

Standard Chartered Bank
(Hong Kong) Limited

Directors' Report and
Consolidated Financial
Statements

For the year ended
31 December 2011

Standard Chartered Bank (Hong Kong) Limited
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Report of the directors

The directors have pleasure in submitting their annual report together with the audited financial statements for the year ended 31 December 2011.

Principal place of business

Standard Chartered Bank (Hong Kong) Limited (the “Bank”) is a bank incorporated and domiciled in Hong Kong and has its registered office at 32/F, 4 – 4A Des Voeux Road Central, Hong Kong.

Principal activities

The Bank is a licensed bank registered under the Hong Kong Banking Ordinance. The Bank’s principal activities are the provision of banking and related financial services. The principal activities and other particulars of the Bank’s principal subsidiaries are set out in note 19 to the financial statements.

Financial statements

The profit of the Bank and its subsidiaries for the year ended 31 December 2011 and the state of the Bank’s and its subsidiaries’ affairs as at that date are set out in the financial statements on pages 5 to 126.

During the year ended 31 December 2011, the directors had declared and paid an ordinary dividend of HK\$3.0114 (2010: HK\$3.6085) per each “A” and “B” ordinary share totalling HK\$5,833 million (2010: HK\$6,990 million).

Details of the movements in reserves are set out in the consolidated statement of changes in equity.

Charitable donations

Charitable donations made by the Bank and its subsidiaries during the year amounted to HK\$10 million (2010: HK\$8 million).

Fixed assets

Details of the movements in fixed assets are set out in note 21 to the financial statements.

Share capital

There were no movements in the Bank’s share capital during the year.

Directors

The directors during the year and up to the date of this report are:

Executive directors

Benjamin Hung Pi Cheng

Saleem Razvi

Tan Siew Boi

Report of the directors (continued)

Non-executive directors

Katherine Tsang King Suen, Chairperson

Jaspal Singh Bindra

Julian Fong Loong Choon

Raymond Kwok Ping Luen*

Ma Xuezheng*

Norman Lyle*

Chan Wing Kin*

Olga Louise Zoutendijk (resigned on 30 June 2011)

Michael Thomas Pratt (resigned on 30 November 2011)

** Independent non-executive directors*

There being no provision in the Bank's Articles of Association for the retirement of directors by rotation, all the present directors continue in office for the ensuing year.

Directors' service contracts

The independent non-executive directors were appointed by the board of directors for a term of 2 years. Their remuneration is determined by the shareholders at the annual general meeting.

Directors' interests in Share Option Schemes

Certain directors of the Bank have been granted options under various share option schemes of Standard Chartered PLC, the ultimate holding company of the Bank. During the year, Jaspal Singh Bindra, Katherine Tsang King Suen, Benjamin Hung Pi Cheng, Julian Fong Loong Choon, Saleem Razvi, Tan Siew Boi and Michael Thomas Pratt were granted options under these schemes.

Directors' rights to acquire shares

At no time during the year was the Bank, any of its holding companies, subsidiaries, or fellow subsidiaries, a party to any other arrangement to enable the directors of the Bank to acquire benefits by means of the acquisition of shares in or debentures of the Bank or any other body corporate.

Directors' interests in contracts

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

Report of the directors (continued)

Auditor

The financial statements have been audited by KPMG who will retire and, being eligible, offer themselves for re-appointment. A resolution for the re-appointment of KPMG as the auditor of the Bank is to be proposed at the forthcoming annual general meeting.

On behalf of the Board

Katherine Tsang King Suen
Chairperson

Hong Kong, 29 February 2012

Independent auditor's report to the shareholders of Standard Chartered Bank (Hong Kong) Limited

(Incorporated in Hong Kong SAR with limited liability)

We have audited the consolidated financial statements of Standard Chartered Bank (Hong Kong) Limited (the "Bank") and its subsidiaries (together "the Bank and its subsidiaries") set out on pages 5 to 126, which comprise the consolidated and the bank balance sheets as at 31 December 2011, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated and the bank statements of changes in equity and the consolidated cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

