held

by a trust for ordinary shares of US\$0.50 each in HSBC Holdings plc were as follows:

	Awards held at 1 January 2004	Awards made during the year	Shares awarded released to the Director during the year	Awards held at 31 December 2004 <sup>(1)</sup>
Mr D G Eldon	289,829	87,302	49,209	341,571
Mr Vincent H C Cheng	155,179	52,963	23,981	191,699
Mr S J Glass	12,467	12,180	–	25,392
Mr W K Mok	59,713	11,571	15,287	58,203
Mr Raymond C F Or	132,036	45,397	22,011	161,789
Mr Joseph C Y Poon	6,199 <sup>(2)</sup>	–	–	6,199

Notes:

<sup>(1)</sup> This includes additional shares arising from scrip dividends.

<sup>(2)</sup> This represents the awards held by Mr Joseph C Y Poon on 7 December 2004 when he was appointed a Director of the Bank.

All the interests stated above represent long positions. As at 31 December 2004, no short positions were recorded in the Register of Directors' and Chief Executives' Interests and Short Positions required to be kept under section 352 of the SFO.

Save as disclosed in the preceding paragraphs, at no time during the year was the Bank or any of its holding companies or its subsidiaries or fellow subsidiaries a party to any arrangement to enable the Directors of the Bank to acquire benefits by means of the acquisition of shares in or debentures of the Bank or any other body corporate.

No right to subscribe for equity or debt securities of the Bank has been granted by the Bank to, nor have any such rights been exercised by, any person during the year ended 31 December 2004.

### DIRECTORS' INTEREST IN COMPETING BUSINESSES

Pursuant to Rule 8.10 of the Listing Rules, at the end of the year, the following Directors had declared interests in the following entities which compete or are likely to compete, either directly or indirectly, with the businesses of the Bank:

Mr D G Eldon is a Director of HSBC Holdings plc, the ultimate holding company of the Bank, and certain of its subsidiaries, including The Hongkong and Shanghai Banking Corporation Limited, the immediate holding company of the Bank.

Mr Vincent H C Cheng is a Director of The Hongkong and Shanghai Banking Corporation Limited and HSBC Insurance (Asia-Pacific) Holdings Limited, a subsidiary of The Hongkong and Shanghai Banking Corporation Limited.

Mr S J Glass is a Director of HSBC Asia Holdings BV, the immediate holding company of The Hongkong and Shanghai Banking Corporation Limited, and certain of its subsidiaries.

Mr W K Mok was a Director of HSBC Asset Management (Hong Kong) Limited and HSBC Investment Funds (Hong Kong) Limited, subsidiaries of The Hongkong and Shanghai Banking Corporation Limited as at 31 December 2004, and has ceased to be a Director of both companies since 7 January 2005.

Mr Raymond C F Or is General Manager of The Hongkong and Shanghai Banking Corporation Limited and was appointed an Executive Director of The Hongkong and Shanghai Banking Corporation Limited with effect from 1 January 2005. Mr Or is a Director of HSBC Insurance (Asia-Pacific) Holdings Limited, a subsidiary of The Hongkong and Shanghai Banking Corporation Limited. He is also a Director of Bank of Communications Limited.

HSBC Holdings plc, through its subsidiaries and associated undertakings, is engaged in providing a comprehensive range of banking, insurance and related financial services.

The entities in which the Directors have declared interests are managed by separate Boards of Directors and management, which are accountable to their respective shareholders.

The Board of the Bank includes eight independent non-executive Directors whose views carry significant weight in the Board's decisions. The Audit Committee of the Bank, which consists of three independent non-executive Directors, meets regularly to assist the Board of Directors in reviewing the financial performance, internal control and compliance systems of the Bank and its subsidiaries. The Bank is, therefore, capable of carrying on its businesses independently of, and at arm's length from, the businesses in which Directors have declared interests.

## DIRECTORS' EMOLUMENTS

The emoluments of the Directors of the Bank (including executive Directors and independent non-executive Directors) on a named basis are set out on page 143 of the Bank's accounts for the year ended 31 December 2004.

## SUBSTANTIAL INTERESTS IN SHARE CAPITAL

The register maintained by the Bank pursuant to the SFO recorded that, as at 31 December 2004, the following corporations had interests (as defined in that Ordinance) in the Bank set opposite their respective names:

Name of Corporation	Number of Ordinary Shares of HK\$5 each in the Bank (Percentage of total)
The Hongkong and Shanghai Banking Corporation Limited	1,188,057,371 (62.14%)
HSBC Asia Holdings BV	1,188,057,371 (62.14%)
HSBC Asia Holdings (UK)	1,188,057,371 (62.14%)
HSBC Holdings BV	1,188,057,371 (62.14%)
HSBC Finance (Netherlands)	1,188,057,371 (62.14%)
HSBC Holdings plc	1,188,057,371 (62.14%)

The Hongkong and Shanghai Banking Corporation Limited is a subsidiary of HSBC Asia Holdings BV, which is a wholly-owned subsidiary of HSBC Asia Holdings (UK), which in turn is a wholly-owned subsidiary of HSBC Holdings BV. HSBC Holdings BV is a wholly-owned subsidiary of HSBC Finance (Netherlands), which in turn is wholly-owned by HSBC Holdings plc. Accordingly, The Hongkong and Shanghai Banking Corporation Limited's interests are recorded as the

interests of HSBC Asia Holdings BV, HSBC Asia Holdings (UK), HSBC Holdings BV, HSBC Finance (Netherlands) and HSBC Holdings plc.

The Directors regard HSBC Holdings plc to be the beneficial owner of 1,188,057,371 ordinary shares in the Bank (62.14%).

All the interests stated above represent long positions. As at 31 December 2004, no short positions were recorded in the Register of Interests in Shares and Short Positions required to be kept under section 336 of the SFO.

## PURCHASE, SALE OR REDEMPTION OF THE BANK'S LISTED SECURITIES

During the year, there was no purchase, sale or redemption by the Bank, or any of its subsidiaries, of the Bank's listed securities.

## SUPERVISORY POLICY MANUAL ON FINANCIAL DISCLOSURE BY LOCALLY INCORPORATED AUTHORISED INSTITUTIONS

The accounts of the Bank for the year ended 31 December 2004 fully comply with the module on "Financial Disclosure by Locally Incorporated Authorised Institutions" under the Supervisory Policy Manual issued by the Hong Kong Monetary Authority in November 2002.

## AUDITORS

KPMG retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of KPMG as auditors of the Bank is to be proposed at the forthcoming Annual General Meeting.

On behalf of the Board

**David Eldon**  
Chairman  
Hong Kong, 28 February 2005