

CORPORATE GOVERNANCE AND OTHER INFORMATION

Hang Seng is committed to high standards of corporate governance with a view to safeguarding the interests of shareholders, customers, staff and other stakeholders. The Bank has followed the module on “Corporate Governance of Locally Incorporated Authorised Institutions” under the Supervisory Policy Manual issued by the Hong Kong Monetary Authority (“HKMA”) and has fully complied with all the code provisions and most of the recommended best practices as set out in the Code on Corporate Governance Practices contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) throughout the year. The Bank also keeps its corporate governance framework under constant review to ensure that it is in line with international and local best practices.

BOARD OF DIRECTORS

The Board has collective responsibility for leadership and control of, and for promoting the success of, the Bank by directing and supervising the Bank’s affairs.

The types of decisions which are to be taken by the Board include those relating to :

- five-year strategic plan;
- annual operating plans and performance targets;
- annual and interim results;
- risk appetite;
- internal control and risk management framework;
- specified senior appointments;
- acquisitions and disposals above predetermined thresholds; and
- substantial changes to balance sheet management policies.

Chairman and Chief Executive

The roles of Chairman of the Board and Chief Executive of the Bank are segregated, with a clear division of responsibilities. The Chairman of the Board is an Independent Non-executive Director who is responsible for the leadership and effective running of the Board. The Chief Executive is an Executive Director who exercises all the powers, authorities and discretions of the Executive Committee as may be delegated to her in respect of the Bank and its subsidiaries.

Board Composition

As at the date of this Annual Report, the Board comprises 15 Directors, of whom two are Executive Directors and 13 are Non-executive Directors. Of the 13 Non-executive Directors, eight are Independent Non-executive Directors. There is a strong independent element on the Board, to ensure the independence and objectivity of the Board’s decision-making process as well as the thoroughness and impartiality of the Board’s oversight of the Management.

All the Independent Non-executive Directors meet the guidelines for assessment of independence as set out in Rule 3.13 of the Listing Rules. The Bank has also received from each of the Independent Non-executive Directors an annual confirmation of his/her independence.

Members of the Board, who come from a variety of different backgrounds, have a diverse range of business, banking and professional expertise. Brief biographical particulars of all the Directors, together with information relating to the relationship among them, are set out in the section “Biographical Details of Directors” in this Annual Report.

Board Process

Regular Board/Board Committee meeting schedules for each year are made available to all Directors/Board Committee members before the end of the preceding year. In addition, notice of meetings will be given to all Directors at least 14 days before each Board meeting.

Other than regular Board meetings, the Chairman also met with Non-executive Directors, including Independent Non-executive Directors, without the presence of Executive Directors, to facilitate an open and frank discussion among the Non-executive Directors on issues relating to the Bank.

Meeting agendas for regular Board meetings are set after consultation with the Chairman and the Chief Executive. All Directors are given an opportunity to include matters in the agenda. Regular reports include the Bank’s financial performance, strategic plan, risk appetite, and review of internal control and risk management framework; as well as the large credit exposures and connected lending of the Bank and its subsidiaries.

Minutes of Board/Board Committee meetings with details of the matters discussed by the Board/Board Committee and decisions made, including any concerns or views of the Directors/Board Committee members, are kept by the Company Secretary and are open for inspection by Directors/Board Committee members.

During 2010, the important matters discussed at the Board meetings included:

- acquisition of headquarters premises in Shanghai by Hang Seng Bank (China) Limited;
- the Bank's internal capital adequacy assessment process;
- review of the Bank's remuneration policy and remuneration system;
- the Bank's strategy for RMB business;
- the Bank's strategy for recruitment, retention and development of talents;
- capital management plan;
- appointments of Directors and senior management; and
- pay review for 2010 and variable incentive pool for 2009.

The Board reviews and evaluates its work process and effectiveness annually, with a view to identifying areas for improvement and further enhancement.

All Directors have access to the Executive Directors as and when they consider necessary. They also have access to the Company Secretary who is responsible for ensuring that the Board procedures, and related rules and regulations, are followed.

Under the Articles of Association of the Bank, a Director shall not vote or be counted in the quorum in respect of any contract, arrangement, transaction or other proposal in which he/she or his/her associate(s), is/are materially interested.

Appointment, Re-election and Removal

The Bank's Articles of Association provide that each Director is required to retire by rotation once every three years and that one-third (or the number nearest to one-third) of the Directors shall retire from office every year at the Bank's Annual General Meeting. A Director's specific term of appointment, therefore, cannot exceed three years. Retiring Directors are eligible for re-election at Annual General Meetings of the Bank.

The Bank uses a formal, considered and transparent procedure for the appointment of new Directors. Before a prospective Director's name is formally proposed, opinions of the existing Directors (including the Independent Non-executive Directors) will be solicited. The appointment will be considered and if thought fit, approved by the Board after due deliberation. In accordance with the requirement under the Banking Ordinance, approval from HKMA will also be obtained. All new Directors are subject to election by shareholders of the Bank at the next Annual General Meeting after their appointments have become effective.

Four new Directors have been appointed since 2010 Annual General Meeting, namely, Ms L Y Chiang, Ms Sarah C Legg, Mr Mark S McCombe and Mr Michael W K Wu. The aforesaid Directors will all stand for election by the Bank's shareholders at the Bank's Annual General Meeting to be held on 13 May 2011.

Responsibilities of Directors

The Bank regularly reminds all Directors of their role and responsibilities. Through regular Board meetings, all Directors are kept abreast of the conduct, business activities and development of the Bank.