The directors of the Bank are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board and with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the Hong Kong Companies Ordinance and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. This report is made solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Bank and its subsidiaries as at 31 December 2011 and of the Bank and its subsidiaries' profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

29 February 2012

Consolidated income statement

For the year ended 31 December 2011

(Expressed in millions of Hong Kong dollars)

	Note	2011 HK\$'M	Restated 2010 HK\$'M
Interest income	4(a)	15,200	11,730
Interest expense	4(b)	(3,477)	(1,923)
Net interest income		<u>11,723</u>	<u>9,807</u>
Fee and commission income		7,067	6,493
Fee and commission expense		(654)	(520)
Net fee and commission income	4(c)	6,413	5,973
Net trading income	4(d)	2,631	2,367
Net (losses)/gains from financial instruments designated at fair value through profit or loss	4(e)	(30)	39
Net gains from disposal of available-for-sale securities	5	307	156
Other operating income	4(f)	450	59
		<u>9,771</u>	<u>8,594</u>
Total operating income		21,494	18,401
Staff costs		(6,272)	(5,754)
Premises and equipment		(1,343)	(1,068)
Others		(3,753)	(4,187)
Operating expenses	4(g)	<u>(11,368)</u>	<u>(11,009)</u>
Operating profit before impairment		10,126	7,392
Impairment charges on advances to banks and customers	6(a)	(592)	(392)
Other impairment (charges)/releases	6(b)	(141)	12
Operating profit after impairment		9,393	7,012
Share of profit of associates		570	326
Profit before taxation		9,963	7,338
Taxation	7(a)	<u>(1,619)</u>	<u>(1,151)</u>
Profit after taxation		<u>8,344</u>	<u>6,187</u>
Attributable to:			
Equity shareholders of the Bank		8,324	6,145
Non-controlling interests		20	42
Profit after taxation		<u>8,344</u>	<u>6,187</u>

The notes on pages 13 to 126 form part of these financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2011

(Expressed in millions of Hong Kong dollars)

	2011 HK\$'M	Restated 2010 HK\$'M
Profit after taxation	8,344	6,187
Other comprehensive (losses)/income:		
Defined benefit plans:		
– Actuarial (losses)/gains	(399)	1
– Related tax effect	65	–
Available-for-sale securities:		
– Changes in fair value recognised during the year	(365)	188
– Changes in fair value transferred to the income statement on disposal	(307)	(156)
– Transfer to the income statement on fair value hedged items attributable to hedged risk	(421)	(204)
– Related tax effect	178	27
Cash flow hedges:		
– Changes in fair value recognised during the year	113	(63)
– Transfer to the income statement on termination of hedging derivatives	31	3
– Related tax effect	(24)	9
Net changes in share option equity reserve	10	294
Exchange difference	99	(16)
	<u>(1,020)</u>	<u>83</u>
Other comprehensive (losses)/income for the year, net of tax		
	<u>7,324</u>	<u>6,270</u>
Total comprehensive income for the year		
	<u><u>7,324</u></u>	<u><u>6,270</u></u>
Attributable to:		
Shareholders of the Bank	7,304	6,228
Non-controlling interests	20	42
	<u>7,324</u>	<u>6,270</u>

The notes on pages 13 to 126 form part of these financial statements.

Consolidated balance sheet as at 31 December 2011*(Expressed in millions of Hong Kong dollars)*

