

Report of the Directors: Corporate Governance

Corporate Governance Report / Letter from the Group Chairman

Corporate Governance

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¹ Appendix to Report of the Directors.

Corporate Governance Report

The statement of corporate governance practices set out on pages 301 to 370 and information incorporated by reference constitutes the Corporate Governance Report of HSBC Holdings. The reports of Board Committees are contained within the Corporate Governance Report.

Letter from the Group Chairman

Dear Shareholder

At HSBC, we are committed to the highest standards of corporate governance. This is more important than ever in light of developments and changes in regulatory policy for financial services, society's view of the role of banks and the need to maintain investor confidence. We believe that a strong and transparent corporate governance framework is directly linked to the long-term success of the Group.

A values-led culture, high behavioural standards and robust procedures are fundamental to a strong corporate governance framework. As we reported to you last year, a renewed emphasis has been placed on values at HSBC, ensuring our employees are empowered to do the right thing and act with courageous integrity. The role played by HSBC Values in daily operating practice is fundamental to our culture and HSBC Values continue to be embedded in how we conduct our business.

In my statement to shareholders on pages 4 to 7 of the *Annual Report and Accounts 2012*, I outline the significant challenges faced by the Group, both during the year and in the future, and the way we endeavour to address these challenges. We now have the structure to help us reduce complexity and to run the Group more effectively on a global basis. We are formulating and implementing global standards to ensure that our conduct matches our values.

In this Corporate Governance Report, we outline the way in which the Group's corporate governance framework operates, including the role and responsibilities of the Board and each of its Committees. We continue to review and develop this framework in light of changes in the Group's businesses and the external environment, taking into account the views of external parties where appropriate. As in previous years, we have benefited from input from a third-party facilitator whose report was used by the Board in its annual review of its own effectiveness.

Ensuring there is an appropriate balance of skills, knowledge and experience on the Board is an important aspect of corporate governance. The expertise and experience of our Board was augmented in 2012 with the appointments of Joachim Faber, former Chief Executive Officer of Allianz Global Investors AG, and John Lipsky, former First Deputy Managing Director of the International Monetary Fund. It was augmented further in 2013 with the appointments of Renato Fassbind, former Chief Financial Officer of Credit

Report of the Directors: Corporate Governance (continued)

Letter from the Group Chairman / Directors

Suisse Group SA, and Jim Comey, former United States Deputy Attorney General.

We have also taken steps to strengthen non-executive oversight of matters relating to anti-money laundering, sanctions, terrorist financing and proliferations financing. A new Board committee, the Financial System Vulnerabilities Committee ('FSVC'), will provide governance, oversight and policy guidance over the framework of controls and procedures designed to identify areas where HSBC may become exposed, and through that exposure, expose the financial system more broadly to financial crime or system abuse. The FSVC will use the knowledge and experience of its members to place the Group in a position of leadership in this area and will provide the Board with a forward-looking perspective on financial crime risk.

The executive committee structure has been enhanced during the year with the establishment of a regular separate meeting of the Group Management Board to focus on developing and implementing global standards reflecting best practices which must be adopted and adhered to consistently throughout the Group.

During the year, the Board adopted a Board diversity policy, which is consistent with the Group's strategic focus on ethnicity, age and gender diversity for the employee base. At the 2011 Annual General Meeting, I stated the Board's intention to exceed the aspirational target set by Lord Davies in his report *Women on Boards* of 25% female representation on the boards of FTSE 100 companies by 2015. Our policy re-states this intention.

We recognise that our strategy to be the world's leading international bank relies on a foundation of good corporate governance and we endeavour to be at the forefront of this field in the coming years.



D J Flint, *Group Chairman*
4 March 2013

Directors

D J Flint, CBE, 57
Group Chairman

Skills and experience: extensive governance experience gained through membership of the Boards of HSBC and BP p.l.c.; considerable knowledge of finance and risk management in banking, multinational financial reporting, treasury and securities trading operations; honoured with a CBE in recognition of his services to the finance industry; member of the Institute of Chartered Accountants of Scotland and the Association of Corporate Treasurers. Fellow of The Chartered Institute of Management Accountants. Joined HSBC in 1995.

Appointed to the Board: 1995

Current appointments include: director of The Hong Kong Association; and Chairman of the Institute of International Finance since 6 June 2012. A member of the Mayor of Beijing's International Business Leaders' Advisory Council as well as the Mayor of Shanghai's International Business Leaders' Advisory Council; and a member of the International Advisory Board of the China Europe International Business School, Shanghai.

Former appointments include: Group Finance Director and Chief Financial Officer; and Executive Director, Risk and Regulation. Co-Chairman of the Counterparty Risk Management Policy Group III; Chairman of the Financial Reporting Council's review of the Turnbull Guidance on Internal Control; member of the Accounting Standards Board and the Standards Advisory Council of the International Accounting Standards Board; served on the Large Business Forum on Tax and Competitiveness and the Consultative Committee of the Large Business Advisory Board of HM Revenue and Customs; partner in KPMG; and non-executive director and Chairman of the Audit Committee of BP p.l.c.

ST Gulliver, 53
Group Chief Executive

Skills and experience: a career banker with over 30 years' international experience with HSBC; has held a number of key roles in the Group's operations worldwide, including in London, Hong Kong, Tokyo, Kuala Lumpur and the United Arab Emirates; played a leading role in developing and expanding Global Banking and Markets, the wholesale banking

division of the Group with operations in over 65 countries and territories. Joined HSBC in 1980.

Appointed to the Board: 2008

Current appointments include: Chairman of The Hongkong and Shanghai Banking Corporation Limited; and Chairman of the Group Management Board. A member of the Monetary Authority of Singapore International Advisory Panel since 1 June 2012 and a member of the International Advisory Council of the China Banking Regulatory Commission since 10 July 2012.

Former appointments include: Chairman, Europe, Middle East and Global Businesses and Chairman of HSBC Bank plc, HSBC Bank Middle East Limited and HSBC Private Banking Holdings (Suisse) SA. Head of Global Banking and Markets; Co-Head of Global Banking and Markets; Head of Global Markets; Head of Treasury and Capital Markets in Asia-Pacific; Deputy Chairman of HSBC Trinkaus & Burkhardt AG and a member of its Supervisory Board. Ceased to be Chairman of HSBC France on 22 November 2012.

SA Catz[†], 51

Skills and experience: a background in international business leadership, having helped transform Oracle into the largest producer of business management software and the world's leading supplier of software for information management.

Appointed to the Board: 2008

Current appointments include: President and Chief Financial Officer of Oracle Corporation. Joined Oracle in 1999 and appointed to the board of directors in 2001.

Former appointments include: Managing Director of Donaldson, Lufkin & Jenrette.

LM L Cha[†], GBS, 63

Member of the Corporate Sustainability Committee and, since 1 January 2013, Chairman.

Skills and experience: extensive regulatory and policy making experience in the finance and securities sector in Hong Kong and mainland China; formerly Vice Chairman of the China Securities Regulatory Commission, being the first person outside mainland China to join the Central Government of the People's Republic of China at vice-ministerial rank; awarded Gold and Silver Bauhinia Stars by the Hong Kong Government for public service; formerly Deputy Chairman of the Securities and Futures Commission

in Hong Kong; and has worked in the US and Asia.

Appointed to the Board: 2011

Current appointments include: non-executive Deputy Chairman of The Hongkong and Shanghai Banking Corporation Limited; non-official member of the Executive Council of Hong Kong SAR; a Hong Kong Deputy to the 12th National People's Congress of China; non-executive director of China Telecom Corporation Limited; member of the Advisory Board of the Yale School of Management; Senior International Advisor for Foundation Asset Management Sweden AB; member of the State Bar of California; and Chairman of the Financial Services Development Council of Hong Kong SAR since 17 January 2013. Appointed a non-executive director of Unilever PLC with effect from 14 May 2013.

Former appointments include: non-executive director of Bank of Communications Co., Ltd., Baoshan Iron and Steel Co. Limited; Johnson Electric Holdings Limited; and Chairman of the University Grants Committee in Hong Kong. Ceased to be a director of Hong Kong Exchanges and Clearing Limited on 24 April 2012; Tata Consultancy Services Limited on 29 June 2012; Chairman of the ICAC Advisory Committee on Corruption on 31 December 2012; and Chairman of the Task Force on the Financial Services Development Council of Hong Kong SAR on 17 January 2013.

M KT Cheung[†], GBS, OBE, 65

Member of the Group Audit Committee.

Skills and experience: a background in international business and financial accounting, particularly in Greater China and the wider Asian economy; retired from KPMG Hong Kong in 2003 after more than 30 years; awarded the Gold Bauhinia Star by the Hong Kong Government. Fellow of the Institute of Chartered Accountants in England and Wales.

Appointed to the Board: 2009

Current appointments include: non-executive director of Hang Seng Bank Limited and HKR International Limited; non-executive Chairman of the Airport Authority Hong Kong and the Council of the Hong Kong University of Science and Technology; director of The Association of Former Council Members of The Stock Exchange of Hong Kong Limited and The Hong Kong International Film Festival Society Ltd; and a member of the Working Group on Transportation under the

Report of the Directors: Corporate Governance (continued)

Directors

Economic Development Commission of the Hong Kong SAR Government since 17 January 2013.

Former appointments include: non-executive director of Sun Hung Kai Properties Limited and Hong Kong Exchanges and Clearing Limited; Chairman and Chief Executive Officer of KPMG Hong Kong; and council member of the Open University of Hong Kong. Ceased to be a non-official member of the Executive Council of the Hong Kong SAR on 1 July 2012.

J B Comey[†], 52

Member of the Financial System Vulnerabilities Committee on 4 March 2013.

Skills and experience: extensive experience in both the public and private sectors in the US federal and state justice systems and as General Counsel to leading international businesses. Former US Deputy Attorney General responsible for supervising operations of the US Department of Justice. As US Attorney for the Southern District of New York, oversaw the prosecution of corporate executives on fraud and securities-related charges and international drug cartels.

Appointed to the Board: 4 March 2013

Current appointments include: Columbia University Law School, Senior Research Scholar and Hertog Fellow on National Security Law.

Former appointments include: General Counsel of Bridgewater Associates, LP; Senior Vice President and General Counsel of Lockheed Martin Corporation; US Deputy Attorney General; US Attorney for the Southern District of New York; and Assistant US Attorney for the Eastern District of Virginia.

J D Coombe[†], 67

Chairman of the Group Audit Committee and member of the Group Risk Committee and Group Remuneration Committee.

Skills and experience: a background in international business, financial accounting and the pharmaceutical industry. Formerly Chief Financial Officer of GlaxoSmithKline plc with responsibility for the group's financial operations globally. Fellow of the Institute of Chartered Accountants in England and Wales.

Appointed to the Board: 2005

Current appointments include: non-executive Chairman of Hogg Robinson Group plc and non-executive Chairman of Home Retail Group plc since 4 July 2012.

Former appointments include: executive director and Chief Financial Officer of GlaxoSmithKline plc; non-executive director of GUS plc; member of the Supervisory Board of Siemens AG; Chairman of The Hundred Group of Finance Directors; and member of the Accounting Standards Board. Ceased to be a council member of The Royal Academy of Arts on 18 September 2012.

J Faber[†], 62

Member of the Group Risk Committee since 1 March 2012.

Skills and experience: a background in banking and asset management with significant international experience, having worked in Germany, Tokyo, New York and London. Former Chief Executive Officer of Allianz Global Investors AG and member of the management board of Allianz SE; 14 years' experience with Citigroup Inc. holding positions in Trading and Project Finance and as Head of Capital Markets for Europe, North America and Japan. Has a doctorate from the University of Administrative Sciences in Speyer.

Appointed to the Board: 1 March 2012

Current appointments include: Chairman of the supervisory board of Deutsche Börse AG; Chairman of the Shareholder Committee of Joh A. Benckiser SARL from 1 January 2012; independent director of Coty Inc.; director of Allianz France S.A., Allianz Investment Management GmbH and Allianz Climate Solutions GmbH; and member of the advisory boards of the Siemens Group Pension Board, the European School for Management and Technology and the German Council for Sustainable Development.

Former appointments include: Chairman of Allianz Global Investors Kapitalanlagegesellschaft and Allianz Global Investors Deutschland GmbH; Chairman of the board of Allianz Global Investors SGR; and member of the board of Allianz SpA and of the supervisory board of Bayerische Boerse AG.

R A Fairhead[†], CBE, 51

Chairman of the Group Risk Committee and the Financial System Vulnerabilities Committee, and member of the Group Audit Committee and Nomination Committee.

Skills and experience: a background in international industry, publishing, finance and general management. Formerly Finance Director of Pearson plc with responsibility for overseeing the day-to-day running of the finance function and directly responsible for global financial reporting and control, tax and treasury. Has a Master's in Business Administration from the Harvard Business School.

Appointed to the Board: 2004

Current appointments include: Chairman and director of Financial Times Group Limited; director of Pearson plc and non-executive director of The Economist Newspaper Limited. Will retire from these appointments on 27 April 2013. Non-executive member of the board of the UK Government's Cabinet Office.

Former appointments include: Executive Vice President, Strategy and Group Control of Imperial Chemical Industries plc; Finance Director of Pearson plc; and Chairman and director of Interactive Data Corporation.

R Fassbind[†], 57

Member of the Group Audit Committee and the Group Remuneration Committee since 1 March 2013.

Skills and experience: a background in financial accounting and international business. Formerly Chief Financial Officer of Credit Suisse Group SA and ABB Group. Has a Master's in Business Administration and a PhD in Economics from the University of Zurich.

Appointed to the Board: 1 January 2013

Current appointments include: Vice Chairman of the Supervisory Board and member of the audit and compensation committees of Swiss Reinsurance Company; member of the supervisory board and audit committee of Kühne + Nagel International AG; independent director of Oanda Corporation; and member of the supervisory board of the Swiss Federal Audit Oversight Authority.

Former appointments include: Chief Financial Officer of Credit Suisse Group AG; Senior Advisor to the Chief Executive, Credit Suisse Group AG;

Chief Executive Officer of Diethelm Keller Group; Chief Financial Officer of ABB Group; Chairman of ABB (Switzerland) AG and DKSH AG; and a member of the supervisory board of Winterthur Insurance Company.

JW J Hughes-Hallett[†], CMG, SBS, 63

Member of the Nomination Committee and until 31 July 2012, the Group Risk Committee. Member of the Corporate Sustainability Committee since 1 January 2013.

Skills and experience: a background in financial accounting and experience of management of a broad range of international businesses, including aviation, insurance, property, shipping, manufacturing and trading in the Far East, UK, US and Australia. Awarded the Silver Bauhinia Star by the Hong Kong Government. Fellow of the Institute of Chartered Accountants in England and Wales.

Appointed to the Board: 2005

Current appointments include: Chairman of John Swire & Sons Limited; non-executive director of Cathay Pacific Airways Limited and Swire Pacific Limited; a trustee of the Esmée Fairbairn Foundation; member of The Hong Kong Association; and Chairman of the Governing Board of the Courtauld Institute of Art.

Former appointments include: non-executive director of The Hongkong and Shanghai Banking Corporation Limited and a trustee of the Dulwich Picture Gallery until 31 December 2012.

W S H Laidlaw[†], 57

Member of the Group Remuneration Committee.

Skills and experience: significant international experience, particularly in the energy sector, having had responsibility for businesses in four continents. Qualified Solicitor and Master's in Business Administration from INSEAD.

Appointed to the Board: 2008

Current appointments include: Chief Executive Officer of Centrica plc; and Lead Non-executive Board Member of the UK Department for Transport.

Former appointments include: Executive Vice President of Chevron Corporation; non-executive director of Hanson PLC; Chief Executive Officer of Enterprise Oil plc; and President and Chief Operating Officer of Amerada Hess Corporation. Ceased to be a member of the UK Prime Minister's Business Advisory Group on 31 December 2012.

Report of the Directors: Corporate Governance (continued)

Directors / Secretary / Adviser to the Board

J P Lipsky[†], 66

Member of the Group Risk Committee since 1 March 2012 and Nomination Committee since 24 May 2012.

Skills and experience: international experience having worked in Chile, New York, Washington and London and interacted with financial institutions, central banks and governments in many countries. Served at the International Monetary Fund as First Deputy Managing Director, Acting Managing Director and as Special Advisor. Has a PhD from Stanford University.

Appointed to the Board: 1 March 2012

Current appointments include: Distinguished Visiting Scholar, International Economics Program at the Paul H. Nitze School of Advanced International Studies, Johns Hopkins University. Co-chairman of the Aspen Institute Program on the World Economy; director of the National Bureau of Economic Research; and member of the advisory board of the Stanford Institute for Economic Policy Research and the Council on Foreign Relations. A director of the Center for Global Development since 1 May 2012; and Global Policy Advisor for Anderson Global Macro, LLC since 4 February 2013.

Former appointments include: Vice Chairman J P Morgan Investment Bank; director of the American Council on Germany and the Japan Society; and a trustee of the Economic Club of New York.

J R Lomax[†], 67

Member of the Group Audit Committee and Group Risk Committee.

Skills and experience: experience in both the public and private sectors and a deep knowledge of the operation of the UK government and financial system.

Appointed to the Board: 2008

Current appointments include: Chairman of the International Regulatory Strategy Group and a director of TheCityUK since 1 January 2013; non-executive director of The Scottish American Investment Company PLC, Reinsurance Group of America Inc., Arcus European Infrastructure Fund GP LLP and Heathrow Airport Holdings Limited (formerly BAA Limited); member of the Council of Imperial College, London; and President of the Institute of Fiscal Studies.

Former appointments include: Deputy Governor, Monetary Stability, at the Bank of England and member of the Monetary Policy Committee; Permanent Secretary at the UK Government Departments for Transport and Work and Pensions and the Welsh Office; and Vice President and Chief of Staff to the President of the World Bank.

I J Mackay, 51

Group Finance Director

Skills and experience: extensive financial and international experience, having worked in London, Paris, US and Asia. Member of the Institute of Chartered Accountants of Scotland. Joined HSBC in 2007.

Appointed to the Board: 2010

Current appointments include: member of the Group Management Board.

Former appointments include: director of Hang Seng Bank Limited; Chief Financial Officer, Asia-Pacific; and Chief Financial Officer, HSBC North America Holdings Inc; Vice President and Chief Financial Officer of GE Consumer Finance and Vice President and Chief Financial Officer of GE Healthcare – Global Diagnostic Imaging.