Induction programmes on the following key areas are arranged for newly appointed Directors:

- the Bank's business operations in Hong Kong, including personal financial services, corporate and commercial banking, treasury and investment services;
- the Bank's business operations on the Mainland; and
- the Bank's financial control, risk management, internal audit, compliance, information technology and support, and human resources.

All Directors are given opportunities to update and develop their skills and knowledge.

All Directors have full and timely access to all relevant information about the Bank so that they can discharge their duties and responsibilities as Directors. There are established procedures for Directors to seek independent professional advice on matters relating to the Bank where appropriate. All costs associated with obtaining such advice will be borne by the Bank. In addition, each Director has separate and independent access to the Bank's senior management.

CORPORATE GOVERNANCE AND OTHER INFORMATION

The Bank has adopted a Code for Securities Transactions by Directors on terms no less exacting than the required standards as set out in the Model Code for Securities Transactions by Directors of Listed Issuers (as set out in Appendix 10 to the Listing Rules). Specific enquiries have been made with all Directors who have confirmed that they have complied with the Bank's Code for Securities Transactions by Directors throughout the year of 2010.

Appropriate Directors' liability insurance cover has also been arranged to indemnify the Directors for liabilities arising out of corporate activities. The coverage and the sum insured under the policy are reviewed annually.

The interests in Group securities, including securities relating to HSBC Holdings plc and the Bank, held by the Directors as at

31 December 2010 are disclosed in the Report of the Directors as set out in this Annual Report.

DELEGATION BY THE BOARD

Board Committees

The Board has set up three committees, namely, the Executive Committee, the Audit Committee and the Remuneration Committee, to assist it in carrying out its responsibilities.

Each of these committees has specific written terms of reference which set out in detail their respective authorities and responsibilities. All committees, except the Executive Committee, are comprised solely of Independent Non-executive Directors. All committees report back to the Board on their decisions or recommendations on a regular basis.

BOARD		
Executive Committee	Audit Committee	Remuneration Committee
Members: Mrs Margaret Leung (Chairman)	Members: Dr Eric K C Li (Chairman)	Members: Dr John C C Chan (Chairman)
Mr William W Leung	Mr Richard Y S Tang	Mr Jenkin Hui
Mr Andrew H C Fung	Dr Marvin K T Cheung	Dr Raymond K F Ch'ien
Mr David W H Tam		
Mr Andrew W L Leung		
Mr Christopher H N Ho		
Mr Nixon L S Chan		

Executive Committee

The Executive Committee meets at least once each month and operates as a general management committee under the direct authority of the Board. It exercises the powers, authorities and discretions as delegated by the Board in so far as they concern the management and day-to-day running of the Bank in accordance with its terms of reference and such other policies and directives as the Board may determine from time to time. The Executive Committee also sub-delegates credit, investment and capital expenditure authorities to its members and senior executives.

To further enhance the Bank's risk management framework and in line with best practices, the Bank has set up a Risk Management Committee to centralise the risk management oversight function of the Bank and its subsidiaries. The Risk

Management Committee reports directly to the Executive Committee. Its main functions are to review, analyse, evaluate, recognise and manage various risks of the Bank, including all the eight types of risks stipulated in the Supervisory Policy Manual of HKMA, namely, credit risk, market risk, liquidity risk, interest rate risk, operational risk, legal and compliance risk, reputation risk and strategic risk. In addition, the Risk Management Committee also covers insurance risk, pension risk and sustainability risk, and is responsible for approval of all risk management related policies.

Audit Committee

The Audit Committee meets at least four times a year, with the Bank's senior executives (including, but not limited to, the Chief Financial Officer, the Chief Risk Officer, the Chief Credit Officer, the Chief Compliance Officer and the Head of Audit)

and representatives of the external auditor, to consider, among other things, the Bank's financial reporting, the nature and scope of audit reviews, and the effectiveness of the systems of internal control and compliance. It is also responsible for the appointment, reappointment, removal and remuneration of the Bank's external auditor. Further, given the importance of risk management to the business and operations of a financial institution, the scope of responsibilities of the Audit Committee has recently been expanded to cover risk management oversight. As such, the Audit Committee will also review the Bank's risk appetite, tolerance and strategy, and the effectiveness of the Bank's risk management framework.

The Audit Committee reports to the Board following each Audit Committee meeting, drawing the Board's attention to salient points that the Board should be aware of, identifying any matters in respect of which it considers that action or improvement is needed and making relevant recommendations.

The Audit Committee held five meetings in 2010. The major work performed by the Committee during 2010 included:

- reviewing the Bank's financial statements for the year ended 31 December 2009 and the related documents, and the management letter and audit issues noted by the Bank's external auditor;
- reviewing the Bank's interim financial statements for the six months ended 30 June 2010 and the related documents, and the issues noted by the Bank's external auditor;
- reviewing essential matters or reports relating to financial control, internal audit, credit, compliance and internal control, and discussing the same with the Management;
- reviewing risk-related matters including the Bank's risk management framework, risk maps, and balance sheet management position;
- reviewing regulatory review reports and internal audit reports, and discussing the same with the Management and Head of Audit;
- reviewing the revised accounting standards and prospective changes to accounting standards, and the impact on the Bank's financial reporting;
- reviewing the internal audit plan for 2011 and monitoring the staffing and resources of the Bank's internal audit function;
- reviewing the remuneration and engagement letters of the Bank's external auditor, and its objectivity and independence;

- reviewing the adequacy of resources, qualifications and experience of the staff of the accounting and financial reporting function of the Bank, and their training programme and budget;
- reviewing the implementation progress of Sarbanes-Oxley Act;
- reviewing the implementation and effectiveness of the Policy for the Reporting of Improperities;
- reviewing the terms of reference of the Audit Committee for the purpose of expanding its role and responsibilities to cover risk management oversight; and
- exercising oversight over the audit committees of the Bank's principal subsidiaries.