	Note	2011 HK\$'M	Restated 2010 HK\$'M
Assets			
Cash and balances with banks, central banks and other financial institutions	10	21,777	29,902
Placements with banks and other financial institutions	11(a)	136,513	97,167
Hong Kong SAR Government certificates of indebtedness	12	31,401	31,581
Trading assets	13	35,377	48,719
Financial assets designated at fair value	14	4,275	6,560
Investment securities	17	135,090	135,019
Advances to customers	15(a)	389,763	334,854
Amounts due from immediate holding company	18	50,957	33,665
Amounts due from fellow subsidiaries	18	17,531	20,660
Interest in associates	20	6,619	4,513
Fixed assets	21	10,522	3,103
Goodwill and intangible assets	22	1,741	1,721
Current tax assets		3	–
Deferred tax assets	28	319	350
Other assets	23	11,966	10,809
		<u>853,854</u>	<u>758,623</u>
Liabilities			
Hong Kong SAR currency notes in circulation	12	31,401	31,581
Deposits and balances of banks and other financial institutions		15,729	19,745
Deposits from customers	25	672,940	573,277
Trading liabilities	29	24,638	36,446
Financial liabilities designated at fair value	27	3,487	3,052
Debt securities in issue	26	13,265	–
Amounts due to immediate holding company	18	13,023	24,586
Amounts due to fellow subsidiaries	18	5,073	5,983
Current tax liabilities		917	360
Deferred tax liabilities	28	5	17
Other liabilities	30	19,775	16,480
Subordinated liabilities	32	13,100	8,055
		<u>813,353</u>	<u>719,582</u>
Equity			
Share capital	33	97	97
Reserves	34	40,346	38,875
Shareholders' equity		40,443	38,972
Non-controlling interests		58	69
		<u>40,501</u>	<u>39,041</u>
		<u>853,854</u>	<u>758,623</u>

Approved and authorised for issue by the Board of Directors on 29 February 2012.

Tsang King Suen Katherine
Chairperson

Hung Pi Cheng Benjamin
Director

Saleem Razvi
Director

Wang Wei Min
Company Secretary

The notes on pages 13 to 126 form part of these financial statements.

Balance sheet as at 31 December 2011*(Expressed in millions of Hong Kong dollars)*

	Note	2011 HK\$'M	Restated 2010 HK\$'M
Assets			
Cash and balances with banks, central banks and other financial institutions	10	21,676	29,892
Placements with banks and other financial institutions	11(a)	136,477	96,900
Hong Kong SAR Government certificates of indebtedness	12	31,401	31,581
Trading assets	13	35,377	48,719
Financial assets designated at fair value	14	4,275	6,560
Investment securities	17	133,263	133,500
Advances to customers	15(a)	377,477	325,591
Amounts due from immediate holding company	18	50,279	33,361
Amounts due from fellow subsidiaries	18	17,370	20,374
Amounts due from subsidiaries of the Bank	18	19,181	8,854
Investments in subsidiaries of the Bank	19	1,096	1,092
Interest in associates	20	4,814	3,362
Fixed assets	21	2,919	2,938
Goodwill and intangible assets	22	921	886
Deferred tax assets	28	275	312
Other assets	23	10,978	9,995
		<u>847,779</u>	<u>753,917</u>
Liabilities			
Hong Kong SAR currency notes in circulation	12	31,401	31,581
Deposits and balances of banks and other financial institutions		14,734	19,036
Deposits from customers	25	672,425	572,813
Trading liabilities	29	24,638	36,446
Financial liabilities designated at fair value	27	3,487	3,052
Debt securities in issue	26	13,265	–
Amounts due to immediate holding company	18	12,366	24,250
Amounts due to fellow subsidiaries	18	3,602	4,563
Amounts due to subsidiaries of the Bank	18	1,891	1,730
Current tax liabilities		762	182
Other liabilities	30	18,987	15,717
Subordinated liabilities	32	13,100	8,055
		<u>810,658</u>	<u>717,425</u>
Equity			
Share capital	33	97	97
Reserves	34	37,024	36,395
Shareholders' equity		<u>37,121</u>	<u>36,492</u>
		<u>847,779</u>	<u>753,917</u>

Approved and authorised for issue by the Board of Directors on 29 February 2012.

Tsang King Suen Katherine
Chairperson

Hung Pi Cheng Benjamin
Director

Saleem Razvi
Director

Wang Wei Min
Company Secretary

The notes on pages 13 to 126 form part of these financial statements.