Sir Simon Robertson[†], 72

Deputy Chairman and senior independent non-executive Director

Chairman of the Nomination Committee and member of the Financial System Vulnerabilities Committee.

Skills and experience: a background in international corporate advisory with a wealth of experience in mergers and acquisitions, merchant banking, investment banking and financial markets; honoured with a knighthood in recognition of his services to business; extensive international experience having worked in France, Germany, the UK and the US.

Appointed to the Board: 2006

Current appointments include: non-executive Chairman of Rolls-Royce Holdings plc until 2 May 2013. The founding member of Robertson Robey Associates LLP, formerly Simon Robertson Associates LLP; non-executive director of Berry Bros. & Rudd Limited, The Economist Newspaper Limited; and, since 8 May 2012, Troy Asset Management; partner of NewShore Partners LLP; and trustee of the Eden Project Trust and the Royal Opera House Endowment Fund.

Former appointments include: Managing Director of Goldman Sachs International and Chairman of Dresdner Kleinwort Benson. Ceased to be a non-executive director of Royal Opera House, Covent Garden Limited on 31 July 2012.

J L Thornton[†], 59

Chairman of the Group Remuneration Committee.

Skills and experience: experience that bridges developed and developing economies and the public and private sectors. A deep knowledge of financial services and education systems, particularly in Asia. During his 23-year career with Goldman Sachs, he played a key role in the firm's global development and was Chairman of Goldman Sachs Asia.

Appointed to the Board: 2008

Current appointments include: non-executive Chairman and director of HSBC North America Holdings Inc.; Director and Co-Chairman of Barrick Gold Corporation since 15 February 2012 and 5 June 2012 respectively; professor and director of the Global Leadership Program at the Tsinghua University School of Economics and Management; Chairman of the Brookings Institution Board of Trustees; non-executive director of Ford Motor Company and China Unicom (Hong Kong) Limited; director of National Committee on United States-China Relations; trustee of China Institute and the China Foreign Affairs University; and member of the Council on Foreign Relations and the China Securities Regulatory Commission International Advisory Committee.

Former appointments include: non-executive director of Industrial and Commercial Bank of China Limited and Intel Corporation, Inc.; trustee of Asia Society; and President of the Goldman Sachs Group, Inc. Ceased to be a non-executive director of News Corporation, Inc. on 30 November 2012.

[†] *Independent non-executive Director.*

Secretary

R G Barber, 62

Group Company Secretary and Head of Corporate Governance

Joined HSBC in 1980. Group Company Secretary since 1986 and Company Secretary of HSBC Holdings plc since 1990. Appointed a Group General Manager in 2006. Chairman of the Disclosure Committee. A member of the Listing Authority Advisory Committee of the Financial Services Authority and of the Primary Markets Group of the London Stock Exchange. Fellow of the Institute of Chartered Secretaries and Administrators. Former HSBC appointments include: Corporation Secretary of The Hongkong and Shanghai Banking Corporation Limited and Company Secretary of HSBC Bank plc.

Adviser to the Board

D J Shaw, 66

Adviser to the Board since 1998. Director of HSBC Bank Bermuda Limited. Ceased to be a director of HSBC Private Banking Holdings (Suisse) SA and HSBC Private Bank (Suisse) SA on 19 September 2012. An independent non-executive director of Kowloon Development Company Limited and Shui On Land Limited. A solicitor and formerly a partner in Norton Rose.

Report of the Directors: Corporate Governance (continued)

Group Managing Directors / Board of Directors > Directors

Group Managing Directors

A Almeida, 56

Group Head of Human Resources and Corporate Sustainability

Joined HSBC in 1992. A Group Managing Director since 2008. Former HSBC appointments include: Global Head of Human Resources for Global Banking and Markets, Global Private Banking, Global Transaction Banking and HSBC Amanah.

S Assaf, 52

Chief Executive, Global Banking and Markets

Joined HSBC in 1994. A Group Managing Director since 2011. Chairman of HSBC France since 22 November 2012. A director of HSBC Trinkaus & Burkhardt AG. Former HSBC appointments include: director of HSBC Global Asset Management Limited; Head of Global Markets; and Head of Global Markets for Europe, Middle East and Africa. Ceased to be a director of HSBC Bank Egypt S.A.E. on 7 November 2012.

I M Dornier, 58

President and Chief Executive Officer of HSBC USA

Joined HSBC in 1986. A Group Managing Director since 1 February 2013. Chairman of HSBC Bank USA, National Association and HSBC USA Inc.; President and Chief Executive Officer of HSBC North America Inc. Former HSBC appointments include: Chairman of HSBC Amanah Malaysia Berhad and HSBC Amanah Takaful (Malaysia) Sendirian Berhad; Deputy Chairman and Chief Executive Officer of HSBC Bank Malaysia Berhad; Chief Operating Officer, Treasury and Capital Markets; General Manager of Marketing, General Manager of Human Resources; and General Manager of Premier and Wealth Management, HSBC Bank plc.

J M Flint, 44

Chief Executive, Retail Banking and Wealth Management

Joined HSBC in 1989. A Group Managing Director since 1 January 2013. A director of HSBC Bank Canada since 15 February 2012. Former HSBC appointments include: Chief of Staff to the Group Chief Executive and Group Head of Strategy and Planning; Chief Executive Officer, HSBC Global

Asset Management; Group Treasurer; and Deputy Head of Global Markets.

M P Kaur, 49

Group Head of Internal Audit

Will join HSBC and become a Group Managing Director on 1 April 2013. Former appointments include: Global Head of Group Audit for Deutsche Bank AG; Chief Financial Officer & Chief Operating Officer, Restructuring & Risk Division, Royal Bank of Scotland Group plc; Group Head of Compliance and Anti-Money Laundering, Lloyds TSB; and Global Director of Compliance, Global Consumer Group, Citigroup.

A M Keir, 54

Global Head of Commercial Banking

Joined HSBC in 1981. A Group Managing Director since 2011. Former HSBC appointments include: Group General Manager, Commercial Banking, Europe and Global Co-Head, Global Commercial Banking.

S A Levey, 49

Chief Legal Officer

Joined HSBC on 13 January 2012. A Group Managing Director since 18 January 2012. Former appointments include: Under Secretary for Terrorism and Financial Intelligence in the US Department of Treasury; Senior Fellow for National Security and Financial Integrity at the Council on Foreign Relations; Principal Associate Deputy Attorney General at the US Department of Justice; and Partner at Miller, Cassidy, Larroca & Lewin LLP and Baker Botts LLP.

A M Losada, 58

Chief Executive, Latin America and the Caribbean

Joined HSBC in 1973. A Group Managing Director since 1 December 2012. Chairman of HSBC Bank (Panama) S.A. since 6 February 2012. A director of HSBC Bank Argentina S.A. since 2 May 2012 and a director of HSBC Mexico, S.A., Institucion de Banca Multiple, Grupo Financiero HSBC and Grupo Financiero HSBC, S.A. de C.V. since 20 February 2012. Former HSBC appointments include: Chief Executive Officer, HSBC Argentina; and Deputy Head, Personal Financial Services, Brazil.

M M Moses, 55

Group Chief Risk Officer

Joined HSBC in 2005. A Group Managing Director since 2010. Director of HSBC Insurance (Bermuda) Limited. A director of HSBC Private Bank (Suisse) SA and HSBC Private Banking Holdings (Suisse) SA since 19 September 2012. Former HSBC appointments include Chief Financial and Risk Officer, Global Banking and Markets.

S P O'Sullivan, 57

Group Chief Operating Officer

Joined HSBC in 1980. A Group Managing Director since 2011. Former HSBC appointments include: Group Chief Technology and Services Officer; director and Chief Operating Officer of HSBC Bank plc; and Chief Operating Officer of HSBC Bank Canada.

B Robertson, 58

Chief Executive, HSBC Bank plc

Joined HSBC in 1975. A Group Managing Director since 2008. Chairman of HSBC Life (UK) Limited. Director of HSBC Bank Bermuda Limited since 1 January 2012. Former HSBC appointments include: Group Chief Risk Officer; Group General Manager, Group Credit and Risk; and Head of Global Banking and Markets for North America.

PT S Wong, 61

Chief Executive, The Hongkong and Shanghai Banking Corporation Limited

Joined HSBC in 2005. A Group Managing Director since 2010. Chairman of HSBC Bank (China) Company Limited and HSBC Bank Malaysia Berhad. Non-executive director of Hang Seng Bank Limited and Bank of Communications Co., Ltd. Independent non-executive director of Cathay Pacific Airways Limited. Former HSBC appointments include: director of HSBC Bank Australia Limited. Ceased to be Vice Chairman of HSBC Bank (Vietnam) Ltd on 16 January 2012 and a director of Ping An Insurance (Group) Company of China, Ltd on 7 December 2012.

Board of Directors

The purpose of HSBC's management structure, headed by the Board of Directors of HSBC Holdings (the 'Board') and led by the Group Chairman, is to promote the long-term success of the Company and deliver sustainable value to our shareholders. The Board sets the strategy and risk appetite for the Group and approves capital and operating plans presented by management for the achievement of the strategic objectives it has set. Implementation of the strategy set by the Board is delegated to the Group Management Board ('GMB') which is led by the Group Chief Executive.

Directors

HSBC Holdings has a unitary Board. The authority of the Directors is exercised in Board meetings where the Board acts collectively. At the time of approval of the *Annual Report and Accounts 2012* on 4 March 2013, the Board comprised the Group Chairman, Group Chief Executive, the Group Finance Director and 13 non-executive Directors whose names and brief biographical particulars are included on pages 302 to 307. The Group Chairman, Group Chief Executive and the Group Finance Director are HSBC employees. Non-executive Directors are not HSBC employees and do not participate in the daily business management of HSBC; they bring an external perspective, constructively challenge and help develop proposals on strategy, scrutinise the performance of management in meeting agreed goals and objectives and monitor the risk profile and the reporting of performance. The non-executive Directors bring experience from a number of industries and business sectors, including the leadership of large complex multinational enterprises.

Terms of appointment

The Board has determined the time commitment expected of non-executive Directors to be 30 to 36 days per annum. Time devoted to the Company could be considerably more, particularly if serving on Board committees.

Letters setting out the terms and conditions of appointment of each of the non-executive Directors, including the time commitment expected of each of them, are available for inspection at 8 Canada Square, London E14 5HQ and will be made available for 15 minutes before the Annual General Meeting and during the Meeting itself.

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Board of Directors > Directors

Powers of the Board

The Board is responsible for managing the business of HSBC Holdings and, in doing so, may exercise its powers, subject to any relevant laws and regulations and to the Articles of Association. In particular, the Board may exercise all the powers of the Company to borrow money and to mortgage or charge all or any part of the undertaking, property or assets (present or future) of HSBC Holdings and may also exercise any of the powers conferred on it by the Companies Act 2006 and/or by shareholders. The Board is able to delegate and confer on any Director holding executive office any of its powers, authorities and discretions (including the power to sub-delegate) for such time and on such terms as it thinks fits. In addition, the Board may establish any local or divisional boards or agencies for managing the business of HSBC Holdings in any specified locality and delegate and confer on any local or divisional board, manager or agent so appointed any of its powers, authorities and discretions (including the power to sub-delegate) for such time and on such terms as it thinks fit. The Board may also, by power of attorney or otherwise, appoint any person or persons to be the agent of HSBC Holdings and may delegate to any such person or persons any of its powers, authorities and discretions (including the power to sub-delegate) for such time and on such terms as it thinks fit.

The Board delegates the management and day-to-day running of HSBC to the GMB but retains to itself approval of certain matters including operating plans, risk appetite and performance targets, procedures for monitoring and controlling operations, the authority or the delegation of authority to approve credit, market risk limits, acquisitions, disposals, investments, capital expenditure or realisation or creation of a new venture, specified senior appointments and any substantial change in balance sheet management policy.

During 2012 the Board adopted terms of reference which are available at www.hsbc.com/1/2/about/board-of-directors. The Board will review its terms of reference annually.

The Directors who served during the year were S A Catz, L M L Cha, M K T Cheung, J D Coombe, J Faber (appointed 1 March 2012), R A Fairhead, D J Flint, A A Flockhart (retired 31 July 2012), S T Gulliver, J W J Hughes-Hallett, W S H Laidlaw, J P Lipsky (appointed 1 March 2012), J R Lomax, I J Mackay, G Morgan (retired 25 May 2012), N R N Murthy (retired 31 December 2012), Sir Simon Robertson, J L Thornton and Sir Brian Williamson (retired 25 May 2012).

HSBC Holdings was registered in Hong Kong under part XI of the Companies Ordinance on 17 January 1991.

Board meetings

Eight Board meetings and a one-day strategy meeting were held in 2012. At least one Board meeting each year is held in a key strategic location outside the UK. During 2012, Board meetings were held in Hong Kong and Washington D.C.

The table below shows each Director's attendance at meetings of the Board held while he or she was a Director during 2012. One meeting of the Board was held at short notice in 2012.

Twelve meetings of committees of the Board appointed to discharge specific business were held during 2012. These meetings are not shown in the table below.

During 2012, the non-executive Directors and the Group Chairman met twice without the other executive Directors. The non-executive Directors also met twice without the Group Chairman, including to appraise the Group Chairman's performance.

Attendance record

	Meetings attended	Meetings eligible to attend as a Director
S A Catz	8	8
L M L Cha	8	8
M K T Cheung	8	8
J D Coombe	8	8
J Faber ^{1,2}	6	6
R A Fairhead ³	6	8
D J Flint	8	8
A A Flockhart ⁴	4	5
S T Gulliver	8	8
J W J Hughes-Hallett	7	8
W S H Laidlaw	8	8
J P Lipsky ¹	6	6
J R Lomax	8	8
I J Mackay	8	8
G Morgan ⁵	4	4
N R N Murthy ⁶	7	8
Sir Simon Robertson	8	8
J L Thornton	8	8
Sir Brian Williamson ⁵	4	4
Meetings held in 2012	8	

1 Appointed a Director on 1 March 2012.

2 Also attended one meeting by invitation before becoming a Director.

3 Took a temporary leave of absence due to illness.

4 Retired as a Director on 31 July 2012.

5 Retired as a Director on 25 May 2012.

6 Retired as a Director on 31 December 2012.

Group Chairman and Group Chief Executive

The roles of Group Chairman and Group Chief Executive are separate and held by experienced full-time Directors. There is a clear division of responsibilities at the head of the Company between the running of the Board and the executive responsibility for running HSBC's business. The key responsibilities of the Group Chairman and the Group Chief Executive are set out below.

Key responsibilities

Group Chairman – D J Flint¹

- Leads the Board and ensures its effectiveness.
- Develops relationships with governments, regulators and investors.
- Leads the Group's interactions on matters of public policy and regulatory reform with regard to the banking and financial services industry.
- Maintains corporate reputation and character.
- Undertakes performance management of the Group Chief Executive.

¹ Appointed Group Chairman in December 2010.

Group Chief Executive – S T Gulliver¹

- Develops, and delivers performance against, business plans.
- Develops Group strategy, in agreement with the Group Chairman, for recommendation to the Board.
- As Chairman of the GMB, drives performance within strategic goals and commercial objectives agreed by the Board.

¹ Appointed Group Chief Executive in January 2011.

The Group Chief Executive has an office in London and in Hong Kong.

Deputy Chairman and senior independent non-executive Director

The key responsibilities of the Deputy Chairman and senior independent non-executive Director are set out below.

Key responsibilities

Deputy Chairman and senior independent non-executive Director – Sir Simon Robertson¹

- Deputises for the Group Chairman at meetings of the Board or shareholders.
- Supports the Group Chairman in his role.
- Acts as an intermediary for other non-executive Directors when necessary.
- Leads the non-executive Directors in the oversight of the Group Chairman.
- Ensures there is a clear division of responsibility between the Group Chairman and Group Chief Executive.
- Is available to shareholders should they have concerns which contact through the normal channels cannot resolve or for which such contact would be inappropriate.

¹ Appointed senior independent non-executive Director in 2007 and Deputy Chairman in December 2010.

Board balance and independence of Directors

The Board includes a strong presence of both executive and non-executive Directors and no individual or small group can dominate its decision making. The size of the Board is appropriate given the complexity and geographical spread of our business and the significant time demands placed on the non-executive Directors, particularly those who serve as members of Board committees.

The Nomination Committee regularly reviews the structure, size and composition of the Board (including the skills, knowledge and experience required of Directors) necessary to address and challenge adequately key risks and issues that confront, or may confront, the Board and makes recommendations to the Board with regard to any changes.

During 2012, the Board adopted a Board diversity policy. Further information on this policy can be found on page 329.

The Board considers all of the non-executive Directors to be independent in character and judgement. The Board has determined S A Catz, L M L Cha, M K T Cheung, J B Comey, J D Coombe, J Faber, R A Fairhead, R Fassbind, J W J Hughes-Hallett, W S H Laidlaw, J P Lipsky, J R Lomax, Sir Simon Robertson and J L Thornton to be independent. When determining independence the Board considers that calculation of the length of service of a non-executive Director begins on the date of his or her first election by shareholders as a Director of HSBC Holdings. Given the complexity and geographical spread of our business, the experience of previous service on a HSBC subsidiary company board can be a considerable benefit and does not detract from a Director's independence. In reaching its determination of each non-executive Director's independence, the Board has concluded that there are no relationships or circumstances which are likely to affect a Director's judgement and any relationships or circumstances which could appear to do so were considered not to be material. From the conclusion of the Annual General Meeting in 2013, R A Fairhead will have served on the Board for more than nine years and, in that respect only, will not meet the usual criteria for independence set out in the UK Corporate Governance Code.

In accordance with the Rules Governing the Listing of Securities on the Stock Exchange of

Report of the Directors: Corporate Governance (continued)

Board of Directors > Directors

Hong Kong Limited, each non-executive Director determined by the Board to be independent has provided an annual confirmation of his or her independence to HSBC Holdings.

Information and support

The Board regularly reviews reports on progress against financial objectives, business developments and investor and external relations. The chairmen of Board committees and the Group Chief Executive report to each meeting of the Board on the activities of the committees since the previous Board meeting. The Board receives regular reports and presentations on strategy and developments in the global businesses and principal geographical areas. Regular reports are also provided to the Board and Board committees on the Group's risk appetite profile, top and emerging risks, risk management, credit exposures and the Group's loan portfolio, asset and liability management, liquidity, litigation, compliance and reputational issues. The agenda and supporting papers are distributed in advance of all Board and Board committee meetings to allow time for appropriate review and to facilitate full discussion at the meetings. All Directors have full and timely access to all relevant information and may take independent professional advice if necessary at the Company's expense.