The Audit Committee meets with the representatives of the Bank's external auditor and Head of Audit on a regular basis and also meets with them without the presence of the Management at least once a year. Further, the Committee meets with the representatives of HKMA to maintain a regular dialogue with the regulator and to share HKMA's general views on their supervisory focus.

In order to identify areas for further improvements, the Audit Committee conducts an annual gap analysis as regards the effective discharge of its role and responsibilities under its terms of reference.

Remuneration Committee

The Remuneration Committee meets at least twice a year to consider human resources issues and make recommendations to the Board on, among others, the Bank's policy and structure for all remuneration and fees of Directors, senior management and key personnel in order to attract, motivate and retain quality personnel. The Committee will also review annually and independently of the Management, the adequacy and effectiveness of the Bank's remuneration policy and its implementation to ensure that the Bank's remuneration policy is consistent with regulatory requirements and promote effective risk management.

In determining the bank-wide remuneration policy, the Remuneration Committee will take into account the Bank's business objective, people strategy, short-term and long-term performance, business and economic environment conditions, market practices and risk management needs, in order to ensure the remuneration aligns with business and individual performances, promotes effective risk management, facilitates retention of quality personnel and is competitive in the market. The Committee may invite any Director, executive, consultant or other relevant party to provide advice in this respect.

CORPORATE GOVERNANCE AND OTHER INFORMATION

The Remuneration Committee held two meetings in 2010. The major work performed by the Committee during 2010 included:

- reviewing the fees payable to the Directors and Board Committee Chairmen/members of the Bank and its subsidiaries;
- reviewing the remuneration packages of the Executive Directors and senior management of the Bank; and the Chief Executive of Hang Seng Bank (China) Limited;
- reviewing the proposed variable incentive pool for 2009;
- reviewing the pay review proposal for 2010;
- determining the proposed revisions of certain senior executives' remuneration packages of the Bank; and
- conducting independent review of the Bank's remuneration system.

In order to identify areas for further improvements, the Remuneration Committee conducts an annual gap analysis as regards the effective discharge of its role and responsibilities under its terms of reference.

Attendance Records

The attendance records of Board and Board Committee meetings are set out in the following table:

	Meetings held in 2010				
	2010 AGM	Board	Executive Committee	Audit Committee	Remuneration Committee
Number of Meetings	1	7	12	5	2
Directors					
Dr Raymond K F Ch'ien* (<i>Chairman</i>) ^{Note 1}	1/1	7/7			N/A
Mrs Margaret Leung (<i>Vice-Chairman and Chief Executive</i>)	1/1	7/7	12/12		
Dr John C C Chan*	1/1	7/7			2/2
Dr Marvin K T Cheung*	1/1	6/7		5/5	
Ms L Y Chiang* ^{Note 2}	N/A	1/1			
Mr Alexander A Flockhart [#] ^{Note 3}	0/1	4/7			
Mr Jenkin Hui*	1/1	7/7			2/2
Ms Sarah C Legg [#] ^{Note 4}	N/A	N/A			
Mr William W Leung	1/1	7/7	11/12		
Dr Eric K C Li*	1/1	5/7		5/5	
Dr Vincent H S Lo [#]	1/1	6/7			
Mr Iain J Mackay [#] ^{Note 3}	1/1	6/7			
Mr Mark S McCombe [#] ^{Note 4}	N/A	N/A			
Mrs Dorothy K Y P Sit [#]	1/1	7/7			
Mr Richard Y S Tang*	1/1	7/7		5/5	
Mr Peter T S Wong [#]	1/1	5/7			
Mr Michael W K Wu* ^{Note 2}	N/A	1/1			
Senior Executives					
Mr Andrew H C Fung			12/12		
Mr Nixon L S Chan			11/12		
Mr Christopher H N Ho			11/12		
Mr Andrew W L Leung			12/12		
Mr David W H Tam			8/12		
Average Attendance Rate	92%	90%	92%	100%	100%

* Independent Non-executive Directors

Non-executive Directors

^{Note 1} Dr Raymond K F Ch'ien was appointed as a member of the Remuneration Committee with effect from 5 November 2010.

^{Note 2} Ms L Y Chiang and Mr Michael W K Wu were appointed as Independent Non-executive Directors with effect from 20 September 2010.

^{Note 3} Mr Alexander A Flockhart and Mr Iain J Mackay resigned from the Board with effect from 31 December 2010.

^{Note 4} Ms Sarah C Legg and Mr Mark S McCombe were appointed as Non-executive Directors with effect from 14 February 2011.

REMUNERATION OF DIRECTORS, SENIOR MANAGEMENT AND KEY PERSONNEL

The Bank's policy on remuneration is to maintain fair and competitive packages based on business needs and industry practice.

The level of fees paid to Non-executive Directors is determined by reference to factors including fees paid by comparable institutions, and Directors' workload and commitments.

The following factors are considered when determining the remuneration packages of Executive Directors:

- business needs;
- general economic situation;
- changes in appropriate markets such as supply/demand fluctuations and changes in competitive conditions;
- individual contributions to results as confirmed in the performance appraisal process; and
- retention consideration and individual potential.