Consolidated statement of changes in equity**For the year ended 31 December 2011***(Expressed in millions of Hong Kong dollars)*

	Attributable to equity shareholders of the Bank												Non-controlling interests	Total
	Share capital	Share premium	Capital redemption reserve	Cash flow hedge reserve	Available-for-sale investment reserve	Revaluation reserve	Pension reserve	Exchange reserve	Retained profits	Share option equity reserve	Merger reserve*	Total		
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
At 1 January 2010, as previously stated	97	12,477	3,804	(70)	190	146	(111)	166	22,345	-	645	39,689	27	39,716
Effect of change in accounting policy	-	-	-	-	-	-	-	-	108	-	-	108	-	108
Restated as at 1 January 2010	97	12,477	3,804	(70)	190	146	(111)	166	22,453	-	645	39,797	27	39,824
Total comprehensive income	-	-	-	(51)	(145)	-	1	(16)	6,145	294	-	6,228	42	6,270
Dividend paid	-	-	-	-	-	-	-	-	(6,990)	-	-	(6,990)	-	(6,990)
Cash distribution to a fellow subsidiary (Note)	-	-	-	-	-	-	-	-	(63)	-	-	(63)	-	(63)
Transfer to retained profits	-	-	-	-	-	-	-	-	645	-	(645)	-	-	-
At 31 December 2010	97	12,477	3,804	(121)	45	146	(110)	150	22,190	294	-	38,972	69	39,041
At 1 January 2011, as previously stated	97	12,477	3,804	(121)	45	146	(110)	150	22,122	294	-	38,904	69	38,973
Effect of change in accounting policy	-	-	-	-	-	-	-	-	68	-	-	68	-	68
Restated as at 1 January 2011	97	12,477	3,804	(121)	45	146	(110)	150	22,190	294	-	38,972	69	39,041
Total comprehensive income	-	-	-	120	(915)	-	(334)	99	8,324	10	-	7,304	20	7,324
Dividend paid	-	-	-	-	-	-	-	-	(5,833)	-	-	(5,833)	(31)	(5,864)
Transfer to retained profits	-	-	-	-	-	-	(15)	-	15	-	-	-	-	-
At 31 December 2011	97	12,477	3,804	(1)	(870)	146	(459)	249	24,696	304	-	40,443	58	40,501

* Merger reserve arising on the acquisition of Prime Credit Limited ("PCL"). On 1 July 2010, the Bank acquired 100 per cent of the share capital of PCL at a cost of HK\$204 million (Note 2)

Note: Dividends of HK\$63 million were paid by PCL to a fellow subsidiary of the Bank prior to the Bank's acquisition of PCL in July 2010.

The notes on pages 13 to 126 form part of these financial statements.

Statement of changes in equity For the year ended 31 December 2011

(Expressed in millions of Hong Kong dollars)

	Share capital HK\$'M	Share redemption premium HK\$'M	Capital reserve HK\$'M	Cash flow hedge reserve HK\$'M	Available- for-sale investment reserve HK\$'M	Pension reserve HK\$'M	Retained profits HK\$'M	Share option equity reserve HK\$'M	Total HK\$'M
At 1 January 2010, as previously stated	97	12,477	3,804	(56)	191	(143)	21,957	-	38,327
Effect of change in accounting policy	-	-	-	-	-	-	108	-	108
Restated as at 1 January 2010	97	12,477	3,804	(56)	191	(143)	22,065	-	38,435
Total comprehensive income	-	-	-	(59)	(140)	-	4,952	294	5,047
Dividend paid	-	-	-	-	-	-	(6,990)	-	(6,990)
At 31 December 2010	97	12,477	3,804	(115)	51	(143)	20,027	294	36,492
At 1 January 2011, as previously stated	97	12,477	3,804	(115)	51	(143)	19,959	294	36,424
Effect of change in accounting policy	-	-	-	-	-	-	68	-	68
Restated as at 1 January 2011	97	12,477	3,804	(115)	51	(143)	20,027	294	36,492
Total comprehensive income	-	-	-	114	(923)	(316)	7,624	(37)	6,462
Dividend paid	-	-	-	-	-	-	(5,833)	-	(5,833)
At 31 December 2011	97	12,477	3,804	(1)	(872)	(459)	21,818	257	37,121

During the year ended 31 December 2011, the directors had declared and paid an ordinary dividend of HK\$3.0114 (2010: HK\$3.6085) per each 'A' and 'B' ordinary share totalling HK\$5,833 million (2010: HK\$6,990 million).

The notes on pages 13 to 126 form part of these financial statements.