The Directors have free and open contact with management at all levels. When attending Board offsites and when travelling for other reasons, non-executive Directors are encouraged to take opportunities to see business operations at first hand and to meet management.

Non-executive Directors have an open invitation to attend meetings of the GMB to further enhance their understanding and awareness of our businesses and the senior leadership team.

Induction

Full, formal and tailored induction programmes, with particular emphasis on risk management and internal controls systems, are arranged for newly appointed Directors. The programmes consist of a series of meetings with other Directors and senior executives to enable new Directors to familiarise themselves with our strategy, risk appetite and risk management, operations and internal controls. Directors also receive comprehensive guidance on directors' duties and liabilities. As part of the induction process the Group Company Secretary will coordinate a development programme based on an individual Director's needs. Induction programmes

are also arranged for newly appointed members of committees.

Training and Development

Focused in-house training sessions are arranged in conjunction with scheduled Board meetings. Unless otherwise indicated, all Directors¹ attended Board Meetings in 2012 at which briefings on the following topics were given:

- Capital market perspectives on HSBC^{2,3}
- CMB strategy² and business update
- GB&M strategy² and business update
- RBWM strategy² and business update
- GPB strategy² and business update³
- Macroeconomic outlook²
- Europe strategy²
- US strategy²
- China strategy²
- Outlook for Greater China²
- Marks and Spencer Bank
- Latin America
- Global geopolitics
- IT infrastructure

Except:

- 1 *R Fassbind and J B Comey who were not Directors at the time of the briefings.*
- 2 *J Faber and J P Lipsky who were not Directors at the time of the briefing.*
- 3 *R A Fairhead who was unable to attend the briefing.*

Executive Directors

In the performance of their roles as Group Chairman, Group Chief Executive and Group Finance Director, respectively, D J Flint, S T Gulliver and I J Mackay develop and refresh their skills and knowledge of the Group's businesses and operations through day-to-day interactions and briefings with senior management of the Group's businesses and functions; and presenting on the Group's businesses to investors and analysts. They remain abreast of developments affecting the financial services sector, and banking in particular, by representing HSBC's interests at conferences, advisory groups and other events and meetings with regulators and other authorities. During 2012, this included the activities set out below:

D J Flint

Chairman of the International Institute of Finance, including leading member's meetings and giving keynote speeches. Participated in panel discussions and gave key note speeches on economic growth and financial regulation at a number of leading events including the International Monetary Conference, the Hong Kong Trade Development Council's *Think Asia Event*, City Week 2012, a Chatham House

conference, St. Gallen Symposium and The Salzburg Global Seminar. Gave the *Aileen Beattie Memorial Lecture* at the Institute of Chartered Accountants of Scotland on the opportunities to improve the financial services sector following the crisis. Presented to the Cambridge Executive Leadership Programme on leadership. Attended and participated in panel discussions at the World Economic Forum in Davos. Attended prudential regulation meetings with the FSA.

S T Gulliver

Gave keynote speeches at the Fung Global Institute annual forum and a Conservative Parliamentary China Group meeting on UK trade links with China. Gave presentations at several Asian-focussed events including the China Development Forum in Beijing, the China Investment Corporation global investment forum, the Association of Southeast Asian Nations Finance Ministers Investors Summit in Hong Kong and the International Advisory Council of the China Banking Regulatory Commission. Attended the World Economic Forum in Davos. Attended prudential regulation meetings with the FSA. Chaired the Group's strategy day for investors in London. Gave the keynote speech at an HSBC-led international corporate and structured banking event for UK exporters.

I J Mackay

Participated in meetings of the European Chief Financial Officers Network, the FSA Chief Financial Officers Group and the Bank for International Settlements. Attended conferences focused on Asian investment and European finance. Attended prudential regulation meetings with the FSA and the Hong Kong Monetary Authority. Presented at the Group's strategy day for investors in London and hosted regular meetings with investors in the UK, US and Hong Kong.

Non-executive Directors

A personalised approach to training and development of non-executive Directors is applied. Non-executive Directors are given opportunities to update and develop their skills and knowledge through briefings by senior executives and externally run seminars. Non-executive Directors have access to internal training and development resources. Development plans and records of training and development activities are maintained by the Group Company Secretary to facilitate the Group Chairman's annual review of each non-executive Director.

In addition to the briefings given at Board Meetings of HSBC Holdings, the following non-executive Directors undertook bespoke training sessions and other activities, including attending Board committee meetings at which briefings were given during 2012 to develop and refresh their knowledge and skills as set out below:

S A Catz

Attended bespoke briefings on managing operational and reputational risk and recovery and resolution planning.

L M L Cha

Gave keynote speeches at the Institute of Directors in Hong Kong on the need for a financial services development council and at the Hong Kong Economic Summit. Participated in the Global Agenda Council on Global Financial system at the World Economic Forum. Attended bespoke briefings from HSBC Holdings on: senior management succession planning and diversity; extraterritorial application of laws and their impact on HSBC's global businesses; HSBC brand management and sponsorship portfolio; the Group's compliance assurance model; regulation and its impact on risk; and the FSA's 'Three lines of defence' operational risk model. As a director and Vice Chairman of The Hongkong and Shanghai Banking Corporation attended bespoke briefings or board meetings at which briefings were given on: the Group's business in Asia-Pacific; international operations; information technology; CMB; financial regulation; GB&M; the Hong Kong SAR's relationships with India and China; and RBWM in India. Participated in the annual forum for HSBC Group non-executive directors.

M K T Cheung

Attended events for independent non-executive directors organised by KPMG and Deloitte and a seminar on international financial reporting standards organised by the Hong Kong Institute of Certified Public Accountants. Attended meetings of the Group Audit Committee at which briefings were given on developments in regulatory and accounting requirements and the regulatory environment. As a director of Hang Seng Bank attended bespoke briefings or board meetings at which briefings were given on: Basel III requirements; RBWM strategy; the Hong Kong Competition Ordinance; supervisory requirements of the Hong Kong Monetary Authority; changes to the Hong Kong Stock Exchange Listing

Report of the Directors: Corporate Governance (continued)

Board of Directors > Directors

Rules; obligations under the Hong Kong Securities and Futures Ordinance; and mechanisms for core risk appetite measures. Participated in the annual forum for HSBC Group non-executive directors.

J D Coombe

Attended events for non-executive directors run by Tapestry Networks and Ernst & Young on bank governance and by PricewaterhouseCoopers on updates in financial accounting. Attended bespoke briefings on prudential regulation, reform of the UK financial services industry regulatory authorities and managing operational risk in the Finance global function. Attended meetings of Board committees at which briefings were given on the regulatory environment and developments in accounting requirements, risk and executive remuneration, the risk control frameworks for the global businesses, Group recovery and resolution planning and legal reform. Chaired the annual forum for the chairmen of HSBC Group audit and risk committees. Participated in the annual forum for HSBC Group non-executive directors.

J Faber

Undertook a personal induction programme comprising bespoke briefings on: CMB and GB&M, with particular focus on operations in the UK and Europe; the structure and responsibilities of a number of the Group's global functions, including: Strategy and Planning; Corporate Sustainability; Risk (including Compliance); Finance; and Legal; and corporate governance (including Directors' duties and obligations, HSBC's governance structure, Global Standards and Business Principles, international corporate governance codes and listing obligations). Attended bespoke briefings on prudential regulation and HSBC's business in Germany. Attended meetings of the Group Risk Committee at which briefings were given on the risk control frameworks for the global businesses, Group recovery and resolution planning and legal and regulatory reform.

R A Fairhead

Attended bespoke briefings on prudential regulation. Attended meetings of committees of the Board at which briefings were given on the regulatory environment and developments in accounting requirements and risk, the risk control frameworks for the global businesses, Group recovery and resolution planning and legal and regulatory reform. Participated in a risk workshop co-hosted by HSBC and Cambridge University Centre for Risk Studies.

R Fassbind¹

Undertook a personal induction programme comprising bespoke briefings on: each of the Group's global businesses; the structure and responsibilities of a number of the Group's global functions, including: Strategy and Planning; Corporate Sustainability; Risk; Finance; Human Resources; and Internal Audit; corporate governance (including Directors' duties and obligations, HSBC's governance structure, Global Standards and Business Principles, international corporate governance codes and listing obligations); IT and Operations; and the Group's Insurance business.

J W J Hughes-Hallet

Attended meetings of the Group Risk Committee at which bespoke briefings were given on the risk control frameworks for the global businesses, Group recovery and resolution planning and legal and regulatory reform.

W S H Laidlaw

Attended bespoke briefings on individual liquidity adequacy assessment in the UK. Attended meetings of the Group Remuneration Committee at which briefings were given on regulatory developments in executive remuneration.

J P Lipsky

Undertook a personal induction programme comprising bespoke briefings on: GB&M; the structure and responsibilities of a number of the Group's global functions, including: Strategy and Planning; Risk (including compliance); Finance ; Legal ; and governance (including Directors' duties and obligations, HSBC's governance structure, Global Standards and Business Principles, international corporate governance codes and listing obligations). Attended bespoke briefings on prudential regulation. Attended meetings of the Group Risk Committee at which briefings were given on the risk control frameworks for the global businesses, Group recovery and resolution planning and legal and regulatory reform. Participated in the annual forum for HSBC Group non-executive directors.

J R Lomax

Attended an event for non-executive directors run by Tapestry Networks and Ernst & Young on bank governance and the Trilateral Commission's Europe conference in Helsinki. Attended meetings of

committees of the Board at which briefings were given on the regulatory environment and developments in regulatory and accounting requirements and risk, the risk control frameworks for the global businesses, Group recovery and resolution planning and legal and regulatory reform. Participated in a risk workshop co-hosted by HSBC and Cambridge University Centre for Risk Studies and in the annual forum for HSBC Group non-executive directors.

Sir Simon Robertson

Attended bespoke briefings on prudential regulation, GPB, GB&M, Legal (including US regulatory matters), and Strategy and Planning. Attended a briefing from the external auditor on its role in the Group's financial reporting. Develops and refreshes knowledge of the Group's businesses and operations through regular interactions with, and receipt of briefings from, the Group Chairman and Group Chief Executive. Participated in the annual forum for HSBC Group non-executive directors.

J L Thornton

Attended bespoke briefings on prudential regulation and anti-money laundering and compliance. Attended meetings of the Group Remuneration Committee at which briefings were given on regulatory developments in executive remuneration. As chairman of HSBC North America Holdings Inc. attended board meetings at which briefings were given on: the Dodd-Frank Act; key US strategic considerations comprising the transformation of the US business (including regulatory and remediation planning, business disposals and demise, core business re-engineering and changing the culture); and the Group's global businesses in the US including, in particular, the US consumer and mortgage lending business.

Performance evaluation

In September 2012, Bvalco Ltd was commissioned to facilitate and report on the review of effectiveness of the Board, with particular focus on the effectiveness of committees and their interaction with the Board, the relationship and information flows between the subsidiaries and the Board, the balance of skills on the Board and the level of time commitment required from Directors. A legal firm which is engaged from time to time by the Company to provide legal services holds a 20% shareholding in Bvalco Ltd. Bvalco Ltd has confirmed that it does not have any other connection with the Company. Bvalco's report was prepared following interviews with Directors and senior members of management

and a review of relevant documents. Factors assessed during Bvalco's review included the Group's culture, handling of reputational issues, composition of the Board, effectiveness of the Group Chairman, interaction between Board members and management, and Board Committee structure. Bvalco's evaluation of the Board considered the balance of skills, experience, independence and knowledge of the Company on the Board, its diversity, including gender, how the Board works together as a unit and other factors relevant to its effectiveness.

The Bvalco report concluded that the Board operates effectively with a number of important strengths. The report is used by the Board in its annual evaluation of its own performance and that of its committees and by the Group Chairman in his review of the individual performance of Directors. The Board will monitor implementation of actions arising from its 2012 performance evaluation. All actions arising from the Board's 2011 performance evaluation have been implemented.

It is the intention of the Board to continue to undertake an evaluation of its performance and that of its committees and individual Directors annually, with external input to the process at least every third year.

Formal evaluation of the individual performance of each Director is undertaken annually by the Group Chairman using the findings of the performance evaluation process undertaken by the Board and, as appropriate, the records of training and development activities undertaken by Directors. During this evaluation, the Group Chairman discusses the contribution of the Director and the time spent by them in performing their responsibilities. The Group Chairman has confirmed that all of the non-executive Directors continue to perform effectively and to demonstrate commitment to their roles.

The non-executive Directors, led by the Deputy Chairman and senior independent non-executive Director, are responsible for the evaluation of the performance of the Group Chairman.

Appointment, retirement and re-election of Directors

The Board may at any time appoint any person who is willing to act as a Director, either to fill a vacancy or as an addition to the existing Board, but the total number of Directors shall not exceed twenty-five. Any Director so appointed by the Board shall retire at the Annual General Meeting following his or her appointment and shall be eligible for re-election but would not be taken into account in determining the

Report of the Directors: Corporate Governance (continued)

Board of Directors > Directors / Corporate governance codes

number of Directors who are to retire by rotation at such meeting in accordance with the Articles of Association. The Board may appoint any Director to hold any employment or executive office and may revoke or terminate any such appointment. Shareholders may, by ordinary resolution, appoint a person a Director or remove any Director before the expiration of his period of office. On the recommendation of the Nomination Committee and in compliance with provision B.7.1 of the UK Corporate Governance Code, the Board has decided that all of the Directors should be subject to annual re-election by shareholders. Accordingly, all of the Directors will retire at the forthcoming Annual General Meeting and offer themselves for re-election. Each of the executive Directors is employed, on a rolling contract which requires 12 months' notice to be given by either party. None of the non-executive Directors has a service contract with HSBC.

Relations with shareholders

All Directors are encouraged to develop an understanding of the views of major shareholders. Non-executive Directors are invited to attend analyst presentations and other meetings with institutional investors and their representative bodies. Directors also meet representatives of institutional shareholders annually to discuss corporate governance matters.

All executive Directors and certain other senior executives hold regular meetings with institutional investors. The Board receives a regular investor relations activity report which provides feedback from meetings with institutional shareholders and brokers, analysts' forecasts, information from research reports and share price performance data. Twice each year the Board also receives a report from one of our corporate brokers on market views and investor relations.

On several occasions during 2012, non-executive Directors, including the senior independent non-executive Director, met or corresponded with institutional investors and their representatives to discuss governance and remuneration.

As senior independent non-executive Director, Sir Simon Robertson is available to shareholders should they have concerns which contact through the normal channels of Group Chairman, Group Chief Executive, Group Finance Director or other executives cannot resolve or for which such contact would be inappropriate. He may be contacted

through the Group Company Secretary at 8 Canada Square, London E14 5HQ.

During 2012, the Board established a shareholder communication policy which is available on www.hsbc.com.

Conflicts of interest, indemnification of Directors, relevant audit information and contracts of significance

The Board has authority to approve Directors' conflicts and potential conflicts of interest and has adopted a policy and procedures for the determination of terms of authorisation for such situations. The Board's powers to authorise conflicts are operating effectively and the procedures are being followed. A review of situational conflicts which have been authorised from time to time and the terms of those authorisations is undertaken by the Board annually.

Our Articles of Association provide that Directors are entitled to be indemnified out of the assets of HSBC Holdings against claims from third parties in respect of certain liabilities. Such indemnity provisions have been in place during the financial year but have not been utilised by the Directors.

Each person who is a Director at the time of approval of this report confirms that so far as he or she is aware, there is no relevant audit information of which the auditor is unaware and the Director has taken all the steps that he or she ought to have taken as a Director in order to make himself or herself aware of any relevant audit information and to establish that the auditor is aware of that information. This confirmation is given pursuant to section 418 of the Companies Act 2006 and should be interpreted in accordance therewith and subject to the provisions thereof.

None of the Directors had, during the year or at the end of the year, a material interest, directly or indirectly, in any contract of significance with any HSBC company.

Corporate governance codes

HSBC is committed to high standards of corporate governance. HSBC has complied during 2012 with the applicable code provisions of: (i) The UK Corporate Governance Code issued by the Financial Reporting Council; (ii) the Code on Corporate Governance Practices set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, from 1 January 2012 until its amendment and replacement

by the Hong Kong Corporate Governance Code on 1 April 2012; and (iii) the Hong Kong Corporate Governance Code from 1 April 2012 to 31 December 2012, save that the Group Risk Committee (all the members of which are independent non-executive Directors), which was established in accordance with the recommendations of the Report on Governance in UK banks and other financial industry entities, is responsible for the oversight of internal control (other than internal control over financial reporting) and risk management systems (Hong Kong Corporate Governance Code provision C.3.3 paragraphs (f), (g) and (h)). If there were no Group Risk Committee, these matters would be the responsibility of the Group Audit Committee. At its meeting on 24 May 2012, the Board adopted Terms of Reference and approved a shareholder communication policy as required under the Hong Kong Corporate Governance Code. The UK Corporate Governance Code is available at www.frc.org.uk and the Hong Kong Corporate Governance Code is available at www.hkex.com.hk.