No individual Director will be involved in decisions relating to his/her own remuneration.

The scales of Director's fees, and additional fees for Chairmen and members of the Audit Committee and Remuneration Committee for 2010 and 2011 respectively, are outlined below:

	Fees for 2010	Fees/Proposed fees for 2011
Board of Directors		
Chairman	HK\$360,000	HK\$440,000 ^{Note 6}
Vice-Chairman	Nil ^{Note 5}	Nil ^{Note 5}
Other Directors	HK\$280,000 ^{Note 5}	HK\$340,000 ^{Notes 5 and 6}
Audit Committee		
Chairman	HK\$120,000	HK\$260,000 ^{Note 7}
Other Members	HK\$80,000	HK\$160,000 ^{Note 7}
Remuneration Committee		
Chairman	HK\$60,000	HK\$90,000 ^{Note 7}
Other Members	HK\$40,000	HK\$60,000 ^{Note 7}

^{Note 5} In line with the remuneration policy of HSBC Group, no Directors' fees are paid to those Directors who are full time employees of the Bank or its subsidiaries.

^{Note 6} Having regard to the latest market trend, and the ever demanding regulatory requirements and industry best practices applicable to the Bank which have significantly expanded the responsibilities and commitments of the Chairman and the Non-executive Directors, a resolution will be proposed for approval by the Bank's shareholders at the 2011 AGM to increase the fees payable by the Bank to the Chairman and the Non-executive Directors to HKD440,000 per annum and HKD340,000 per annum respectively. If approved by the shareholders, the proposed fees will become effective retrospectively as from 1 January 2011. More information on the proposed fees to the Chairman and the Non-executive Directors is set out in the Circular in relation to the 2011 AGM to be issued in March 2011.

^{Note 7} Having regard to the latest market trend, and the workload and commitments required, the Board has approved the increase in the fees payable to the Chairmen and Members of Audit Committee and Remuneration Committee, which became effective as from 1 January 2011.

Information relating to the remuneration of each Director for 2010 is set out in Note 19 to the Bank's 2010 Financial Statements.

Aggregate quantitative information on the remuneration for the Bank's senior management and key personnel is set out below:

- (i) Amount of remuneration for the financial year 2010, split into fixed and variable remuneration, and number of beneficiaries;

Fixed Remuneration (HKD)	34,760,000
Variable Remuneration (HKD)	29,283,000
Number of beneficiaries	12

CORPORATE GOVERNANCE AND OTHER INFORMATION

- (ii) Amounts and form of variable remuneration for the financial year 2010, split into cash, shares and share-linked instruments and other instruments (if any);

Variable Remuneration in Cash (HKD) (a)	16,170,000
Variable Remuneration in Shares (HKD) (b)	13,113,000
Variable Remuneration (HKD) (a) + (b)	29,283,000

- (iii) Amount of deferred remuneration during the financial year 2010 was HKD13,113,000. The aforesaid relates to share awards (variable remuneration) granted and unvested in 2010. According to the terms of the share scheme, the shares awarded have a vesting period of three years, commencing from the first anniversary of the date of award;
- (iv) As mentioned in item (iii) above, the share awards were unvested in the financial year 2010. Accordingly, there was no deferred remuneration awarded during 2010 being paid out or reduced through performance adjustment; and
- (v) No senior management or key personnel has been awarded with new sign-on or severance payment during the financial year 2010.

ACCOUNTABILITY AND AUDIT

Financial Reporting

The Board aims at making a balanced, clear and comprehensive assessment of the Bank's performance, position and prospects. An annual operating plan is reviewed and approved by the Board on a yearly basis. Reports on financial results, business performance and variances against the approved annual operating plan are submitted to the Board for regular discussion and monitoring at Board meetings.

Strategic planning cycles are generally from three to five years. The Bank's strategic plan for 2008 to 2012, following an interim review and adjustments, was reviewed by the Board in December 2009. Progress on the implementation of the strategic plan was reported to and reviewed by the Board on a regular basis.

The annual and interim results of the Bank are announced in a timely manner within the limits of three months and two months respectively after the end of the relevant year or period.

The Directors acknowledge their responsibilities for preparing the accounts of the Bank. As at 31 December 2010, the Directors were not aware of any material uncertainties relating to events or conditions which may cast significant doubt upon the Bank's ability to continue as a going concern. Accordingly, the Directors have prepared the financial statements of the Bank on a going-concern basis.

The responsibilities of the external auditor with respect to financial reporting are set out in the Independent Auditor's Report attached to the Bank's 2010 Financial Statements.

Internal Controls

System and Procedures

The Board is responsible for internal control at the Bank and its subsidiaries and for reviewing its effectiveness.

The Bank's internal control system comprises a well-established organisational structure and comprehensive policies and standards. Areas of responsibilities for each business and functional unit are clearly defined to ensure effective checks and balances.

Procedures have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; and for ensuring the reliability of financial information used within the business or for publication. The procedures provide reasonable but not absolute assurance against material errors, losses or fraud. Procedures have also been designed to ensure compliance with applicable laws, rules and regulations.