Consolidated cash flow statement

For the year ended 31 December 2011

(Expressed in millions of Hong Kong dollars)

	Note	2011 HK\$'M	Restated 2010 HK\$'M
Operating activities			
Profit before taxation		9,963	7,338
Adjustments for:			
Impairment charges on advances to banks and customers		592	392
Advances written off net of recoveries		(682)	(823)
Unwinding of discount on loan impairment charges		(23)	(25)
Other impairment charges/(releases)		141	(12)
Depreciation		315	189
Amortisation of intangible assets		93	93
Gains on disposal of fixed assets		(20)	(32)
Net (gains)/losses on revaluation of investment properties		(5)	51
Share of profit of associates		(570)	(326)
Interest expense on subordinated liabilities		410	198
Fair value losses transferred from reserves on cash flow hedges		31	3
Exchange translation on subordinated liabilities		(6)	(2)
		10,239	7,044
(Increase)/decrease in operating assets:			
Placements with banks and other financial institutions with original maturity beyond three months		(5,764)	13,464
Trading assets		9,695	601
Financial assets designated at fair value		2,285	(6,560)
Investment securities		(1,235)	9,222
Gross advances to customers		(54,446)	(98,344)
Amounts due from immediate holding company and fellow subsidiaries		(10,996)	52,052
Other assets		(3,239)	(3,211)
Increase/(decrease) in operating liabilities:			
Deposits and balances of banks and other financial institutions		(4,047)	(2,711)
Deposits from customers		99,668	48,104
Debt securities in issue		13,265	(1,063)
Financial liabilities designated at fair value		435	(4,514)
Amounts due to immediate holding company and fellow subsidiaries		(13,194)	19,397
Trading liabilities		(11,808)	7,410
Other liabilities		3,324	3,369
		34,182	44,260
Cash generated from operations		34,182	44,260
Income tax paid		(827)	(954)
		33,355	43,306
Net cash generated from operating activities		33,355	43,306

Consolidated cash flow statement (continued)**For the year ended 31 December 2011***(Expressed in millions of Hong Kong dollars)*

	Note	2011 HK\$'M	Restated 2010 HK\$'M
Investing activities			
Dividend received from associates		70	169
Payment for purchases of consumer finance businesses, net of cash and cash equivalents acquired		–	(5,574)
Acquisition of a subsidiary from a fellow subsidiary		–	(204)
Payment for additional investment in associates		(1,507)	(795)
Payment for purchase of fixed assets		(7,799)	(181)
Payment for purchase of intangible assets		(115)	(74)
Proceeds from disposal of fixed assets		90	48
Proceeds from disposal of intangible assets		2	31
		<u> </u>	<u> </u>
Net cash used in investing activities		(9,259)	(6,580)
		<u>-----</u>	<u>-----</u>
Financing activities			
Proceeds from issuance of subordinated liabilities		4,597	5,785
Interest paid on subordinated liabilities		(350)	(186)
Cash distribution to a fellow subsidiary		–	(63)
Dividend paid to shareholders of the Bank		(5,833)	(6,990)
Dividend paid to non-controlling interests		(31)	–
		<u> </u>	<u> </u>
Net cash used in financing activities		(1,617)	(1,454)
		<u>-----</u>	<u>-----</u>
Net increase in cash and cash equivalents		22,479	35,272
Cash and cash equivalents at 1 January		124,308	88,405
Effect of foreign exchange		1,738	631
		<u> </u>	<u> </u>
Cash and cash equivalents at 31 December	35	148,525	124,308
		<u>=====</u>	<u>=====</u>
Cash flows from operating activities include:			
Interest received		14,500	11,340
Interest paid		2,731	1,602
Dividends received		19	16
		<u> </u>	<u> </u>

The notes on pages 13 to 126 form part of these financial statements.

Notes to the financial statements

(Expressed in millions of Hong Kong dollars)

1 Principal activities

The principal activities of Standard Chartered Bank (Hong Kong) Limited (the “Bank”) and its subsidiaries (together referred to as the “Bank and its subsidiaries”) are the provision of banking and related financial services.