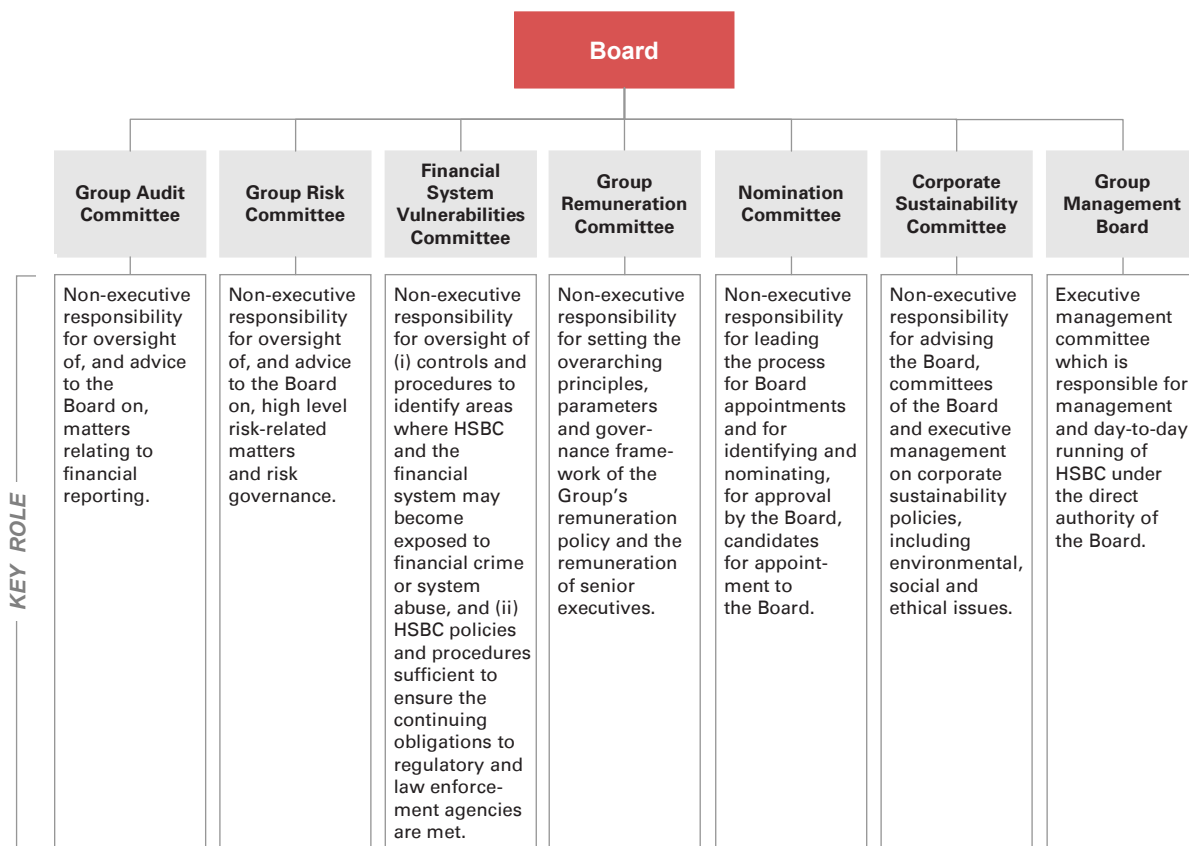
The Board has adopted a code of conduct for transactions in HSBC Group securities by Directors. The code of conduct complies with The Model Code in the Listing Rules of the FSA and with The Model

Code for Securities Transactions by Directors of Listed Issuers ('Hong Kong Model Code') set out in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, save that The Stock Exchange of Hong Kong Limited has granted certain waivers from strict compliance with the Hong Kong Model Code. The waivers granted by The Stock Exchange of Hong Kong Limited primarily take into account accepted practices in the UK, particularly in respect of employee share plans. Following specific enquiry, each Director has confirmed that he or she has complied with the code of conduct for transactions in HSBC Group securities throughout the year, save that, on 15 June 2012, an independent non-executive Director acquired an interest as beneficial owner in 3,950 retail bonds and as non-beneficial owner in 1,170 retail bonds of RMB10,000 each issued by HSBC Bank plc before giving notification and receiving written clearance to deal. On 10 January 2013, an independent non-executive Director disposed of an interest as beneficial owner in 500 units of euro-denominated preferred securities of EUR1,000 each issued by HSBC Capital Funding (Euro 2) L.P. before giving notification. All Directors have since been reminded of their obligations under the code of conduct for transactions in HSBC Group Securities.

Report of the Directors: Corporate Governance (continued)

Board committees > Group Management Board / Group Audit Committee

Board committees



The Board has established a number of committees consisting of Directors, Group Managing Directors and, in the case of the Financial System Vulnerabilities Committee and Corporate Sustainability Committee, co-opted non-director members. The key roles of the principal committees are described above. The Chairman of each non-executive Board committee reports to each meeting of the Board on the activities of the committee since the previous Board meeting.

The terms of reference of the non-executive Board committees are available at www.hsbc.com/boardcommittees. Each non-executive Board committee reviews its terms of reference annually.

Appointments of Directors to each non-executive Board committee are made for periods of up to three years, extendable by no more than two additional three-year periods.

Group Management Board

Members^{1,2} S T Gulliver (Chairman) and I J Mackay, who are executive Directors, and A Almeida, S Assaf, I M Dorner, J M Flint, A M Keir, S A Levey, A M Losada, M M Moses, S P O'Sullivan, B Robertson and P T S Wong, all of whom are Group Managing Directors.

¹ As at 4 March 2013.

² M P Kaur has been appointed a member with effect from 1 April 2013.

The head of each global business and global function and the chief executive of each region attend GMB meetings, either as members or by invitation.

The GMB meets frequently and exercises the powers, authorities and discretions of the Board in so far as they concern the management and day-to-day running of HSBC Holdings. Matters reserved for approval by the Board are described on page 310.

The GMB is a key element of our management reporting and control structure such that all of our line operations are accountable either to a member of the GMB or directly to the Group Chief Executive, who in turn reports to the Group Chairman. The Board has set objectives and measures for the GMB. These align senior executives' objectives and measures with the strategy and operating plans throughout HSBC.

The Group Chief Executive (who is Chairman of the GMB) reports to each meeting of the Board on the activities of the GMB.

Regular Risk Management Meetings of GMB, chaired by the Group Chief Risk Officer, are held to establish, maintain and periodically review the policy and guidelines for the management of risk within the Group.

Regular Global Standards Steering Meetings of the GMB, co-chaired by the Group Chief Risk Officer and Group Chief Legal Officer, are held to develop and implement global standards reflecting best practices which must be adopted and adhered to consistently throughout the Group.

Group Audit Committee

The Group Audit Committee ('GAC') has non-executive responsibility for oversight of, and advice to, the Board on matters relating to financial

reporting and for non-executive oversight of internal controls over financial reporting.

	Meetings attended	Meetings eligible to attend
Members¹		
J D Coombe (Chairman)	5	5
M K T Cheung	5	5
R A Fairhead	5	5
J R Lomax	5	5
Meetings held in 2012	5	

1 All members are independent non-executive Directors.

R Fassbind was appointed a member of the GAC on 1 March 2013.

The Board has determined that M K T Cheung, J D Coombe, R A Fairhead, R Fassbind and J R Lomax are independent according to SEC criteria and may be regarded as audit committee financial experts for the purposes of section 407 of the Sarbanes-Oxley Act and have recent and relevant financial experience for the purposes of the UK Corporate Governance Code.

The governance structure for the oversight of financial reporting is set out below. Each major operating subsidiary has established a board committee with non-executive responsibility for oversight of matters relating to financial reporting.

Governance

Authority	Membership	Responsibilities include:
Board	Executive and non-executive Directors	<ul style="list-style-type: none"> Financial reporting Appoints senior financial officers Delegates authorities in relation to financial matters
GAC	Independent non-executive Directors	<ul style="list-style-type: none"> Monitors the integrity of financial statements Oversees the internal control systems over financial reporting, including reviewing their effectiveness Monitors and reviews the effectiveness of the internal audit function Reviews the Company's financial and accounting policies and practices Advises the Board on appointment of the external auditor and is responsible for oversight and remuneration of the external auditor
Disclosure Committee	Representatives from global businesses, functions and certain Group companies	<ul style="list-style-type: none"> Reviews the Group's material communications with investors Assists the Group Chief Executive and Group Finance Director to discharge their obligations relating to financial reporting under the Securities Exchange Act of 1934 Monitors and reviews the effectiveness of controls and procedures established to ensure that information is disclosed appropriately and on a timely basis Reports findings and makes recommendations to the Group Chief Executive, Group Finance Director and the GAC
Subsidiary board committees responsible for oversight of financial reporting and global business audit committees	Independent non-executive directors and/or independent members, as appropriate	<ul style="list-style-type: none"> Provide certification to the GAC or intermediate audit committee on financial statements and internal controls over financial reporting of relevant subsidiaries or businesses, as appropriate

Report of the Directors: Corporate Governance (continued)

Board committees > Group Audit Committee

Committee activities

The GAC undertook the following activities in the discharge of its responsibilities:

- **Financial reporting.** The Committee advised the Board on meeting its external financial reporting obligations through its reviews of financial statements, interim reports and interim management statements prior to approval by the Board. The Committee also undertook the following:
 - endorsed the going concern statement and the statement of compliance with the UK Corporate Governance Code and Hong Kong Corporate Governance Code (formerly the Code on Corporate Governance Practices in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited) for inclusion in the financial statements;
 - advised the Board that the annual report and accounts, taken as a whole, is fair, balanced and understandable;
 - received reports on proposed changes to the Group's disclosures in the financial statements and the adequacy of procedures to identify transactions and matters requiring disclosure under certain accounting standards;
 - reviewed accounting policies and practices, including approval of the critical accounting policies;
 - considered provisioning for, and disclosure of, certain litigation and regulatory matters with external legal counsel providing a status update on these matters;
 - received a presentation from the Global Head of Tax on current tax issues;
 - received a report on the European Banking Authority Capital Exercise 2012 to monitor adherence to recommended core tier 1 ratios; and
 - reviewed the procedures for the submission by employees of concerns regarding accounting and/or auditing matters.

During 2012, the GAC considered the significant accounting issues described below. In addressing these issues the Committee considered the appropriateness of management's judgements and estimates and, where appropriate, discussed these judgements and

estimates with the external auditor. The Committee considered:

- the circumstances leading to the recognition of a provision at 30 June 2012 relating to US regulatory and law enforcement investigations into inadequate compliance with anti-money laundering, US Bank Secrecy and sanctions laws. The Committee noted that management had considered the available information, recent developments, the opinions of external legal counsel and the outcome of past cases on similar matters. The Committee discussed the judgements exercised by management in forming a best estimate of the amount that might have been required to settle the matter, and agreed that a provision of US\$700m should be made, while noting that this estimate was highly uncertain, and that the amount, when determined, could be higher, possibly significantly so. In the third quarter, the Committee considered the latest developments in this matter and discussed the possibility of a criminal prosecution being brought against one or more Group companies and the possible implications. The Committee agreed with management's judgement that the provision should be increased to US\$1.5bn, while continuing to note that the final amount could be significantly higher. Subsequently, the Committee noted the payments made in December 2012 under the agreements to achieve resolution with US and UK government agencies, and the terms of the Deferred Prosecution Agreement;
- the developments in the industry investigations and reviews into the setting of Libor, Euribor and other benchmark interest and foreign exchange rates by various regulators and competition and enforcement authorities around the world. The Committee discussed the high degree of uncertainty as to the resolution of these regulatory investigations and reviews, including the timing and potential impact;
- HSBC's exposure to the payment of redress in respect of the possible mis-selling of payment protection insurance policies in the UK and the related provisions. The Committee considered the key assumptions which determine the provisions and the factors driving the increase during the year. Management's assessment was that the amount of provision at 31 December 2012

- of US\$1.3bn is based on appropriate assumptions about future expected redress payments, while noting the sensitivity of the provision to different outcomes from those assumed;
- HSBC’s involvement in the sale of interest rate swaps to small and medium sized businesses in the UK and the potential costs of remediation. The Committee noted that the provision of US\$598m at 31 December 2012 reflected the outcome of the FSA’s findings from the pilot reviews completed by banks on the selling of these products to customers;
 - the level of loan impairment allowances and charges throughout the year, discussing with management the reasons for significant increases, notably in Brazil as a result of economic conditions and strong growth in lending in recent periods. The Committee considered the judgements and estimates involved in applying roll rate methodologies and noted the recognition of an additional impairment allowance of US\$225m in respect of the US mortgage lending portfolios to reflect a longer estimated average period of time from current status to write-off. In response to an industry letter from the FSA concerning the application of loan impairment methodologies to loan portfolios vulnerable to credit stresses, the Committee considered reports on the application of HSBC’s accounting policies and loan impairment methodologies. The Committee also considered a report on credit exposures and the extent of refinancing risk in HSBC’s UK corporate real estate lending portfolio, and how this is reflected in loan impairment allowances;
 - the recoverability of major deferred tax assets balances recognised, including the deferred tax asset balances recognised in the US, Mexico and Brazil;
 - management’s judgements involved in the change in estimation methodology for credit valuation adjustments and debit valuation adjustments on derivative financial instruments as at 31 December 2012 as a result of changing market practices;
 - the impairment test performed on HSBC’s investment in Bank of Communications Co., Limited as at 31 December 2012. During the year, the market value of the investment was below the carrying amount for a period of approximately ten months, which gave rise to an indicator of impairment. The impairment test identified that, based on an assessment of the value in use of the investment, the investment is not impaired; and
 - management’s conclusion that goodwill relating to GB&M Europe is not impaired following reduced profitability in the second half of 2012 which triggered the re-testing of the related goodwill as at 31 December 2012. The Committee noted that disclosure has been made with regards to the extent to which a change in key assumptions would result in the recoverable amount to be equal to its carrying amount (see note 23 on the financial statements).
- **Internal controls over financial reporting.**
The Committee undertook an annual review of HSBC’s systems of internal controls over financial reporting. During 2012, the Committee monitored the effectiveness of such internal controls and reported regularly to the Board as described on page 334. The Committee received regular reports from the Group Finance Director, the Group Chief Accounting Officer, and the Group Head of Internal Audit. Minutes of the Group Risk Committee (‘GRC’) and executive committee meetings including the GMB and Risk Management Meetings were provided to the Committee members. The Committee also reviewed the adequacy of resources, qualifications and experience of staff in the Finance function. Reports were submitted to the Committee on internal control matters in relation to the Sarbanes-Oxley Act. The Group Finance Director, the Group Chief Risk Officer, the Group Head of Internal Audit, the Group Chief Accounting Officer, Group Company Secretary, external auditor and other senior executives attended Committee meetings. The Committee had regular discussions with the external auditor and the Group Head of Internal Audit, with an opportunity at each meeting for discussions to take place without management present.
 - **Effectiveness of the internal audit function.**
The Committee satisfied itself that the internal audit function was effective and adequately resourced through regular meetings held with, and reports provided by, the Group Head of Internal Audit on internal audit issues, including the effectiveness and adequacy of resources. KPMG undertook a quality assurance review of

Report of the Directors: Corporate Governance (continued)

Board committees > Group Audit Committee / Group Risk Committee

the internal audit function and concluded that overall, the internal audit function generally conformed to the Institute of Internal Auditors' International Standards and Code of Ethics for the Professional Practice on Internal Auditing. The Committee received reports over the course of 2012 on the activities of the internal audit function and reviewed its planned activities for the following year.

- **Legal and regulatory environment.** The Committee received regular reports on litigation and on the application of changes in law, regulation, accounting policies and practices and regulatory developments, including reports on developments in the programme to change International Financial Reporting Standards, Basel III, the recommendations of the Independent Commission on Banking, Dodd-Frank Act and changes in the UK Corporate Governance Code and Guidance on Audit Committees.
- **External auditor.** The Committee provided oversight of the external auditor through regular meetings with the external auditor, including meetings without management present, and receiving reports on the external auditor's strategy in relation to the audit of financial statements and the progress of the audit. The Committee monitored the effectiveness of the audit process through a review of the public report published by the Financial Reporting Council's Audit Inspection Unit on the inspection of the external auditor, an assessment against a best practice checklist for evaluating external auditors, an external audit assessment questionnaire completed by the chief financial officers of the Group's major geographical regions, a review of the relationship between the Group and the external auditor at a senior level and considered the results of feedback provided to the external auditor by members of the finance function throughout the Group. The Committee approved the remuneration and terms of engagement and recommended to the Board the re-appointment of the external auditor.
- **Terms of reference and effectiveness of the Committee.** The Committee undertook an annual review of its terms of reference and of its own effectiveness. Changes were made to the Committee's terms of reference to reflect changes to the requirements of the UK Corporate Governance Code applicable to financial years beginning on or after 1 October

2012 and the Hong Kong Corporate Governance Code.

In addition to the scheduled Committee meetings, the Chairman met regularly with the Group Finance Director, the Group Chief Accounting Officer, the Group Chief Risk Officer, the Group Head of Internal Audit, other senior executives and the external auditor.

Terms of reference and subsidiary company audit oversight

The GAC is responsible for non-executive oversight of internal controls over financial reporting.

To ensure consistency of scope and approach by subsidiary company audit committees, the GAC has established core terms of reference to guide subsidiary companies when adopting terms of reference for their audit committees. The Committee's endorsement is required for any proposed material changes to subsidiary audit committee terms of reference and for appointments to such committees.

A forum for the chairmen of our principal subsidiary company committees with responsibility for non-executive oversight of financial reporting and risk-related matters was held in June 2012 to share understanding and to facilitate a consistent approach to the way in which these subsidiary company committees operate. The next forum will be held in June 2013.

Arrangements relating to the external auditor

The Committee has recommended to the Board that KPMG Audit Plc be reappointed as auditor at the forthcoming Annual General Meeting.

KPMG has been the Group's auditor since 1991, when HSBC Holdings became the ultimate holding company of the Group, without a tender process for the external audit contract having taken place. It is our intention that a tender process for the external audit contract will be undertaken, with the successful audit firm being appointed by 2015.

The Board has approved, on the recommendation of the Committee, a policy for the employment by HSBC of former employees of KPMG. The Committee receives an annual report on such former employees who are employed and the number in senior positions. This report enables the Committee to consider whether there has been any impairment, or appearance of impairment, of the external auditor's judgement, objectivity or independence in respect of the audit. The external

auditor provided written confirmation of its independence under industry standards.

The policies for the pre-approval of specific services that may be provided by the principal auditor are kept under review by the Committee and amended as necessary to meet the dual objectives of ensuring that we benefit in a cost effective manner from the cumulative knowledge and experience of our auditor, while also ensuring that our external auditor maintains the necessary degree of independence and objectivity. These pre-approval policies apply to all services where any HSBC company pays for the service, or is a beneficiary or addressee of the service, and has selected or influenced the choice of KPMG. All services provided by KPMG during 2012 were pre-approved by the Committee or were entered into under pre-approval policies established by the Committee.

The pre-approved services relate to regulatory reviews, agreed-upon procedures reports, other types of attestation reports, the provision of advice and other non-audit services allowed under SEC independence rules. The services fall into the categories of audit services, audit-related services, tax services and other services.

An analysis of the remuneration paid in respect of audit and non-audit services provided by KPMG for each of the past three years is disclosed in Note 8 on the Financial Statements.

Group Risk Committee

The GRC is responsible for advising the Board on high-level risk-related matters and risk governance and for non-executive oversight of risk management and internal controls (other than over financial reporting).

	Meetings attended	Meetings eligible to attend
Members¹		
R A Fairhead ² (Chairman)	6	7
J D Coombe	7	7
J Faber ³	5	5
J W J Hughes-Hallett ⁴	4	5
J P Lipsky ³	5	5
J R Lomax	7	7
Meetings held in 2012	7	

- 1 All members are independent non-executive Directors.
- 2 Took a temporary leave of absence due to illness.
- 3 Appointed a member of the Committee on 1 March 2012.
- 4 Retired as a member of the Committee on 31 July 2012.