Systems and procedures are in place in the Bank to identify, control and report on the major types of risks the Bank faces. Business and functional units are responsible for the assessment of individual types of risk arising under their areas of responsibilities, the management of the risks in accordance with risk management procedures and reporting on risk management. The Board maintains an effective risk management framework through the Risk Management Committee which reports to the Executive Committee by setting up of specialised management committees for supervision of major risk areas and the establishment of risk management departments for relevant functions of the Bank. The scope of responsibilities of the Audit Committee has also been recently expanded to cover risk management oversight. The relevant risk management reports are submitted to Asset and Liability

Management Committee, Risk Management Committee, Executive Committee and Audit Committee, and ultimately to the Board for monitoring the respective types of risk. The Bank's risk management policies and major control limits are approved by the Board or its delegated committees, and are monitored and reviewed regularly according to established procedures of the Bank.

More detailed discussions on the policies and procedures for management of each of the major types of risk the Bank faces, including credit, market, liquidity and operational risks, are included in the risk management section of the "Financial Review" under the Bank's 2010 Annual Report, and in Note 61 to the Bank's 2010 Financial Statements.

Annual Assessment

A review of the effectiveness of the Bank's internal control system covering all controls, including financial, operational and compliance, and risk management controls, is conducted annually. The review at the end of 2010 was conducted with reference to the COSO (The Committee of Sponsoring Organisations of the Treadway Commission) internal control framework, which assesses the Bank's internal control system against the five elements of control environment, risk assessment, control activities, communication and monitoring. The Bank has also conducted an annual review to assess the adequacy of resources, qualifications and experience of staff of the Bank's accounting and financial reporting function, and their training programmes and budget. The approach, findings, analysis and results of these annual reviews have been reported to the Audit Committee and the Board.

Framework for Disclosure of Price Sensitive Information

The Bank has put in place a robust framework for the disclosure of price-sensitive information in compliance with the Listing Rules and other regulatory requirements in this respect. The framework sets out the procedures and internal controls for the handling and dissemination of price-sensitive information in a timely manner so as to allow the shareholders, customers, staff and other stakeholders to apprehend the latest position of the Bank and its subsidiaries. The framework and its effectiveness are subject to review on a regular basis according to established procedures.

Internal Audit

The internal audit function plays an important role in the Bank's internal control framework. It monitors the effectiveness of internal control procedures and compliance with policies and standards across all business and functional units. All management letters from external auditor and reports from regulatory authorities will be reviewed by the Audit Committee and all recommendations will be implemented. The Management is required to provide the internal audit function with an annual written confirmation that it has acted fully on all recommendations made by external auditor and regulatory authorities. The internal audit function also advises the Management on operational efficiency and other risk management issues. The work of the internal audit function is focused on areas of greatest risk to the Bank as determined by risk assessment. The Bank's Head of Audit reports to the Chairman and the Audit Committee.

External Auditor

KPMG is the Bank's external auditor. The Audit Committee is responsible for making recommendations to the Board on the appointment, reappointment, removal and remuneration of the external auditor. The external auditor's independence and objectivity are also reviewed and monitored by the Audit Committee on a regular basis.

During 2010, fees paid to the Bank's external auditor for audit services amounted to HK\$13.3m, compared with HK\$13.4m in 2009. For non-audit services, the fees paid to the Bank's external auditor amounted to HK\$5.8m, compared with HK\$5.6m in 2009. In 2010, the significant non-audit service assignments covered by these fees include the following:

Nature of service	Fees paid (HK\$m)
Other assurance services	5.7
Tax services	0.1
	<u>5.8</u>

Audit Committee

The Audit Committee assists the Board in meeting its responsibilities for ensuring effective systems of risk management, internal control and compliance, and in meeting its financial reporting obligations.

COMMUNICATION WITH SHAREHOLDERS

Effective Communication

The Bank attaches great importance to communication with shareholders. To this end, a number of means are used to promote greater understanding and dialogue with the investment community. The Bank holds group meetings with analysts in connection with the Bank's annual and interim results. The results announcements are also broadcast live via webcast. Apart from the above, designated senior executives maintain regular dialogue with institutional investors and analysts to keep them abreast of the Bank's development, subject to compliance with the applicable laws and regulations. Including the two results announcements, a total of 95 meetings with 308 analysts and fund managers from 222 companies were held in 2010. In addition, the Bank's Vice-Chairman and Chief Executive; and Chief Financial Officer also made presentations and held group meetings with investors at investor forums in Hong Kong and overseas.

Further, the Bank's website (www.hangseng.com) contains an investor relations section which offers timely access to the Bank's press releases and other business information. For efficient communication with shareholders and in the interest of environmental preservation, shareholders are encouraged to browse the Bank's corporate communications on the Bank's website, in the place of receiving printed copies of the same.

The Annual General Meeting provides a useful forum for shareholders to exchange views with the Board. The Bank's Chairman, Executive Directors, Chairmen of the Board Committees and Non-executive Directors are available at the Annual General Meeting to answer questions from shareholders. Separate resolutions are proposed at general meetings for each substantial issue, including the re-election and election (as the case may be) of individual Directors. An explanation of the detailed procedures of conducting a poll will be provided to shareholders at the commencement of the Annual General Meeting, to ensure that shareholders are familiar with such procedures.

The Bank's last Annual General Meeting was held on Friday, 14 May 2010 at Hang Seng Bank Headquarters, 83 Des Voeux Road Central, Hong Kong. All the resolutions proposed at that meeting were approved by the shareholders by poll voting. Details of the poll results are available under the investor relations section of the Bank's website at www.hangseng.com.

The next Annual General Meeting will be held on Friday, 13 May 2011, the notice of which will be sent to shareholders at least 20 clear business days before the said meeting. Shareholders may refer to the section "Corporate Information and Calendar" in this Annual Report for information on other important dates for shareholders in year 2011.