2 Significant accounting policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards (“HKFRSs”), which collective term includes all applicable Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (“HKASs”) and Interpretations issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. As HKFRSs are consistent with International Financial Reporting Standards (“IFRSs”), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards and Interpretations issued by the International Accounting Standards Board (“IASB”), these financial statements also comply with IFRSs.

(b) Basis of preparation of the financial statements

(i) Basis of Preparation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries made up to 31 December 2011.

The consolidated and the Bank’s financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment properties, available-for-sale assets, and financial assets and liabilities (including derivatives) at fair value through profit or loss.

The preparation of financial statements in conformity with adopted HKFRS/IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank and its subsidiaries’ accounting policies. Actual results may differ from these estimates. The significant judgements made by management in applying the accounting policies and key sources of uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended 31 December 2010.

Application of merger accounting

On 1 July 2010, the Bank acquired 100 per cent of the share capital of Prime Credit Limited (“PCL”), from a fellow subsidiary company at a cost of HK\$204 million.

As the Bank and PCL were under the common control of Standard Chartered PLC Group (the “Group”) before and after the above-mentioned acquisition, the Bank has applied Accounting Guideline No.5 – “Merger Accounting for Common Control Combinations” issued by the HKICPA in accounting for the acquisition of PCL in its consolidated financial statements. In accordance with the principles of merger accounting, the Bank and its subsidiaries’ consolidated financial statements have been presented as if the acquisition by the Bank had occurred from the date when PCL first came under the control of Standard Chartered PLC Group.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(b) Basis of preparation of the financial statements (continued)****(i) Basis of Preparation (continued)**

The net assets of PCL have been recognised using the carrying amounts in the consolidated financial statements of Standard Chartered PLC Group. Comparative amounts have been restated so that they are presented as if PCL had been combined at the previous balance sheet date.

The excess of carrying value over consideration at the time of acquisition was recognised as a merger reserve in equity. The effects of all transactions between the Bank and its subsidiaries and PCL, whether occurring before or after the combination, are eliminated in preparing the consolidated financial statements. The transaction costs for the acquisition were expensed in the consolidated income statement.

The accounting policies set out below have been applied consistently across the Bank and its subsidiaries and to all periods presented in these financial statements.

(ii) Consolidated Financial Statements

During the year, the Bank had subordinated debts in issue. These subordinated debts were issued under a note issuance programme which is listed on the Stock Exchange of Hong Kong. Consequently, the Bank is required to produce consolidated financial statements in accordance with HKAS 27/IAS 27 "Consolidated and Separate Financial Statements".

(c) Subsidiaries and non-controlling interests

Subsidiaries are entities controlled by the Bank and its subsidiaries. Control exists when the Bank and its subsidiaries have the power to directly or indirectly govern the financial and operating policies so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Non-controlling interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Bank, whether directly or indirectly through subsidiaries, and in respect of which the Bank and its subsidiaries have not agreed any additional terms with the holders of those interests which would result in the Bank and its subsidiaries as a whole having a contractual obligation in respect of those interests that meet the definition of a financial liability. Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity shareholders of the Bank. Non-controlling interests are presented on the face of the consolidated income statement and the consolidated statement of comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the Bank.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(c) Subsidiaries and non-controlling interests (continued)**

Where losses applicable to the non-controlling interest exceed its interest in the equity of a subsidiary, the excess, and any further losses applicable to the non-controlling interest, are charged against the Bank and its subsidiaries' interest except to the extent that the non-controlling interest has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Bank and its subsidiaries' are allocated all such profits until the non-controlling interest's share of losses previously absorbed by the Bank and its subsidiaries have been recovered.

In the Bank's balance sheet, its investments in subsidiaries are stated at cost less impairment losses, if any.

(d) Associates

Associates are entities in respect of which the Bank has significant influence, but not control, over the financial and operating policies and procedures. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements and are initially recognised at cost.

The Bank and its subsidiaries' share of its associates' post-acquisition profits or losses are recognised in the income statement, and the share of post-acquisition movements in reserves are recognised in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment in the consolidated balance sheet. When the Bank and its subsidiaries' share of losses in an associate is equal to or exceeds its interest in the associate, including any other unsecured receivables, the Bank and its subsidiaries do not recognise further losses, unless they have incurred obligations or made payments on behalf of the associate.