John Trueman, a non-executive director of HSBC Bank plc and Chairman of its risk and audit committees has continued to attend meetings of the GRC by invitation during 2012. Robert Herdman, a non-executive director of HSBC North America Holdings Inc. and HSBC Bank USA, has been invited by the GRC to attend its meetings from the beginning of 2013. Their experience of risk-related matters in the financial services industry is valued by the Committee.

Governance

All of HSBC's activities involve, to varying degrees, the measurement, evaluation, acceptance and management of risk or combinations of risks. The Board, advised by the Committee, requires and encourages a strong risk governance culture which shapes the Group's attitude to risk. The Board and the Committee oversee the maintenance and development of a strong risk management framework by continually monitoring the risk environment, top and emerging risks facing the Group and mitigating actions planned and taken.

The Committee monitors the effectiveness of the Group's risk management and internal controls systems other than over financial reporting, which are monitored by the GAC.

The governance structure for the management of risk is set out in the following table. Each major operating subsidiary has established a board committee with non-executive responsibility for oversight of risk-related matters and an executive committee with responsibility for risk-related matters.

Report of the Directors: Corporate Governance (continued)

Board committees > Group Risk Committee

Governance structure for the management of risk		
Authority Board	Membership Executive and non-executive Directors	Responsibilities include: <ul style="list-style-type: none"> • Approves risk appetite, strategy and performance targets for the Group • Approves appointment of senior risk officers • Delegates authority for risk management • Encourages a strong risk governance culture which shapes the Group's attitude to risk
GRC	Independent non-executive Directors	<ul style="list-style-type: none"> • Advises the Board on: <ul style="list-style-type: none"> – risk appetite and alignment with strategy – alignment of remuneration with risk appetite (through advice to the Group Remuneration Committee) – risks associated with proposed strategic acquisitions and disposals • Reviews the effectiveness of the Group's systems of risk management and internal controls (other than over financial reporting) • Oversees the maintenance and development of a supportive culture in relation to the management of risk
Financial System Vulnerabilities Committee	Executive Directors and co-opted non-director members	<ul style="list-style-type: none"> • Oversees controls and procedures designed to identify areas of exposure to financial crime or system abuse • Oversees matters relating to anti-money laundering, sanctions, terrorist financing and proliferation financing • Reviews policies and procedures to ensure continuing obligations to regulatory and law enforcement agencies are met
Risk Management Meeting of the GMB	Group Chief Risk Officer Group Chief Legal Officer Group Chief Executive Group Finance Director All other Group Managing Directors	<ul style="list-style-type: none"> • Formulates high-level global risk policy • Exercises delegated risk management authority • Oversees implementation of risk appetite and controls • Monitors all categories of risk and determines appropriate mitigating action • Promotes a supportive Group culture in relation to risk management
Global Standards Steering Meeting of the GMB	Group Chief Risk Officer Group Chief Legal Officer Group Chief Executive Group Finance Director All other Group Managing Directors	<ul style="list-style-type: none"> • Develops and implements global standards reflecting best practices which must be adopted and adhered to throughout the Group • Oversees initiatives to ensure our conduct matches our values
Global Risk Management Board	Group Chief Risk Officer Chief Risk Officers of HSBC's global businesses and regions Heads of risk areas within the Global Risk Function	<ul style="list-style-type: none"> • Supports the Risk Management Meeting and the Group Chief Risk Officer in providing strategic direction for the Global Risk function, sets priorities and oversees their execution • Oversees consistent approach to accountability for, and mitigation of, risk across the Global Risk function
Subsidiary board committees responsible for risk-related matters and global business risk committees	Independent non-executive directors and/or other independent members, as appropriate	<ul style="list-style-type: none"> • Provides certification to the GRC or intermediate risk committee on risk-related matters and internal controls (other than over financial reporting) of relevant subsidiaries or businesses, as appropriate

Risk reporting and monitoring

The GRC regularly monitors:

- the Group's risk appetite and risk profile against key performance/risk indicators, as set out in the Group's Risk Appetite Statement, on a Group-wide, global business and regional basis;
- the top and emerging risks facing the Group; and
- the risk profiles for separate categories of risk within the Group's business identified in the

Group's Risk Appetite Statement, on a Group-wide, global business and regional basis;

and reviews the mitigating actions proposed by management.

Reports on these items are presented at each meeting of the Committee. Regular reports from the Risk Management Meeting, which is the executive body responsible for overseeing risk, are also presented.

In carrying out its responsibilities the Committee is closely supported by the Group Chief Risk Officer. The Committee also receives regular

presentations from the Group Head of Compliance, Group Head of Internal Audit, the Chief Legal Officer and other business, function and risk heads.

Risk appetite

Risk appetite is a key component of our management of risk. The Board, advised by the GRC, approves the Group's risk appetite, which describes the types and levels of risk that the Group is prepared to accept in executing our strategy and which is set out in the Group's Risk Appetite Statement. Embedding risk appetite statements and the related monitoring and reporting framework across the Group has continued to be an area of significant focus in 2012 with initiatives undertaken to:

- further integrate consideration of risk appetite into the process for developing the Annual Operating Plan and to enhance alignment between Group strategy and risk appetite; and

- continue to embed and develop risk appetite statements throughout the global businesses and functions.

Our risk appetite framework is underpinned by the following core characteristics:

Risk appetite: core characteristics

- Risk must be commensurate with sustainable returns
- Strong balance sheet
- Healthy capital position
- Conservative liquidity management
- Strong brand
- Robust Group structure of separate legal entities
- The global businesses should produce sustainable long-term earnings growth
- Risk diversification

These core characteristics are applied to define the risk appetite statements on a Group-wide, global business and regional level. The relevant strategic and operational objectives, within which we expect businesses and regions to operate, are expressed quantitatively across the following dimensions:

Strategic and operational objectives	
Earnings	1. Generate sustainable economic profit commensurate with the risks taken
Capital and liquidity	2. Maintain capital in excess of regulatory and internal economic capital requirements
	3. Maintain a strong tier 1 ratio comprising a high proportion of core tier 1
	4. Maintain a well diversified funding structure with a particular focus on advances to core funding ratios
	5. Off-balance sheet vehicles should not be material in size relative to the total balance sheet
Impairments and expected losses	6. Manage impairments and expected losses within the Group's tolerance
Risk category and diversification	7. Manage all risk categories within the risk appetite
	8. Harness benefits from business diversification to generate non-volatile and sustainable earnings
	9. Compete for business with international customers where market connectivity is critical, businesses with local customers where we have local scale and products where global scale is critical to effectiveness
Scenario and stress testing	10. Use robust and appropriate scenario stress testing to assess the potential impact on the Group's capital adequacy and strategic plans

Top and emerging risks

Identifying and monitoring top and emerging risks is integral to our approach to risk management. We define a 'top risk' as being a current, emerged risk which has arisen across any of our risk categories, regions or global businesses and has the potential to have a material impact on our financial results or our reputation and the sustainability of our long-term business model, and which may form and crystallise within a one year horizon. We consider an 'emerging risk' to be one which has large uncertain outcomes which may form and crystallise beyond a one-year horizon and, if it were to crystallise, could have a material effect on our long-term strategy.

The GRC discusses top and emerging risks with management at each of its meetings. Current top and emerging risks, which are summarised below, are viewed as falling into three broad categories: macroeconomic and geopolitical; macro-prudential, regulatory and legal risks to our business model; and risks related to our business operations, governance and internal control systems.

The following table shows the current top and emerging risks identified through our risk management processes:

Report of the Directors: Corporate Governance (continued)

Board committees > Group Risk Committee

Current top and emerging risks	
Categories	Top and emerging risks
Macroeconomic and geopolitical risk	<ul style="list-style-type: none"> • Emerging market slow down • Macroeconomic risks within developed economies • Increased geopolitical risk in certain regions
Macro-prudential, regulatory and legal risks to our business model	<ul style="list-style-type: none"> • Regulatory developments affecting our business model and Group profitability • Regulatory investigations, fines, sanctions and requirements relating to conduct of business and financial crime negatively affecting our results and brand • Dispute risk
Risks related to our business operations, governance and internal control systems	<ul style="list-style-type: none"> • Regulatory commitments and consent orders including under the Deferred Prosecution Agreement • Challenges to achieving our strategy in a downturn • Internet crime and fraud • Level of change creating operational complexity and heightened operational risk • Information security risk • Model risk

Stress testing

Our stress testing and scenario analysis programme is central to the monitoring of top and emerging risks. It highlights the vulnerabilities of our business and capital plans to the adverse effects of extreme but plausible events.

The outcome of the testing and analysis is also used to assess the potential impact of the relevant scenarios on the demand for regulatory capital compared with its supply.

Management develops action plans to mitigate risks identified. The extent to which those action plans are implemented depends on management's evaluation of the risks and their potential consequences, taking into account HSBC's risk appetite.

Further information on scenario stress testing is set out on pages 127 and 128.

Stress tests and scenario tests fall into three main classifications: regulatory scenarios; Group-wide business scenarios; and specific business or exposure scenarios.

During the year, the GRC reviewed the outcome of a number of stress tests undertaken by the Group and the implementation of action plans to mitigate risks where appropriate; including stress tests on the Annual Operating Plan under mild and severe macroeconomic scenarios, a Group reverse liquidity stress test, a Group reverse solvency stress test and a eurozone break-up stress test.

Internal Audit has conducted a review of stress testing within the Group including model development, validation and use, and the methodology, governance and management of

enterprise-wide stress testing. The development of HSBC's stress testing and scenario testing analysis programme will continue to be an area of focus for the Committee.

Committee activities

The GRC undertook the following key activities in the discharge of its responsibilities:

- **Oversight of executive risk management.** Regular reports and presentations were received from the Group Chief Risk Officer including at each meeting a presentation of a 'risk map', which provided analysis, on a Group-wide, global business and regional basis, of risk profiles for categories of risk identified in the Group Risk Appetite Statement, and a top and emerging risks report which summarised proposed mitigating actions for identified risks.
- **Legal and regulatory environment.** Reports were received from the Chief Legal Officer on forward-looking legal risks, the Group Head of Compliance on forward-looking compliance risks and the Head of Group Performance and Reward. Regular updates were received on the investigations by US regulatory and law enforcement authorities and US dispute risk and compliance matters in the US and the steps taken to remediate these compliance issues. The Group Finance Director, Group Chief Risk Officer, Group Chief Accounting Officer, Group Company Secretary and the external auditor and other senior executives attended Committee meetings.
- **Stress testing.** The Committee reviewed the outcome of certain stress tests referred to in the

section headed 'Stress Testing' on pages 127 and 128.

- **Review of effectiveness of internal controls.** The Committee undertook an annual review of HSBC's systems of internal controls, other than over financial reporting. During 2012, the Committee monitored the effectiveness of such internal controls and reported regularly to the Board as described on page 334. A series of presentations were made, and reports submitted, by the Group Chief Risk Officer and other business and function heads to the Committee on the risk control framework in their respective business or function. Reports from the Group Head of Internal Audit on the internal audit process and weaknesses identified in internal controls (other than over financial reporting) were presented to the Committee, as well as reports from regulators relating to the internal control systems.
- **Risk appetite.** The Committee reviewed the alignment of risk appetite and Group strategy. Regular reviews were undertaken of the Group's risk profile against the key performance indicators set out in the risk appetite statement which considered the need for any adjustment to the risk appetite. Refinements to the 2012 Risk Appetite Statement were approved with the refined 2012 Risk Appetite Statement being used in the preparation of the Annual Operating Plan for 2013. Reports and presentations were received from the Group Chief Risk Officer, including on the results of HSBC's stress testing and scenario analysis programme.
- **Alignment of remuneration with risk appetite.** Presentations and reports were received on remuneration-related proposals to assist the Committee in giving advice to the Group Remuneration Committee on the alignment of remuneration with risk appetite. The GRC considered risk-related issues to have been appropriately taken into account by the Group Remuneration Committee, including when determining the total variable pay funding pool for the 2012 performance year and the proposed design of the performance scorecard for the 2013 performance year. The Committee received presentations on the procedure for determining individual variable pay awards, including the risk assessment process for identifying matters for which risk-related adjustments may be made to individual and team awards. The process by which an individual's adherence to HSBC Values and the Group's risk-related policies and procedures is

taken into account in performance assessment and determination of variable pay was also reported to the Committee. The Committee provided advice and feedback on risk-related matters to the Group Remuneration Committee where appropriate.

- **Top and emerging risks.** In monitoring top and emerging risks the Committee received reports from the Group Chief Risk Officer and the Group Head of Compliance as well as other members of senior management on risks identified and developments in the Group's business, including the changing regulatory environment; the implications of regulatory investigations and global market risk such as the implications of an emerging market slowdown and the impact on trade and capital flows.
- **Acquisitions and disposals.** The Committee received reports and presentations on risk issues relating to proposed strategic acquisitions and the risk management of disposals and advised the Board appropriately. The Group Head of Mergers and Acquisitions and other members of senior management involved in proposed acquisitions and disposals attended meetings of the Committee as appropriate.
- **Oversight of risk governance framework.** Minutes of the GAC, Group Remuneration Committee and executive committee meetings including the GMB, the Risk Management Meeting and the Group Reputational Risk Policy Committee were provided to Committee members. From January 2013 the minutes of the Global Standards Steering Meeting and from February 2013 the minutes of the Financial System Vulnerabilities Committee will be made available to the Committee.
- **Terms of reference and Committee effectiveness.** The Committee undertook a review of its terms of reference and of its own effectiveness. The Committee recommended to the Board a change to its terms of reference to maintain consistency with the terms of reference of the GAC which were amended to comply with changes to the requirements of the Hong Kong Corporate Governance Code.
- In addition to the scheduled Committee meetings, the Chairman met regularly with the Group Chief Risk Officer, the Group Head of Internal Audit, the Group Finance Director, the Chief Legal Officer and other senior executives as required.

Report of the Directors: Corporate Governance (continued)

Board committees > Financial System Vulnerabilities Committee / Group Remuneration Committee / Nomination Committee

Professional external advice on US compliance matters has been provided by Promontory Financial Group, US financial consultants.

Terms of reference and subsidiary company risk oversight

The GRC is responsible for non-executive oversight of risk management and internal controls, other than internal controls over financial reporting which is the responsibility of the GAC.

To ensure consistency of scope and approach by subsidiary company committees, the GRC has established core terms of reference to guide subsidiary companies when adopting terms of reference for their non-executive risk committees (or audit committees if those committees are also responsible for the oversight of risk related matters).

The Committee's endorsement is required for any proposed material changes to subsidiary company risk committee terms of reference and for appointments to such committees.

A forum for the chairmen of HSBC's principal subsidiary company committees with responsibility for non-executive oversight of financial reporting and risk-related matters was held in June 2012 to share understanding and to facilitate a consistent approach to the way in which these subsidiary committees operate. The next forum will be held in June 2013.

Financial System Vulnerabilities Committee

Members¹	R A Fairhead (Chairman)
	J B Comey ²
	N Fishwick ³
	D Hartnett ^{3,4}
	W Hughes ³
	Sir Simon Robertson
	L H Schrank ³
	J C Zarate ^{3,5}

1 All members appointed on 18 January 2013, unless otherwise indicated.

2 Appointed on 4 March 2013, being the date he became a Director.

3 Co-opted non-director member of the Committee.

4 Appointed on 1 February 2013.

5 Also provides advisory services to the board of HSBC North America Holdings Inc.

The Financial System Vulnerabilities Committee, established by resolution of the Board in January 2013, has non-executive responsibility for governance, oversight and policy guidance over the framework of controls and procedures designed to identify areas where HSBC may become exposed and through that exposure, expose the financial system more broadly to financial crime or system abuse. The Committee will also have oversight of

matters relating to anti-money laundering, sanctions, terrorist financing and proliferation financing, including the establishment, implementation, maintenance and review of adequate policies and procedures sufficient to ensure the continuing obligations to regulatory and law enforcement agencies are met.

The Committee will oversee and report to the Board on implementation of the actions necessary to build assurance in these areas and will seek to provide the Board with a forward-looking perspective on financial crime risk.

The Committee will meet at least four times each year.

Co-opted non-director members

Five co-opted non-director members have been appointed advisers to the Committee to support its work. Brief biographical particulars are set out below:

N Fishwick, CMG: former senior official in the Foreign and Commonwealth Office ('FCO'), specialising in security and counter-terrorism; seconded from 2001 to 2004 to HM Customs and Excise as Head of Intelligence (Law Enforcement), focusing on international counter-narcotics, tax and excise fraud; awarded the CMG in 2009.

D Hartnett, CB: former Permanent Secretary for Tax at HM Revenue and Customs; focused on tax policy development, compliance and enforcement and international tax issues during his 36-year career in tax administration; former deputy chairman of the Organisation for Economic Co-operation and Development's Forum on Tax Administration.

W Hughes, CBE QPM: former head of the UK's Serious Organised Crime Agency; international experience in the disruption, dismantling and criminal investigation of organised crime.

L H Schrank: former chief executive officer of SWIFT, the global financial messaging system which supplies secure standardised financial messaging services and interface software to financial institutions; oversaw SWIFT's relationship with the US Treasury Department and other countries on counter-terrorism issues.

The Honourable J C Zarate: Senior Adviser at the Center for Strategic and International Studies; the Senior National Security Analyst for CBS News; a Visiting Lecturer of Law at the Harvard Law School; national security consultant; former Deputy Assistant

to the President and Deputy National Security Advisor for Combating Terrorism responsible for developing and implementing the US Government's counter-terrorism strategy and policies related to transnational security threats; former Assistant Secretary of the Treasury for Terrorist Financing and Financial Crime; and former federal prosecutor who served on terrorism prosecution teams.

Group Remuneration Committee

	Meetings attended	Meetings eligible to attend
Members¹		
J L Thornton (Chairman)	7	8
J D Coombe	8	8
W S H Laidlaw	8	8
G Morgan ²	5	5
Meetings held in 2012	8	

1 All members are independent non-executive Directors.

2 Retired as a Director on 25 May 2012.

R Fassbind has been appointed a member of the Committee since March 2013.