OTHER INFORMATION

The Annual and Interim Reports contain comprehensive information on business strategies and developments. Discussions and analyses of the Bank's performance during 2010 and the material factors underlying its results and financial position can be found in the sections "Business in Hong Kong", "Business on the Mainland" and "Financial Review" in this Annual Report.

Material Related Party Transactions and Contracts of Significance

The Bank's material related party transactions are set out in Note 60 to the 2010 Financial Statements. These transactions include those that the Bank has entered into with its immediate holding company and fellow subsidiary companies in the ordinary course of its interbank activities, including the acceptance and placement of interbank deposits, corresponding banking transactions, off-balance sheet transactions, and the provision of other banking and financial services.

The Bank uses the information technology services of, and shares an automated teller machine network with, The Hongkong and Shanghai Banking Corporation Limited, its immediate holding company. The Bank also shares information technology and certain processing services with fellow subsidiaries on a cost recovery basis. In 2010, the Bank's share of the costs includes HK\$164m for system development, HK\$214m for data processing, and HK\$168m for administrative services.

The Bank maintains a staff retirement benefit scheme for which a fellow subsidiary company acts as insurer and administrator. As part of its ordinary course of business with other financial institutions, the Bank also markets Mandatory Provident Fund products and distributes retail investment funds for fellow subsidiaries, with a fee income of HK\$209m and HK\$81m respectively in 2010. Hang Seng Investment Management Limited, a wholly owned subsidiary of the Bank, manages in the ordinary course of its business a fund administered by a fellow subsidiary, to which management fee rebates were made. The rebate for 2010 amounted to HK\$137m.

These transactions were entered into by the Bank in the ordinary and usual course of business on normal commercial terms, and in relation to those which constituted connected transactions under the Listing Rules, they also complied with applicable requirements under the Listing Rules. The Bank regards its usage of the information technology services of The Hongkong and Shanghai Banking Corporation Limited (amount of information technology services cost incurred for 2010: HK\$478m) as contracts of significance for 2010.

Connected Transaction and Continuing Connected Transactions

Connected Transaction

On 20 May 2010, Hang Seng Bank (China) Limited ("HACN"), a wholly-owned subsidiary of the Bank, entered into a sale and purchase agreement with HSBC Bank (China) Company Limited ("HBCN") and Shanghai Senmao International Real Estate Company Limited. Pursuant to the aforesaid agreement, HACN conditionally agreed to acquire (the "Acquisition") from HBCN, Unit 101 and the whole of 34th, 35th and 36th Floors (the "Property") of HSBC Tower (now renamed as Hang Seng Bank Tower) (the "Building") at 1000 Lujiazui Ring Road, Shanghai, the People's Republic of China, together with the right to the exclusive use of certain car parking spaces, and the naming right in respect of the Building and the right to put up signages on certain designated places of the Building (collectively the "Naming and Signage Rights"), at a total consideration of RMB510m.

Following the completion of all conditions precedent, the Acquisition was completed on 16 September 2010. The consideration was funded by internal resources of the Group.

HACN would relocate its headquarters to the Property for its long term development and achievement of the China strategies of the Group. The acquisition of the Naming and Signage Rights would serve the dual purposes of enhancing the Group's corporate profile and image on the Mainland, and signifying its commitment to the mainland market.

The Directors (including the Independent Non-executive Directors) consider that the Acquisition is in the ordinary and usual course of business of the Bank and the terms of the Acquisition are on normal commercial terms, fair and reasonable and in the interests of the Bank and its shareholders as a whole.

HBCN is a wholly-owned subsidiary of HSBC Holdings plc ("HSBC"), the controlling shareholder of the Bank and therefore a connected person of the Bank. Accordingly, the Acquisition constituted a connected transaction for the Bank under the Listing Rules. An announcement relating to the aforesaid was issued by the Bank on 20 May 2010. The Bank has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules.

Continuing Connected Transactions

- (a) On 22 June 2007, Hang Seng Life Limited ("HSL") entered into the following agreements, which expired on 21 June 2010:
 - (i) A management services agreement ("Previous Management Services Agreement") for a term of three years with HSBC Life (International) Limited ("INHK"), pursuant to which INHK would continue to provide certain management services, being services relating to risk management, back office processing and administration, development and pricing for selected products, information technology and business recovery, financial control and actuarial services (the "Management Services"), to HSL to enable HSL to conduct its life insurance business.

INHK charged HSL for the provision of the services on a fully absorbed cost basis plus a mark-up of 5%. These charges were determined following negotiation on an arm's length basis and in accordance with the policy of HSBC Group, which took into account the transfer pricing guidelines of UK and the Organisation for Economic Co-operation and Development ("OECD").

- (ii) An investment management agreement (“Previous Investment Management Agreement”) for a term of three years with HSBC Global Asset Management (Hong Kong) Limited (formerly known as HSBC Investments (Hong Kong) Limited) (“ISHK”), pursuant to which ISHK would continue to act as investment manager in respect of certain of HSL’s assets held from time to time to maintain business continuity of HSL.

HSL paid to ISHK a fee of between 0.17% and 0.375% per annum of the mean value of the assets under management, which was determined on an arm’s length basis.