The Group Remuneration Committee is responsible for approving remuneration policy. As part of its role, it considers the terms of annual incentive plans, share plans, other long-term incentive plans and the individual remuneration packages of executive Directors and other senior Group employees, including all in positions of significant influence and those having an impact on our risk profile and in doing so takes into account the pay and conditions across the Group. No Directors are involved in deciding their own remuneration.

The Directors' Remuneration Report is set out on pages 347 to 367.

Nomination Committee

	Meetings attended	Meetings eligible to attend
Members¹		
Sir Simon Robertson (Chairman)	4	4
R A Fairhead ²	3	4
J W J Hughes-Hallett	4	4
J P Lipsky ³	2	2
Sir Brian Williamson ⁴	1	2
Meetings held in 2012	4	

1 All members are independent non-executive Directors.

2 Took a temporary leave of absence due to illness.

3 Appointed a member of the Committee on 24 May 2012.

4 Retired as a Director on 25 May 2012.

Committee activities

The Committee undertook the following key activities in the discharge of its responsibilities:

- **Appointments of new Directors.** The Committee oversaw the process for the appointments of J Faber, R Fassbind and J P Lipsky as Directors. An external search consultancy, MWM Consulting, was used in relation to these appointments. MWM Consulting has no other connection with HSBC. The Committee also oversaw the process for the appointment of J B Comey, who was introduced to us by a member of senior management. Having regard to his public and private sector roles neither external consultants nor advertising were considered necessary in relation to this appointment.
- **Board appointment process.** The Committee leads the process for Board appointments, with the support of external consultants as appropriate. The Board has satisfied itself that the Committee has appropriate plans in place for orderly succession to the Board reflecting an appropriate balance of skills and experience on the Board.
- **Forward planning.** The Committee adopts a forward-looking approach to potential candidates for appointment to the Board that takes into account the needs and development of the Group's businesses and the expected retirement dates of current Directors.
- **Size, structure and composition.** The Committee monitored the size, structure and composition of the Board through consideration of the skills, knowledge and experience required of the Board and the skills, knowledge and experience of the current Directors. The Committee considered the re-election of Directors at the Annual General Meeting and has recommended to the Board that all Directors should stand for re-election.
- **Diversity.** During the year, the Board adopted a policy on Board diversity which is consistent with the Group's strategic focus on ethnicity, age and gender diversity for the employee base. Board appointments will continue to be made based on merit and candidates will be considered against objective criteria, having due regard for the benefits of diversity on the Board, including gender. The Committee developed measurable objectives to implement this policy and monitored progress towards achieving these objectives. The Board diversity

Report of the Directors: Corporate Governance (continued)

Board committees > Corporate Sustainability Committee

policy is available at www.hsbc.com/investor-relations/governance/corporate-governance-codes. The benefits of diversity continue to influence succession planning and are key criteria in the instructions to external search consultants.

- **Director training and development.** The Committee reviewed and monitored the training and continuous professional development of Directors and senior management.
- **Time commitment and independence of non-executive Directors.** The Committee made recommendations to the Board, having assessed the independence of, and time required from, the non-executive Directors.
- **Terms of reference and Committee effectiveness.** The Committee undertook a review of its terms of reference and its own effectiveness including the Committee's role in assessing the independence of the non-executive Directors as required following changes made to The Hong Kong Corporate Governance Code.

Before recommending an appointment to the Board, the Committee evaluates the balance of skills, knowledge and experience of the Board and, in light of this, and taking into account the needs of the Group's businesses, identifies the role and capabilities required for a particular appointment. Candidates are considered on merit against these criteria. Care is taken to ensure that appointees have enough time to devote to us. Prospective Directors are asked to identify any significant other commitments and confirm they have sufficient time to discharge what is expected of them.

Corporate Sustainability Committee

	Meetings attended	Meetings eligible to attend
Members		
L M L Cha (Chairman) ¹	3	4
N R N Murthy ²	4	4
G V I Davis ³	3	4
Lord May ⁴	4	4
Dame Mary Marsh ⁴	4	4
Meetings held in 2012	4	

1 Appointed Chairman on 1 January 2013.

2 Retired as a Director and Chairman of the Committee on 31 December 2012.

3 Retired as a co-opted non-director member of the Committee on 29 November 2012.

4 Co-opted non-director member of the Committee.

J W J Hughes-Hallett has been a member of the Committee since 1 January 2013.

Sustainability governance

The Corporate Sustainability Committee is responsible for advising the Board, committees of the Board and executive management on corporate sustainability policies across the Group including environmental, social and ethical issues.

Corporate Sustainability exists as a global function. Senior executives are charged with implementing sustainable business practice in all major regions through inclusion in the HSBC Global Standards Manuals; and, through induction and developmental training. Local teams are in charge of embedding corporate sustainability strategies within banking activities.

HSBC reports on its progress in developing and implementing its sustainability strategy annually in the HSBC Sustainability Report, which is independently verified and prepared using the Global Reporting Initiative framework. The *HSBC Sustainability Report 2012* will be issued on 24 May 2013 and will be available at www.hsbc.com/sustainability.

Corporate sustainability

At HSBC, we understand that the success of our business is closely connected to the environmental, social and economic landscape. For us, corporate sustainability means achieving sustainable profit growth so that we can continue to reward shareholders and employees, build long-lasting relationships with customers and suppliers, pay taxes and duties in those countries where we operate, and invest in communities for future growth. The way we do business is as important as what we do: our responsibilities to our customers, employees and shareholders as well as to the countries and communities in which we operate go far wider than simply being profitable.

Our continuing financial success depends, in part, on our ability to identify and address environmental, social and ethical factors which present risks or opportunities for the business. These can affect our reputation, drive employee engagement, help manage the risks of lending, leverage savings through eco-efficiency and secure new revenue streams. They generally fall into one or more of the four broad areas discussed below.

Business finance

We aim to build long-term customer relationships around the world through the provision of a consistent and high-quality service and customer experience. We use the benefits of our scale,

financial strength, geographical reach and strong brand value to achieve this.

We aim to take advantage of the opportunities and manage the risks presented by emerging global trends by developing sustainable business models to address them. We understand 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; we face local water supply shortages as global demand increases.

HSBC continues to play 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, our Climate Change Centre of Excellence has continued to research the likely effects that climate change, and the responses to it, will have on our business and those of our customers. In the past 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 continues to support 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. 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 HSBC'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

We focus our environmental initiatives primarily on addressing and responding to issues associated with climate change, including energy use, water and waste management. This issue has the potential to affect materially our customers and, by extension, our long-term success, introducing new risks to business activity. We continue to focus on the ten

goals of our operational sustainability strategy, which we announced at the end of 2011. Between 2012 and 2020 we aim to reduce our annual employee carbon emissions by one tonne, from 3.5 to 2.5 tonnes.

HSBC's carbon dioxide emissions

For the period 1 October 2011 to 30 September 2012, carbon dioxide emissions from HSBC's global operations were 963,000 tonnes. This was 3% less than the 991,000 tonnes emitted in 2011. This figure is subject to independent verification. Further information on the Group's carbon dioxide emissions will be given in the *HSBC Sustainability Report 2012*.

Community investment

We have a long-standing commitment to the communities in which we operate. Many of our key markets are emerging economies. Our operations bring benefits to our host countries through tax contributions, and to local people and businesses through employment, training, purchasing and investment. Beyond our core business, we aim to encourage social and economic opportunity through community investment activities. Our focus is on education and the environment because we believe 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 non-government organisations ('NGOs') and charities. Our global education programmes focus on helping disadvantaged children, promoting financial literacy and international and cultural understanding.

In 2012, we launched our new flagship environmental programme, the HSBC Water Programme. This is a five-year, US\$100m 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 economies to prosper, driving development and social-economic growth. Following the success of our previous HSBC Climate Partnership, this programme will create a community of employees and opportunities for employee involvement and volunteering.

In 2012, we donated a total of US\$120m to community investment projects (2011: US\$96m).

Report of the Directors: Corporate Governance (continued)

Internal control

Employee issues

'Employee engagement' describes employees' emotional and intellectual commitment to their organisation and its success and is critical to the long-term ability of the Group to deliver the highest quality of financial services. Our Global People Survey is carried out every other year and shows that employees value our commitment to sustainable business practices and view us as being a leader in this regard. In the latest survey, taken in 2011, 81% of colleagues said they were satisfied with the actions HSBC is taking to embed sustainability (e.g. environmental and social issues) into the way we run our business.

Sustainability risk

Our approach to managing sustainability risk is detailed in the Appendix to Risk on page 280.

Internal control

The Directors are responsible for internal control in HSBC and for reviewing its effectiveness. Procedures have been designed for safeguarding assets against unauthorised use or disposal; for maintaining proper accounting records; and for the reliability and usefulness of financial information used within the business or for publication. Such procedures are designed to manage and mitigate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement, errors, losses or fraud. The procedures also enable HSBC Holdings to discharge its obligations under the 'Handbook of Rules and Guidance' issued by the FSA, HSBC's lead regulator.

The key procedures that the Directors have established are designed to provide effective internal control within HSBC and accord with the 'Internal Control: Revised Guidance for Directors on the Combined Code' issued by the Financial Reporting Council. Such procedures for the ongoing identification, evaluation and management of the significant risks faced by HSBC have been in place throughout the year and up to 4 March 2013, the date of approval of the *Annual Report and Accounts 2012*. In the case of companies acquired during the year, the internal controls in place are being reviewed against HSBC's benchmarks and integrated into HSBC's processes.

HSBC's key internal control procedures include the following:

- **Global standards.** Functional, operating, financial reporting and certain management reporting standards are established by global

function management committees, for application throughout HSBC. These are supplemented by operating standards set by functional and local management as required for the type of business and geographical location of each subsidiary.

- **Delegation of authority within limits set by the Board.** Authority to operate the various subsidiaries and responsibilities for financial performance against plans and for capital expenditure are delegated to their respective chief executive officers within limits set by the Board. Delegation of authority from the Board to individuals requires those individuals to maintain a clear and appropriate apportionment of significant responsibilities and to oversee the establishment and maintenance of systems of control appropriate to the business. The appointment of executives to the most senior positions within HSBC requires the approval of the Board.
- **Risk identification and monitoring.** Systems and procedures are in place in HSBC to identify, control and report on the major risks including credit, market, liquidity, capital, financial management, model, reputational, pension, strategic, sustainability, operational (including accounting, tax, legal, compliance, fiduciary, information, external fraud, internal fraud, political, physical, business continuity, systems operations, project and people risk) and Islamic finance risk. Exposure to these risks is monitored by risk management committees, asset and liability committees and executive committees in subsidiaries and, for the Group, in Risk Management Meetings ('RMM') of the GMB which are chaired by the Group Chief Risk Officer. RMM meets each month (except August) to address asset, liability and risk management issues. HSBC's operational risk profile and the effective implementation of the Group's operational risk management framework is monitored by the Global Operational Risk and Control Committee ('GORCC'), which reports to the RMM. Model risks are monitored by the Model Oversight Committee which also reports to the RMM. The minutes of the GMB meetings and the RMM are provided to members of the GAC, the GRC and the Board.
- **Changes in market conditions/practices.** Processes are in place to identify new risks arising from changes in market conditions/practices or customer behaviours, which could expose HSBC to heightened risk

of loss or reputational damage. During 2012, attention was focused on:

- severe economic slowdown in mature economies impacting global growth;
 - eurozone members departure from the currency union;
 - increased geopolitical risk;
 - emerging market slowdown;
 - macroeconomic risks within developed economies;
 - regulatory developments affecting our business model and Group profitability;
 - regulatory investigations, fines, sanctions and requirements relating to conduct of business and financial crime negatively affecting our results and brand;
 - dispute risk;
 - regulatory commitments and consent orders including the Deferred Prosecution Agreements;
 - challenges to achieving our strategy in a downturn;
 - internet crime and fraud;
 - social media risk;
 - level of change creating operational complexity and heightened operational risk;
 - information risk; and
 - model risk.
- **Strategic plans.** Periodic strategic plans are prepared for global businesses, global functions and certain geographical regions within the framework of the Group's strategy. Annual Operating Plans, informed by detailed analysis of risk appetite describing the types and quantum of risk that we are prepared to take in executing our strategy, are prepared and adopted by all major HSBC operating companies and set out the key business initiatives and the likely financial effects of those initiatives.
 - **Disclosure Committee.** The Disclosure Committee reviews material public disclosures made by HSBC Holdings for any material errors, misstatements or omissions. The membership of the Disclosure Committee, which is chaired by the Group Company Secretary, includes the heads of Global Finance, Legal, Risk and Compliance, Communications, Investor Relations and Internal Audit functions and representatives from the principal regions and global businesses. The integrity of disclosures is underpinned by structures and processes within the Finance and Risk functions that support expert and rigorous analytical review of financial reporting complemented by certified reviews by heads of global businesses,

global functions and certain legal entities.

- **Financial reporting.** The Group financial reporting process for preparing the consolidated *Annual Report and Accounts 2012* is controlled using documented accounting policies and reporting formats, supported by a chart of accounts with detailed instructions and guidance on reporting requirements, issued by Group Finance to all reporting entities within the Group in advance of each reporting period end. The submission of financial information from each reporting entity to Group Finance is subject to certification by the responsible financial officer, and analytical review procedures at reporting entity and Group levels.
- **Responsibility for risk management.** Management of global businesses and global functions are primarily accountable for managing, measuring and monitoring their risks and controls. Processes consistent with the Three Lines of Defence principle are in place to ensure weaknesses are escalated to senior management and addressed.
- **IT operations.** Centralised functional control is exercised over all IT developments and operations. Common systems are employed for similar business processes wherever practicable.
- **Functional management.** Global functional management is responsible for setting policies, procedures and standards for the following risks: credit, market, liquidity, capital, financial management, model, reputational, pension, strategic, sustainability and operational risk (including accounting, tax, legal, compliance, fiduciary, information security, security and fraud, systems and people risk). Authorities to enter into credit and market risk exposures are delegated with limits to line management of Group companies. The concurrence of the appropriate global function is required, however, to credit proposals with specified higher risk characteristics. Credit and market risks are measured and reported on in subsidiaries and aggregated for review of risk concentrations on a Group-wide basis.
- **CEO Attestation process.** Global Operational Risk coordinate the annual CEO Attestation process under which the chief executive officer of each of the Group's material subsidiaries confirms that the internal control framework applicable to that subsidiary has been assessed and any significant open issues have been identified, with action plans in place to address weaknesses. The remediation of these issues is

Report of the Directors: Corporate Governance (continued)

Internal control > Going concern basis / Employees

monitored by the Operational Risk and Internal Control ('ORIC') teams for the relevant regions/global businesses and reports on progress are presented to their ORIC committees and quarterly to Global Operational Risk. An annual report and updates on identified issues and remediation plans are presented to the GRC and the GAC.

- Internal Audit.** The establishment and maintenance of appropriate systems of internal control is primarily the responsibility of business management. The Global Internal Audit function, which is centrally controlled, provides independent assurance in respect of the design and operating effectiveness of the risk management and control frameworks across the Group, focusing on the areas of greatest risk to HSBC using a risk-based approach. The head of this function reports to the Group Chairman, the Group Chief Executive Officer, the GAC and the GRC on risk-related matters.
- Internal Audit recommendations.** Executive management is responsible for ensuring that recommendations made by the Internal Audit function are implemented within an appropriate and agreed timetable. Confirmation to this effect must be provided to Internal Audit.
- Reputational risk.** Policies to guide subsidiary companies and management at all levels in the conduct of business to safeguard the Group's reputation are established by the Board and its committees, subsidiary company boards and their committees and senior management. Reputational risks can arise from a variety of causes including environmental, social and governance issues, as a consequence of operational risk events and as a result of employees acting in a manner inconsistent with HSBC's Values. As a banking group, HSBC's good reputation depends upon the way in which it conducts its business but it can also be affected by the way in which clients, to which it provides financial services, conduct their business or use financial products and services.

The GAC has non-executive responsibility for oversight of internal controls over financial reporting and the GRC has non-executive responsibility for internal controls other than over financial reporting.

The GRC and the GAC have kept under review the effectiveness of this system of internal control and have reported regularly to the Board of Directors. In carrying out their reviews the GRC and the GAC receive regular business and operational risk assessments; regular reports from the Group

Chief Risk Officer and the Head of Global Internal Audit; reports on the annual reviews of the internal control framework of HSBC Holdings which cover all internal controls, both financial and non-financial; annual confirmations from chief executives of principal subsidiary companies as to whether there have been any material losses, contingencies or uncertainties caused by weaknesses in internal controls; internal audit reports; external audit reports; prudential reviews; and regulatory reports. The GRC monitors the status of top and emerging risks which impact or may impact the Group and considers whether the mitigating actions put in place are appropriate. In addition, when unexpected losses have arisen or when incidents have occurred which indicate gaps in the control framework or in adherence to Group policies, the GRC and the GAC review special reports, prepared at the instigation of management, which analyse the cause of the issue, the lessons learned and the actions proposed by management to address the issue.

The Directors, through the GRC and the GAC, have conducted an annual review of the effectiveness of our system of internal control covering all material controls, including financial, operational and compliance controls, risk management systems, the adequacy of resources, qualifications and experience of staff of the accounting and financial reporting function and the risk function, and their training programmes and budget. The review does not extend to joint ventures or associates. The GRC and the GAC have received confirmation that executive management has taken or is taking the necessary actions to remedy any failings or weaknesses identified through the operation of our framework of controls.

Going concern basis

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Group and parent company have the resources to continue in business for the foreseeable future. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including future projections of profitability, cash flows and capital resources. Further information relevant to the assessment is provided elsewhere in this report. In particular, HSBC's principal activities, business and operating models, strategic direction and top and emerging risks are described in the 'Overview' section; a financial summary, including a review of the consolidated income statement and consolidated balance sheet, is provided in the 'Operating and Financial Review' section; HSBC's objectives,

policies and processes for managing credit, liquidity and market risk are described in the 'Risk' section; and HSBC's approach to capital management and allocation is described in the 'Capital' section.

Employees

At 31 December 2012 we had a total workforce of 270,000 full-time and part-time employees compared with 298,000 at the end of 2011 and 307,000 at the end of 2010. Our main centres of employment are the UK with approximately 48,000 employees, India 30,000, Hong Kong 28,000, Brazil 23,000, mainland China 18,000, Mexico 18,000, the US 17,000 and France 10,000.

In the context of the current global financial services operating environment, a high performance and values-led work force is critical. We encourage open and honest communication in decision making. Employment issues and financial, economic, regulatory and competitive factors affecting HSBC's performance are regularly shared with our employees.

Global People Survey

In 2012, quarterly Pulse Surveys were introduced to assess in a more timely way the understanding and execution of our Group strategy, our culture, our performance and the engagement of our people generally. Every three months, a quarter of the Group's employees are randomly sampled and hence all employees are covered over the course of the year. A Global People Survey will take place biennially, the next one being in 2013.

Over 2012, the Group strategy index score improved by 2% to 54% in the fourth quarter and the average participation rate was 56%, which is around median for comparable surveys externally.

Reward

Our approach to reward is meritocratic and market competitive, underpinned by an ethical and values based performance culture which aligns the interests of our employees, shareholders, regulators and customers. See 'Employee share plans' on pages 336 to 337.

Employee relations

We negotiate and consult with recognised unions as appropriate. The five highest concentrations of union membership are in Argentina, Brazil, mainland China, Malta and Mexico. It is our policy to maintain well-developed communications and consultation programmes with all employee representative bodies and there have been no material disruptions to our operations from labour disputes during the past five years.

Diversity and inclusion

HSBC is committed to building a values-driven high performance culture where all employees are valued, respected and where their opinions count. We remain committed to meritocracy, which requires a diverse and inclusive culture where employees believe that their views are heard, their concerns are attended to and they work in an environment where bias, discrimination and harassment on any matter, including gender, age, ethnicity, religion, sexuality and disability are not tolerated and where advancement is based on objectivity. Our inclusive culture helps us respond to our diverse customer base, while developing and retaining a secure supply of skilled, committed employees. Our culture will be strengthened by employing the best people and optimising their ideas, abilities and differences.

Oversight of our diversity and inclusion agenda and related activities resides with executives on the Group Diversity Committee, complemented by the Group People Committee and local People/Diversity Committees.

Staff development

The development of employees in both developed and emerging markets is essential to the future strength of our business. We have implemented a systematic approach to identifying, developing and deploying talented employees to ensure an appropriate supply of high calibre individuals with the values, skills and experience for current and future senior management positions.

In 2012, we continued to build global consistency across our learning curricula and to improve the relevance and quality of learning programmes. We have endeavoured to achieve a standard of excellence focusing on leadership, values and technical capability.

Report of the Directors: Corporate Governance (continued)

Employees

Employment of disabled persons

We believe in providing equal opportunities for all employees. The employment of disabled persons is included in this commitment and the recruitment, training, career development and promotion of disabled persons is based on the aptitudes and abilities of the individual. Should employees become disabled during their employment with us, efforts are made to continue their employment and, if necessary, appropriate training and reasonable equipment and facilities are provided.

Health and safety

The maintenance of appropriate health and safety standards remains a key responsibility of all managers and we are committed to proactively managing all health and safety risks associated with our business. Our objectives are to identify, remove, reduce or control material risks relating to fires and accidents or injuries to employees, customers and visitors.

Group policies, standards and guidance for the management of health and safety are set by global Corporate Real Estate. Achieving these in each country in which we operate is the responsibility of the Chief Operating Officer of that country with support and coordination provided by the Health and Safety Coordinator for that country.

In terms of physical and geopolitical risk, Global Security and Fraud Risk provide regular security risk assessments to assist management in judging the level of terrorist and violent criminal threat. Regional Security and Fraud Risk functions conduct regular security reviews of all Group buildings to ensure measures to protect our staff, buildings, assets and information are appropriate to the level of threat.

We remain committed to maintaining our preparedness and to ensuring the highest standards of health and safety wherever in the world we operate.

Remuneration policy

The quality and commitment of our human capital is fundamental to our success and accordingly the Board aims to attract, retain and motivate the very best people. As trust and relationships are vital in our business our goal is to recruit those who are committed to making a long-term career with the organisation.

HSBC's reward strategy supports this objective through balancing of both short-term and sustainable performance. Our reward strategy aims to reward

success, not failure, and be properly aligned with our risk framework and related outcomes. In order to ensure alignment between remuneration and our business strategy, individual remuneration is determined through assessment of performance delivered against both annual and long-term objectives summarised in performance scorecards as well as adherence to the HSBC Values of being 'open, connected and dependable' and acting with 'courageous integrity'. Altogether, performance is judged, not only on what is achieved over the short and long-term, but also on how it is achieved, as the latter contributes to the sustainability of the organisation.

The financial and non-financial measures incorporated in the annual and long-term scorecards are carefully considered to ensure alignment with the long-term strategy of the Group.

Further information on the Group's approach to remuneration is given on page 347.

Employee share plans

Share options and discretionary awards of shares granted under HSBC share plans align the interests of employees with those of shareholders. The tables on the following pages set out the particulars of outstanding options, including those held by employees working under employment contracts that are regarded as 'continuous contracts' for the purposes of the Hong Kong Employment Ordinance. The options were granted at nil consideration. No options have been granted to substantial shareholders, suppliers of goods or services, or in excess of the individual limit for each share plan. No options were cancelled by HSBC during the year.

A summary for each plan of the total number of the options which were granted, exercised or lapsed during 2012 is shown in the following tables. Further details required to be disclosed pursuant to Chapter 17 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited are available on our website at www.hsbc.com by selecting 'Investor Relations', then 'Governance', then 'Share Plans', and on the website of The Stock Exchange of Hong Kong Limited at www.hkex.com.hk or can be obtained upon request from the Group Company Secretary, 8 Canada Square, London E14 5HQ. Particulars of options held by Directors of HSBC Holdings are set out on page 363.

Note 7 on the Financial Statements gives details on share-based payments, including discretionary awards of shares granted under HSBC share plans.

All-employee share option plans

All-employee share option plans have operated within the Group and employees on the first working day of the year were eligible to be granted options to acquire HSBC Holdings ordinary shares. Options under the plans are usually exercisable after one, three or five years. The exercise of options may be advanced to an earlier date in certain circumstances, for example on retirement, and may be extended in certain circumstances, for example on the death of a participant, the executors of the participant's estate may exercise options up to six months beyond the

normal exercise period. The middle market closing price for HSBC Holdings ordinary shares quoted on the London Stock Exchange, as derived from the Daily Official List on 23 April 2012, the day before options were granted in 2012, was £5.46. A review of the plans will be undertaken in 2013 and there will be no grant of options while that review is ongoing.

The all-employee share option plans will terminate on 27 May 2015 unless the Directors resolve to terminate the plans at an earlier date.

HSBC Holdings All-employee Share Option Plans

						HSBC Holdings ordinary shares				
Dates of awards		Exercise price		Exercisable		At	Granted	Exercised	Lapsed	At
from	to	from	to	from	to	1 Jan 2012	during year	during year	during year	31 Dec 2012
Savings-Related Share Option Plan¹										
26 Apr 2006	24 Apr 2012	(£) 3.3116	(£) 6.6870	1 Aug 2011	31 Jan 2018	68,499,109	20,726,298	25,390,031	8,859,311	54,976,065
Savings-Related Share Option Plan: International²										
26 Apr 2006	24 Apr 2012	(£) 3.3116	(£) 6.6870	1 Aug 2011	31 Jan 2018	26,615,253	8,549,570	12,032,666	5,663,420	17,468,737
26 Apr 2006	24 Apr 2012	(US\$) 4.8876	(US\$) 12.0958	1 Aug 2011	31 Jan 2018	9,752,066	2,666,374	3,440,522	2,489,024	6,488,894
26 Apr 2006	24 Apr 2012	(€) 3.6361	(€) 9.5912	1 Aug 2011	31 Jan 2018	3,176,265	827,832	1,407,390	416,444	2,180,263
26 Apr 2006	24 Apr 2012	(HK\$) 37.8797	(HK\$) 94.5057	1 Aug 2011	31 Jan 2018	45,422,511	12,098,312	21,684,534	4,198,449	31,637,840

1 The weighted average closing price of the shares immediately before the dates on which options were exercised was £5.46.

2 The weighted average closing price of the shares immediately before the dates on which options were exercised was £5.45.

Discretionary Share Option Plans

There have been no grants of discretionary share options under employee share plans since 30 September 2005.

						HSBC Holdings ordinary shares			
Dates of awards		Exercise price (£)		Exercisable		At	Exercised	Lapsed	At
from	to	from	to	from	to	1 Jan 2012	during year	during year	31 Dec 2012
HSBC Holdings Group Share Option Plan^{1,2}									
7 May 2002	20 Apr 2005	6.0216	7.9606	7 May 2005	20 Apr 2015	120,797,419	1,606,032	32,018,464	87,172,923
HSBC Share Plan									
30 Sep 2005		7.9911		30 Sep 2008	30 Sep 2015	86,046	—	—	86,046

1 The HSBC Holdings Group Share Option Plan expired on 26 May 2005. No options have been granted under the Plan since that date.

2 The weighted average closing price of the shares immediately before the dates on which options were exercised was £6.43.

Subsidiary company share plans

HSBC France

When it was acquired in 2000, HSBC France and certain of its subsidiary companies operated employee share option plans under which options could be granted over their respective shares.

Under the terms of the employee share option plan, holders of options to acquire shares of HSBC France were obliged to exchange the HSBC France shares they received on exercise of these options for HSBC Holdings ordinary shares. Details of options to acquire shares in HSBC France are set out in the following table. No further options will be granted under this share plan.

Report of the Directors: Corporate Governance (continued)**Employees > Other required disclosures / 2013 AGM***HSBC France*

Date of award	Exercise price (€)	Exercisable		HSBC France shares of €5			
		from	to	At 1 Jan 2012 ¹	Exercised during year	Lapsed during year	At 31 Dec 2012 ¹
1 Oct 2002	142.84	2 Oct 2005	1 Oct 2012	22,645	—	22,645	—

1 If options over HSBC France Shares had been exercised, these options would have been exchanged for HSBC Holdings ordinary shares in the ratio of 13.499897 HSBC Holdings ordinary shares for each HSBC France share. At 31 December 2012, The CCF Employee Benefit Trust 2001 (Private Banking France) held 989,502 HSBC Holdings ordinary shares.

HSBC Finance

Upon the acquisition of HSBC Finance in 2003, all outstanding options over, and rights to receive, HSBC Finance common shares were converted into options over, and rights to receive, HSBC Holdings ordinary shares in the same ratio as the share exchange offer for the acquisition of HSBC Finance (2.675 HSBC Holdings ordinary shares for each

HSBC Finance common share). The exercise price payable for each option was adjusted using the same exchange ratio.

Details of options to acquire shares in HSBC Holdings under the share plan of HSBC Finance are set out in the following table. No further options will be granted under this share plan.

HSBC Finance: 1996 Long-Term Executive Incentive Compensation Plan

Date of award	Exercise price (US\$)	Exercisable		HSBC Holdings ordinary shares			
		from	to	At 1 Jan 2012	Exercised during year ¹	Lapsed during year	At 31 Dec 2012 ²
20 Nov 2002	9.29	20 Nov 2003	20 Nov 2012	2,429,538	2,053,838	375,700	—

1 The weighted average closing price of the shares immediately before the dates on which options were exercised was £6.06.

2 At 31 December 2012, the HSBC (Household) Employee Benefit Trust 2003 held 281,477 HSBC Holdings ordinary shares and 1,455 American Depositary Shares, each of which represents five HSBC Holdings ordinary shares.

HSBC Bank Bermuda

Upon the acquisition of HSBC Bank Bermuda Limited ('HSBC Bank Bermuda') in 2004, all outstanding options over HSBC Bank Bermuda shares were converted into options to acquire HSBC Holdings ordinary shares using an exchange ratio calculated by dividing US\$40 (being the consideration paid for each HSBC Bank Bermuda share) by the average price of HSBC Holdings

ordinary shares over the five day period to the completion of the acquisition. The exercise price payable for each option was adjusted using the same exchange ratio.

Details of options to acquire shares in HSBC Holdings under the share plans of HSBC Bank Bermuda are set out in the following table. No further options will be granted under the share plans of HSBC Bank Bermuda.

HSBC Bank Bermuda

Dates of awards		Exercise price (US\$)		Exercisable		HSBC Holdings ordinary shares			
						At	Exercised	Lapsed	At
from	to	from	to	from	to	1 Jan 2012	during year	during year	31 Dec 2012 ¹
Share Option Plan 2000									
30 Jan 2002	21 Apr 2003	9.32	14.02	30 Jan 2003	21 Apr 2013	1,014,026	—	864,102	149,924
Directors' Share Option Plan									
3 Apr 2002		13.95		3 Apr 2003	3 Apr 2012	16,881	—	16,881	—

1 At 31 December 2012, the HSBC (Bank of Bermuda) Employee Benefit Trust 2004 held 2,108,830 HSBC Holdings ordinary shares which may be used to satisfy the exercise of employee share options.

Other required disclosures

Further information about share capital, directors' interests, supplier payment policy, dividends and shareholders is set out in the Appendix to this section on pages 340 to 346.

2013 Annual General Meeting

Our Annual General Meeting in 2013 will be held at the Barbican Hall, Barbican Centre, London EC2 on 24 May 2013 at 11.00am.

An informal meeting of shareholders will be held at 1 Queen's Road Central, Hong Kong on Monday 20 May 2013 at 4.30pm.

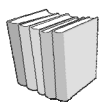
Resolutions to receive the *Annual Report and Accounts 2012*, approve the Directors' Remuneration Report, elect or re-elect Directors and reappoint KPMG Audit Plc as auditor will be submitted to the Annual General Meeting. KPMG Audit Plc has expressed its willingness to continue in office and

the Group Audit Committee and the Board has recommended that KPMG Audit Plc be reappointed. Resolutions will also be submitted to the Annual General Meeting to renew the authority for the allotment of shares, disapply pre-emption rights, renew the authority for the purchase of ordinary shares, and approve general meetings (other than Annual General Meetings) being called on a minimum of 14 clear days' notice.

A live webcast of the Annual General Meeting will be available on www.hsbc.com. From shortly after the conclusion of the Annual General Meeting until 30 June 2013 a recording of the proceedings will be available on www.hsbc.com.

On behalf of the Board
D J Flint, *Group Chairman*
HSBC Holdings plc
Registered number 617987

4 March 2013

Report of the Directors: Corporate Governance (continued)**Appendix > Other required disclosures > Share capital****Appendix to Report of the Directors****Other required disclosures****Share capital****Issued share capital**

The nominal value of our issued share capital paid up at 31 December 2012 was US\$9,238,018,832 divided into 18,476,008,664 ordinary shares of US\$0.50 each, 1,450,000 non-cumulative preference shares of US\$0.01 each and 1 non-cumulative preference share of £0.01.

The percentage of the nominal value of our total issued share capital paid up at 31 December 2012 represented by the ordinary shares of US\$0.50 each, non-cumulative preference shares of US\$0.01 each and the non-cumulative preference share of £0.01 was approximately 99.9998%, 0.0002%, and 0%, respectively.

Rights and obligations attaching to shares

The rights and obligations attaching to each class of shares in our share capital are set out in our Articles of Association subject to certain rights and obligations that attach to each class of preference share as determined by the Board prior to allotment of the relevant preference shares. Set out below is a summary of the rights and obligations attaching to each class of shares with respect to voting, dividends, capital and, in the case of the preference shares, redemption.

To be registered, a transfer of shares must be in relation to shares which are fully paid up and on which we have no lien and to one class of shares denominated in the same currency. The transfer must be in favour of a single transferee or no more than four joint transferees and it must be duly stamped (if required). The transfer must be delivered to our registered office or our Registrars accompanied by the certificate to which it relates or such other evidence that proves the title of the transferor.

If a shareholder or any person appearing to be interested in our shares has been sent a notice under section 793 of the Companies Act 2006 (which confers upon public companies the power to require information from any person whom we know or have reasonable cause to believe to be interested in the shares) and has failed in relation to any shares (the 'default shares') to supply the information requested within the period set out in the notice, then the member, unless the Board otherwise determines, is not entitled to be present at or to vote the default shares at any general meeting or to exercise any other right conferred by being a shareholder. If the default shares represent at least 0.25% in nominal value of the issued shares of that class, unless the Board otherwise determines, any dividend shall be withheld by the Company without interest, no election may be made for any scrip dividend alternative, and no transfer of any shares held by the member will be registered except in limited circumstances.

Ordinary shares

Subject to the Companies Act 2006 and the Articles of Association, HSBC Holdings may, by ordinary resolution, declare dividends to be paid to the holders of ordinary shares, though no dividend shall exceed the amount recommended by the Board. The Board may pay interim dividends as appears to the Board to be justified by the profits available for distribution. All dividends shall be apportioned and paid proportionately to the percentage of the nominal amount paid up on the shares during any portion or portions of the period in respect of which the dividend is paid, but if any share is issued on terms providing that it shall rank for dividend as from a particular date, it shall rank for dividend accordingly. Subject to the Articles of Association, the Board may, with the prior authority of an ordinary resolution passed by the shareholders and subject to such terms and conditions as the Board may determine, offer to any holders of ordinary shares the right to elect to receive ordinary shares of the same or a different currency, credited as fully paid, instead of cash in any currency in respect of the whole (or some part, to be determined by the Board) of any dividend specified by the ordinary resolution. At the 2012 Annual General Meeting shareholders gave authority to the Directors to offer a scrip dividend alternative until the earlier of the conclusion of the Annual General Meeting in 2017 or 24 May 2017.

Preference shares

There are three classes of preference shares in the share capital of HSBC Holdings, non-cumulative preference shares of US\$0.01 each (the 'Dollar Preference Shares'), non-cumulative preference shares of £0.01 each (the

‘Sterling Preference Shares’) and non-cumulative preference shares of €0.01 (the ‘Euro Preference Shares’). The Dollar Preference Shares in issue are Series A Dollar Preference Shares and the Sterling Preference Share in issue is a Series A Sterling Preference Share. There are no Euro Preference Shares in issue.

Dollar Preference Shares

Holders of the Dollar Preference Shares are only entitled to attend and vote at general meetings if any dividend payable on the relevant preference shares in respect of such period as the Board shall determine prior to allotment thereof is not paid in full or in such other circumstances, and upon and subject to such terms, as the Board may determine prior to allotment of the relevant preference shares. In the case of the Dollar Preference Shares in issue at 4 March 2013 the relevant period determined by the Board is four consecutive dividend payment dates. Whenever holders of the Dollar Preference Shares are entitled to vote on a resolution at a general meeting, on a show of hands every such holder who is present in person or by proxy shall have one vote and on a poll every such holder who is present in person or by proxy shall have one vote per preference share held by him or her or such number of votes per share as the Board shall determine prior to allotment of such share.