HSL has become a wholly-owned subsidiary of Hang Seng Insurance Company Limited (“HSIC”), which in turn is a wholly-owned subsidiary of the Bank, since September 2007. As part of the plan of the Bank to rationalise its insurance business structure, HSL’s long term insurance business has been integrated into that of HSIC. Accordingly, all rights and obligations under the agreements entered into between HSL and the third parties have then been novated to HSIC. These agreements include, among others, the Previous Management Services Agreement and the Previous Investment Management Agreement.

Details of the terms of and the annual caps under the Previous Management Services Agreement and the Previous Investment Management Agreement for the years 2007, 2008 and 2009 were announced by the Bank on 22 June 2007. The Bank has also set the caps under each of the aforesaid agreements for the period from 1 January to 22 June 2010, details of which were announced by the Bank on 18 December 2009.

- (b) On 22 June 2010, HSIC entered into the following new agreements:

- (i) a new management services agreement (“New Management Services Agreement”) with INHK for a term of three years commencing from 22 June 2010, pursuant to which INHK, directly or through one or more of its affiliates, would provide the Management Services to HSIC.

INHK will charge HSIC for the provision of the services on a fully absorbed cost basis plus a mark-up of 5%, which is the same as that under the Previous Management Services Agreement. These charges have been determined following negotiation on an arm’s length basis and in accordance with the policy of the HSBC Group, which takes into account UK and OECD transfer pricing guidelines.

- (ii) a new investment management agreement (“New Investment Management Agreement”) with ISHK for a term of three years commencing from 22 June 2010, pursuant to which ISHK would act as investment manager in respect of certain of HSIC’s assets held from time to time.

HSIC will pay, on a quarterly basis, to ISHK a fee of between 0.17% and 0.375% per annum of the mean value of the assets under management, which is equal to the fee payable under the Previous Investment Management Agreement and has been determined on an arm’s length basis.

Details of the terms of and the caps under the New Management Services Agreement and the New Investment Management Agreement for the period from 22 June to 31 December 2010, and for the years ending 31 December 2011 and 2012, and for the period from 1 January to 21 June 2013, were announced by the Bank on 22 June 2010.

The Directors believed that the New Management Services Agreement would enable HSIC to run at a reasonably low cost structure by leveraging on the shared infrastructure and expertise of INHK. The resulting cost efficiency has contributed to increased competitiveness of HSIC’s manufactured products in the market, which the Directors considered to be essential to the future business growth of HSIC.

The New Investment Management Agreement was based on the commercial terms set out in the Previous Investment Management Agreement and the Directors (including the Independent Non-executive Directors) believed that these terms should remain in place.

INHK and ISHK are both indirect wholly-owned subsidiaries of HSBC, the controlling shareholder of the Bank and therefore are connected persons of the Bank. Accordingly, the Previous Management Services Agreement, the Previous Investment Management Agreement, the New Management Services Agreement and the New Investment Management Agreement all constituted continuing connected transactions of the Bank. The Bank has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules.

For the year ended 31 December 2010, the aggregate amount paid under the Previous and the New Management Services Agreements was HK\$97m, whereas the aggregate amount paid under the Previous and the New Investment Management Agreements was HK\$52m.

In respect of the agreements mentioned in paragraphs (a) and (b) above which constituted the Bank's continuing connected transactions, all the Independent Non-executive Directors of the Bank have reviewed the said transactions and confirmed that the said transactions have been entered into:

- (1) in the ordinary and usual course of business of the Group;
- (2) on normal commercial terms; and
- (3) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the Bank and its shareholders as a whole.

Further, the Bank has engaged its external auditor to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditor has issued an unqualified letter containing their findings and conclusions in respect of the continuing connected transactions set out in paragraphs (a) and (b) above in accordance with Listing Rule 14A.38. A copy of the auditor's letter has been provided by the Bank to The Stock Exchange of Hong Kong Limited.

Human Resources

The human resources policies of the Bank are designed to attract people of the highest calibre and to motivate them to excel in their careers, as well as uphold the Bank's brand equity and culture of quality service.

Employee Statistics

As at 31 December 2010, the Bank's total headcount was 9,642, representing an increase by 300, or 3.2%, compared with a year earlier. The total headcount comprised 1,251 executives, 3,896 officers and 4,495 clerical and non-clerical staff.

Grading Structure

To simplify the Bank's job grade structure and to facilitate the implementation of a market pay strategy, "Broadbanding" is introduced to replace the Bank's existing grading structure with effect from 1 January 2011.

The broad-banded structure allows for greater ease of movement by enabling career and/or salary progression without the prerequisite of changing job grade. It also provides flexibility to match internal pay levels to market trends and to differentiate rewards based on performance and potential.

The implementation of Broadbanding will facilitate the Bank in adopting a market-led strategy which helps to attract, develop and motivate the best employees which should ultimately result in improved productivity and achievement of business objectives.

Employee Remuneration

The Bank has adopted the Total Reward Approach which focuses on staff's total compensation with fixed pay based on individual market pay position and variable pay differentiated by performance. To facilitate the implementation of the Bank's performance-based reward strategy, individual and business performances are assessed systemically against pre-determined business, compliance and risk management objectives in guiding reward decisions. In determining the total remuneration for employees, the Bank will take into account the seniority, responsibility, remuneration package and risk profile to ensure an appropriate balance between the fixed pay and variable pay.

Fixed pays take into account levels and composition of pay in the markets in which the Bank operates. Salaries are reviewed in the context of individual and business performance, market practice, internal relativities, risk management requirements and competitiveness compared to peers.