Subject to the Articles of Association, holders of the Dollar Preference Shares have the right to a non-cumulative preferential dividend at such rate, on such dates and on such other terms and conditions as may be determined by the Board prior to allotment thereof in priority to the payment of any dividend to the holders of ordinary shares and any other class of shares of HSBC Holdings in issue (other than (i) the other preference shares in issue and any other shares expressed to rank *pari passu* therewith as regards income; and (ii) any shares which by their terms rank in priority to the relevant preference shares as regards income). A dividend of US\$62 per annum is payable on each Dollar Preference Share in issue at 4 March 2013. The dividend is paid at the rate of US\$15.50 per quarter at the sole and absolute discretion of the Board.

A dividend will not be declared or paid on the Dollar Preference Shares if payment of the dividend would cause HSBC Holdings not to meet the applicable capital adequacy requirements of the FSA or the profit of HSBC Holdings available for distribution as dividends is not sufficient to enable HSBC Holdings to pay in full both dividends on the relevant preference shares and dividends on any other shares that are scheduled to be paid on the same date and that have an equal right to dividends. Dividends will not be declared or paid on any class of shares of HSBC Holdings ranking lower in the right to dividends than the Dollar Preference Shares nor redeem nor purchase in any manner any of its other shares ranking equal with or lower than the Dollar Preference Shares unless it has paid in full, or set aside an amount to provide for payment in full, the dividends on the Dollar Preference Shares for the then-current dividend period.

The Dollar Preference Shares carry no rights to participate in the profits or assets of HSBC Holdings other than as set out in the Articles of Association and subject to the Companies Act 2006, do not confer any right to participate in any offer or invitation by way of rights or otherwise to subscribe for additional shares in HSBC Holdings, do not confer any right of conversion and do not confer any right to participate in any issue of bonus shares or shares issued by way of capitalisation of reserves.

Subject to the relevant insolvency laws and the Articles of Association of HSBC Holdings, holders of the Dollar Preference Shares have the right in a winding up of HSBC Holdings to receive out of the assets of HSBC Holdings available for distribution to its shareholders, in priority to any payment to the holders of the ordinary shares and any other class of shares of HSBC Holdings in issue (other than (i) the other relevant preference shares and any other shares expressed to rank *pari passu* therewith as regards repayment of capital; and (ii) any shares which by their terms rank in priority to the relevant preference shares as regards repayment of capital), a sum equal to any unpaid dividend on the Dollar Preference Shares which is payable as a dividend in accordance with or pursuant to the Articles of Association and the amount paid up or credited as paid up on the Dollar Preference Shares together with such premium (if any) as may be determined by the Board prior to allotment thereof. In the case of the Dollar Preference Shares in issue at 4 March 2013, the premium is US\$999.99 per Dollar Preference Share.

The Dollar Preference Shares may be redeemed in accordance with the Articles of Association and the terms on which Dollar Preference Shares were issued and allotted. In the case of the Dollar Preference Shares in issue at 4 March 2013, HSBC Holdings may redeem such shares in whole at any time on or after 16 December 2010, subject to the prior consent of the FSA.

Report of the Directors: Corporate Governance (continued)**Appendix > Other required disclosures > Share capital / Directors' interests***Sterling Preference Shares*

The Sterling Preference Shares carry the same rights and obligations under the Articles of Association as the Dollar Preference Shares, save in respect of certain rights and obligations that attach to Sterling Preference Shares to be determined by the Board prior to allotment of the relevant preference shares and the timing and payment of proceeds from the redemption of each class of share. The one Sterling Preference Share in issue at 4 March 2013 carries the same rights and obligations as the Dollar Preference Shares in issue at 4 March 2013 to the extent described in the section above save as follows:

1. the holder of the Sterling Preference Share is not entitled to attend or vote at general meetings;
2. the Sterling Preference Share may be redeemed in whole on any date as may be determined by the Board; and
3. the exceptions to the circumstances in which a dividend will not be declared or paid do not apply.

A dividend of £0.04 per annum is payable on the Sterling Preference Share in issue at 4 March 2013. The dividend is paid at the rate of £0.01 per quarter at the sole and absolute discretion of the Board.

Euro Preference Shares

The Euro Preference Shares carry the same rights and obligations under the Articles of Association as the Dollar Preference Shares, save in respect of certain rights and obligations that attach to Euro Preference Shares which are to be determined by the Board prior to allotment of the relevant preference shares and the timing and payment of proceeds from the redemption of each class of share.

Share capital during 2012

The following events occurred during the year in relation to the ordinary share capital of HSBC Holdings:

Script dividends

Issued in lieu of	HSBC Holdings ordinary shares		Market value	
	In	Number	US\$	£
Third interim dividend for 2011	January 2012	96,994,187	7.4224	4.7461
Fourth interim dividend for 2011	May 2012	28,357,393	9.1170	5.7466
First interim dividend for 2012	July 2012	91,127,385	8.2065	5.2022
Second interim dividend for 2012	October 2012	87,820,228	8.9127	5.6560
Third interim dividend for 2012	December 2012	65,036,059	9.8255	6.1138

All-Employee share plans

	Number		Exercise price	
			from	to
HSBC Holdings savings-related share option plans				
HSBC ordinary shares issued in £	37,422,697	£	3.3116	6.1760
HSBC ordinary shares issued in HK\$	21,684,534	HK\$	37.8797	63.9864
HSBC ordinary shares issued in US\$	3,440,522	US\$	4.8876	8.7225
HSBC ordinary shares issued in €	1,407,390	€	3.6361	6.0657
Options over HSBC ordinary shares lapsed	21,626,648			
Options over HSBC ordinary shares granted in response to approximately 53,000 applications from HSBC employees in over 60 countries and territories on 24 April 2012	44,868,386			
Plan d'Epargne Entreprise				
HSBC ordinary shares issued for the benefit of non-UK resident employees of HSBC France and its subsidiaries	2,274,523	€	5.695	

Discretionary share incentive plans

	HSBC ordinary shares issued	Exercise price (£)	Options lapsed
Options exercised under:			
The HSBC Holdings Group Share Option Plan	1,606,032	6.0216	32,018,464

Authority to allot shares

At the Annual General Meeting in 2012, shareholders renewed the general authority for the Directors to allot new shares. The general authority is to allot up to 3,624,050,000 ordinary shares, 15,000,000 non-cumulative preference shares of £0.01 each, 15,000,000 non-cumulative preference shares of US\$0.01 each and 15,000,000 non-cumulative preference shares of €0.01 each. Within this, the Directors have authority to allot up to a maximum of 906,012,000 ordinary shares wholly for cash to persons other than existing shareholders.

Other than as described above, the Directors did not allot any shares during 2012.

Treasury shares

In accordance with the terms of a waiver granted by the Hong Kong Stock Exchange on 19 December 2005, HSBC Holdings will comply with the applicable law and regulation in the UK in relation to the holding of any shares in treasury and with the conditions of the waiver in connection with any shares it may hold in treasury. No shares are currently held in treasury.

Directors' interests

Pursuant to the requirements of the UK Listing Rules and according to the register of Directors' interests maintained by HSBC Holdings pursuant to section 352 of the Securities and Futures Ordinance of Hong Kong, the Directors of HSBC Holdings at 31 December 2012 had the following interests, all beneficial unless otherwise stated, in the shares and loan capital of HSBC Holdings and its associated corporations:

Directors' interests – shares and loan capital

	At 31 December 2012					
	At 1 January 2012	Beneficial owner	Child under 18 or spouse	Jointly with another person	Trustee	Total interests ¹
HSBC Holdings ordinary shares						
J D Coombe	21,139	22,387	–	–	–	22,387
R A Fairhead	21,300	–	–	21,300	–	21,300
D J Flint	272,861	313,326	–	–	37,162 ²	350,488
S T Gulliver	2,731,100	2,553,592	176,885	–	–	2,730,477
J W J Hughes-Hallett	46,952	–	–	–	–	–
W S H Laidlaw	31,872	32,252	–	–	1,416 ²	33,668
J P Lipsky ³	–	15,000	–	–	–	15,000
I J Mackay	133,648	118,813	–	–	–	118,813
Sir Simon Robertson	176,709	9,486	–	–	167,750 ²	177,236
J L Thornton ⁴	10,250	–	10,250	–	–	10,250
	US\$000	US\$000	US\$000	US\$000	US\$000	US\$000
HSBC Holdings 6.5% Subordinated Notes 2036						
L M L Cha	300	300	–	–	–	300
	RMBm	RMBm	RMBm	RMBm	RMBm	RMBm
HSBC Bank 2.875% Notes 2015						
J Faber ⁵	–	5.1	–	–	–	5.1

1 Details of executive Directors' other interests in HSBC Holdings ordinary shares arising from the HSBC Holdings savings-related share option plans, the HSBC Share Plan and the HSBC Share Plan 2011 are set out in the Directors' Remuneration Report on page 363. At 31 December 2012, the aggregate interests under the Securities and Futures Ordinance of Hong Kong in HSBC Holdings ordinary shares, including interests arising through employee share plans were: D J Flint – 566,423; S T Gulliver – 5,178,992 and I J Mackay – 536,205. Each Director's total interests represents less than 0.03% of the shares in issue.

2 Non-beneficial.

3 Interest in 3,000 listed American Depositary Shares ('ADS'), which are categorised as equity derivatives under Part XV of the Securities and Futures Ordinance of Hong Kong. Each ADS represents five HSBC Holdings ordinary shares.

4 Interest of spouse in 2,050 listed ADS.

5 Non-beneficial interest in renminbi (RMB) 1.2m 2.875% Notes 2015.

Report of the Directors: Corporate Governance (continued)

Appendix > Other required disclosures > Supplier payment policy / Dividends and shareholders

S T Gulliver ceased to have an interest as beneficial owner in one share of €5 in HSBC France (representing less than 0.01 per cent of the shares in issue), following his resignation as a director of that company on 22 November 2012. S T Gulliver had waived his rights to receive dividends on the share and had undertaken to transfer the share to HSBC on ceasing to be a director of HSBC France.

No Directors held any short position as defined in the Securities and Futures Ordinance of Hong Kong in the shares and loan capital of HSBC Holdings and its associated corporations. Save as stated above, none of the Directors had an interest in any shares or debentures of HSBC Holdings or any associated corporation at the beginning or at the end of the year, and none of the Directors or members of their immediate families were awarded or exercised any right to subscribe for any shares or debentures in any HSBC corporation during the year. Since the end of the year, the aggregate interests of the following Director has increased by the number of HSBC Holdings ordinary shares shown against his name:

HSBC Holdings ordinary shares

D J Flint (beneficial owner)	35 ¹
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1 The acquisition of shares in the HSBC Holdings UK Share Incentive Plan through regular monthly contributions.

Since the end of the year, the aggregate interests of the following Director have decreased by the number of debentures shown against his name.

HSBC Capital Funding (Euro 2) L.P. 5.3687% Preferred Securities 2014

R Fassbind (beneficial owner)	EUR000 500
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There have been no other changes in the share and loan capital interests of the Directors from 31 December 2012 to the date of this Report. Any subsequent changes up to the last practicable date before the publication of the *Notice of Annual General Meeting* will be set out in the notes to that Notice.

At 31 December 2012, non-executive Directors and senior management (being executive Directors and Group Managing Directors of HSBC Holdings) held, in aggregate, beneficial interests in 14,450,028 HSBC Holdings ordinary shares (0.08% of the issued ordinary shares).

At 31 December 2012, executive Directors and senior management held, in aggregate, options to subscribe for 357,509 of HSBC Holdings ordinary shares under the HSBC Holdings savings-related share option plans and HSBC Holdings Group Share Option Plan. These options are exercisable between 2012 and 2016 at prices ranging from £3.3116 to £7.2181 per ordinary share.

Supplier payment policy

HSBC has signed up to the Government's Prompt Payment Code (further information on, and copies of, the Code can be obtained by visiting www.promptpaymentcode.org.uk).

Our policy is to settle terms of payment with our suppliers when agreeing the terms of each transaction, to ensure that those suppliers are made aware of the terms of payment and to abide by the terms of payment.

The amount due to trade creditors at 31 December 2012 represented 39 days' average daily purchases of goods and services received from such creditors, calculated in accordance with the Companies Act 2006, as amended by Statutory Instrument 2008 No. 410. The average amount due to trade creditors during 2012 represented 28 days' average daily purchases of goods and services received from such creditors.

Dividends and shareholders

Dividends for 2012

First, second and third interim dividends for 2012, each of US\$0.09 per ordinary share, were paid on 5 July 2012, 4 October 2012 and 12 December 2012 respectively. Note 10 on the Financial Statements gives more information on the dividends declared in 2012. On 4 March 2013, the Directors declared a fourth interim dividend for 2012 of US\$0.18 per ordinary share in lieu of a final dividend, which will be payable on 8 May 2013 in cash in US dollars, or in sterling or Hong Kong dollars at exchange rates to be determined on 29 April 2013, with a scrip dividend alternative. As the fourth interim dividend for 2012 was declared after 31 December 2012 it has not been included

in the balance sheet of HSBC as a debt. The reserves available for distribution at 31 December 2012 were US\$38,175m.

A quarterly dividend of US\$15.50 per 6.20% non-cumulative US Dollar Preference Share, Series A ('Series A Dollar Preference Share'), (equivalent to a dividend of US\$0.3875 per Series A American Depositary Share, each of which represents one-fortieth of a Series A Dollar Preference Share), was paid on 15 March, 15 June, 17 September and 17 December 2012.

Dividends for 2013

The proposed timetable for interim dividends in respect of 2013 on the ordinary shares is set out in the Shareholder Information section on page 516.

Quarterly dividends of US\$15.50 per Series A Dollar Preference Share (equivalent to a dividend of US\$0.3875 per Series A American Depositary Share, each of which represents one-fortieth of a Series A Dollar Preference Share) and £0.01 per Series A Sterling Preference Share were declared on 7 February 2013 for payment on 15 March 2013.

Communication with shareholders

Communication with shareholders is given high priority. The Board has adopted a shareholder communication policy which is available on www.hsbc.com. Extensive information about our activities is provided to shareholders in the *Annual Report and Accounts*, the *Annual Review* and the *Interim Report* which are available on www.hsbc.com. There is regular dialogue with institutional investors and enquiries from individuals on matters relating to their shareholdings and our business are welcomed and are dealt with in an informative and timely manner. All shareholders are encouraged to attend the Annual General Meeting or the informal meeting of shareholders held in Hong Kong to discuss our progress. Shareholders may send enquiries to the Board in writing to the Group Company Secretary, HSBC Holdings plc, 8 Canada Square, London E14 5HQ or by sending an email to shareholderquestions@hsbc.com.

Shareholders may require the Directors to call a general meeting, other than an annual general meeting as provided by the UK Companies Act 2006. Requests to call a general meeting may be made by members representing at least 5% of the paid-up capital of the Company as carries the right of voting at general meetings of the Company (excluding any paid-up capital held as treasury shares). A request must state the general nature of the business to be dealt with at the meeting and may include the text of a resolution that may properly be moved and is intended to be moved at the meeting. A resolution may properly be moved at a meeting unless it would, if passed, be ineffective (whether by reason of inconsistency with any enactment or the Company's constitution or otherwise); it is defamatory of any person; or it is frivolous or vexatious. A request may be in hard copy form or in electronic form and must be authenticated by the person or persons making it. A request may be made in writing to the postal address referred to in the paragraph above or by sending an email to shareholderquestions@hsbc.com. At any meeting convened on such request no business shall be transacted except that stated by the requisition or proposed by the Board.

Notifiable interests in share capital

At 31 December 2012, we had received the following disclosures (which have not been subsequently changed) of major holdings of voting rights pursuant to the requirements of Rule 5 of the FSA Disclosure Rules and Transparency Rules:

- Legal & General Group Plc gave notice on 9 March 2010 that it had a direct interest on 8 March 2010 in 696,851,431 HSBC Holdings ordinary shares, representing 3.99% of the total voting rights at that date; and
- BlackRock, Inc. gave notice on 9 December 2009 that on 7 December 2009 it had the following: an indirect interest in HSBC Holdings ordinary shares of 1,142,439,457; qualifying financial instruments with 705,100 voting rights that may be acquired if the instruments are exercised or converted; and financial instruments with similar economic effect to qualifying financial instruments which refer to 234,880 voting rights, each representing 6.56%, 0.0041% and 0.0013% respectively, of the total voting rights at that date.

At 31 December 2012, according to the register maintained by HSBC Holdings pursuant to section 336 of the Securities and Futures Ordinance of Hong Kong:

- JPMorgan Chase & Co. gave notice on 7 November 2012 that on 30 October 2012 it had the following interests in HSBC Holdings ordinary shares: a long position of 1,261,592,952 shares; a short position of 71,252,702

Report of the Directors: Corporate Governance (continued)**Appendix – Other required disclosures > Dividends and shareholders // DRR**

shares; and a lending pool of 1,007,026,189 shares, each representing 6.85%, 0.39% and 5.47%, respectively, of the ordinary shares in issue at that date. Since 31 December 2012 and following interim notifications on 14, 17, 23 January and 13 February 2013, JPMorgan Chase & Co. gave notice on 15 February 2013 that on 12 February 2013 it had the following interests in HSBC Holdings ordinary shares: a long position of 1,294,366,810 shares; a short position of 64,591,997 shares; and a lending pool of 1,017,759,703 shares each representing 7.00%, 0.35% and 5.51% respectively, of the ordinary shares in issue at that date.

- BlackRock, Inc. gave notice on 10 November 2012 that on 7 November 2012 it had the following interests in HSBC Holdings ordinary shares: a long position of 1,103,721,816 shares and a short position of 35,922,568 shares, each representing 5.99% and 0.19%, respectively, of the ordinary shares in issue at that date. Since 31 December 2012 and following interim notifications on 3 and 4 January 2013, BlackRock, Inc. gave notice on 8 January 2013 that on 3 January 2013 it had the following interests in HSBC Holdings ordinary shares: a long position of 1,110,172,768 shares and a short position of 35,234,325 shares, each representing 6.00% and 0.19%, respectively, of the ordinary shares in issue at that date.

In compliance with the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited at least 25% of the total issued share capital has been held by the public at all times during 2012 and up to the date of this Report.

Dealings in HSBC Holdings shares

Except for dealings as intermediaries by HSBC Bank and The Hongkong and Shanghai Banking Corporation, which are members of a European Economic Area exchange, neither we nor any of our subsidiaries have purchased, sold or redeemed any of our listed securities during the year ended 31 December 2012.