Under appropriate circumstances, performance-related variable pay is provided as an incentive for those eligible staff members under performance-based remuneration strategy. In determining the size and allocation of variable pay budget, the Bank will take into consideration the Bank's performance over the longer term, the economic outlook, market practices, risk appetite, capital and liquidity position as well as other non-financial factors. Variable pays for individual employees are differentiated with their responsibilities, performance, potential, and contributions. According to specific variable pay award criteria, a portion of variable pay of senior staff is deferred in the share award so as to tie them to the future performance of the Group and ensure effective alignment of incentive reward to effective risk management. The deferred share award has a vesting period of three years; with gradual vesting on a pro-rata basis commencing from the first anniversary of the date of award. The vesting of share award is also subject to the employee's continued employment.

In addition, the Bank has participated in the HSBC Holdings Savings-related Share Option Plan ("Sharesave"), under which staff members can make monthly savings for the purchase of shares of HSBC Holdings plc after a specified period. For Sharesave 2010, 2,349 staff members have subscribed to the plan.

Employee Involvement

Communication with staff is a key aspect of the Bank's policies. Information relating to employment matters, the Bank's business direction and strategies, and factors affecting the Bank's performance are conveyed to staff via different channels, including an intranet site, in-house magazines, morning broadcasts and training programmes.

The fourth bankwide Global People Survey was conducted in June 2010 as a continuous initiative to measure staff engagement level. The results were very positive as the employee engagement index was among the best in class. Communication sessions to staff were organised to share the survey results and collect feedback for continual enhancement.

Staff Development

In order to fully develop staff capability and potential, the Bank offers a wide range of training and development programmes that help the staff fulfill their personal career goals and professional requirements, including those for regulated businesses and activities, and equip them to meet future challenges.

New staff joining the Bank will participate in a comprehensive induction programme that provides them with an understanding of the Bank's history, culture, values and corporate governance. Sustainable development of staff is enabled through multiple learning channels, including instructor-led training courses and web-based learning via an intranet platform. Staff members are also encouraged to pursue professional or academic qualifications through the Bank's Professional Qualifications and Education Award Scheme.

A talent strategy has been in place with the aim to provide a ready, good quality internal pipeline to fill critical positions, and to build talents to feed leadership roles across the Bank. Identified talents are populated into the succession plans to critical positions and are provided with a mix of development interventions to accelerate their growth.

On average, our staff members received six days of training in 2010.

Recruitment and Retention

The employment market was very active especially in the second half of 2010. Vigorous recruitment activities continued to meet business needs and for replacement of staff turnover, especially for front-line sales positions, experienced professionals and specialists.

There were also conscious efforts on retention of talents and key staff. As part of the Bank's staff retention strategies, remuneration packages and career paths for certain job positions have been reviewed to increase career advancement opportunities and ensure market competitiveness. Further, trainee programmes have been provided for jobs in selected functional areas in order to build pipeline for succession.

Business principles and values

The Bank has adopted HSBC Group's business principles and values requiring staff to keep the highest personal standards of integrity at all levels, to commit to truth, fair dealing, quality and competence as well as to comply with the spirit and letter of all laws and regulations when conducting business. "Commitment to integrity and ethics" is also one of the expectations on its staff. Staff members are required to adhere strongly to high professional ethics and demonstrate an honest and credible character in work as well as in the relationship with the Bank's customers.

Code of Conduct

To ensure the Bank operates according to the highest standards of ethical conduct and professional competence, all staff are required to strictly follow the Code of Conduct contained in the Bank's Staff Handbook. With reference to the applicable regulatory guidelines and other industry best practices, the Code sets out ethical standards and values to which all the Bank's staff are required to adhere and covers various legal, regulatory and ethical issues. These include topics such as prevention of bribery, dealing in securities, personal benefits, outside employment and anti-discrimination policies.

The Bank uses various communication channels to periodically remind staff of the requirement to adhere to the rules and ethical standards set out in the Code of Conduct.

Health and Safety

The Bank acknowledges and accepts its responsibilities for securing the health, safety and welfare of all its employees, of contractors working at premises over which it has control, and

of visiting members of the public. By successfully implementing the certified BS OHSAS 18001:2007-compliant Safety Management System, the Bank marks its achievement to be the first bank world-wide to conform to this internationally acclaimed best practice aiming at reducing the exposure of the Bank's staff and customers to occupational safety and health risks associated with its business activities.

The Bank provides a range of training and promotional activities to enhance the knowledge of its staff in occupational safety and health, fire safety, manual handling, and office safety.

The Bank maintains a Contingency Plan for Communicable Disease. This sets out the key issues to be addressed and the actions to be taken by various units in the event of the occurrence of a serious communicable disease, and the arrangement of keeping adequate stock of Face Masks and Tamiflu by the Bank to cater for the needs of its staff in case of an outbreak of influenza pandemic. Staff have been made aware through various communication channels of the importance of personal hygiene and health, and informed of the contingency measures to be adopted. This is to ensure that the Bank will be in a position to continue with its services to the community in the event of an outbreak of a serious communicable disease.

The Bank also operates a Staff Recreation Centre at Kowloon Bay with various facilities for health enhancement and leisure activities as a means to foster work life balance among its staff and their family members.

Corporate Governance Recognition

In recognition of the Bank's continuous excellence in and reputation for its leading approach to good corporate governance, it was named No.3 in the Best Corporate Governance Awards in Hong Kong by Euromoney, a leading financial sector publication, in 2010. The Euromoney's award, which was based on a survey of market analysts at leading banks and research institutes in Asia, affirmed the Bank's adherence to the highest standards of business ethics and corporate governance.