Unrealised gains and losses on transactions between the Bank and its associates are eliminated to the extent of the Bank and its subsidiaries' interest in the associates.

In the Bank's balance sheet, investment in associates are stated at cost less impairment losses and dividends from pre-acquisition profits received prior to 1 January 2009, if any.

(e) Intangible assets**(i) Goodwill**

Goodwill represents the excess of the cost of an acquisition over the fair value of the Bank and its subsidiaries' share of the net identifiable assets and contingent liabilities of the acquired subsidiary/ associate at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in "Goodwill and intangible assets". Goodwill on acquisitions of associates is included in "Interest in associates".

Goodwill included in "Goodwill and intangible assets" is tested annually for impairment and carried at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units for the purpose of impairment testing.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(e) Intangible assets (continued)****(ii) Acquired intangibles**

At the date of acquisition of a subsidiary or associate, intangible assets which are deemed separable and that arise from contractual or other legal rights are capitalised and included within the net identifiable assets acquired. These intangible assets are initially measured at fair value, which reflects market expectations of the probability that the future economic benefits embodied in the asset will flow to the entity, and are amortised on the basis of their expected useful lives (4 to 16 years). At each balance sheet date, these assets are assessed for indicators of impairment. In the event that an asset's carrying amount is determined to be greater than its recoverable amount, the asset is written down immediately.

(iii) Computer software

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Costs associated with the development of software are capitalised where it is probable that it will generate future economic benefits in excess of its cost. Computer software costs are amortised on the basis of expected useful life (3 to 5 years). Costs associated with maintaining computer software programmes are recognised as an expense as incurred.

(f) Investment properties

Investment properties are land and buildings which are owned either to earn rental income or for long term investments or for both. Investment properties are stated in the balance sheet at fair value. Any gains or losses arising from a change in fair value or from the disposal of an investment property is recognised in the income statement.

(g) Other property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and impairment, if any. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation on fixed assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

- Buildings, leasehold land and leasehold improvements, are depreciated over the shorter of their estimated useful lives, being 50 years from the date of completion, and the unexpired terms of the lease.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(g) Other property, plant and equipment (continued)**

- Equipment and motor vehicles, are depreciated over 3 to 15 years.
- Aircrafts and vessels, are depreciated over 25 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Gains and losses on disposals are included in the income statement.

(h) Leases

Where the Bank and its subsidiaries are the lessees

The leases entered into by the Bank and its subsidiaries are primarily operating leases. The total payments made under operating leases are charged to the income statement on a straight-line basis over the period of the leases.

Where the Bank and its subsidiaries are the lessors

When assets are leased to customers under finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return ignoring tax cash flows.

Assets leased to customers under operating leases are included within Fixed assets and depreciated over their estimated useful lives. Rental income on these leased assets is recognised in the income statement on a straight-line basis unless another systematic basis is more representative.

(i) Financial assets and liabilities (excluding derivatives)

Financial assets are classified into the following categories: financial assets held at fair value through profit or loss, loans and receivables, and available-for-sale financial assets. Financial liabilities are classified as either held at fair value through profit or loss, or at amortised cost. Management determines the classification of the financial assets and liabilities on initial recognition or, where appropriate, at the time of reclassification.

(i) Financial assets and liabilities held at fair value through profit or loss

This category has two sub-categories: financial assets and liabilities held for trading, and those designated at fair value through profit or loss at inception. A financial asset or liability is classified as trading if acquired principally for the purpose of selling or repurchasing in the short term or is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.

Financial assets and liabilities may be designated at fair value through profit or loss when:

- the designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities on a different basis, or

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(i) Financial assets and liabilities (excluding derivatives) (continued)***(i) Financial assets and liabilities held at fair value through profit or loss (continued)*

- a group of financial assets and/or liabilities is managed and its performance evaluated on a fair value basis, or
- assets or liabilities include embedded derivatives and such derivatives are not recognised separately.

(ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

(iii) Available-for-sale assets

Available-for-sale assets are those non-derivative financial assets intended to be held for an indefinite period of time, which may be sold in response to liquidity requirements or changes in interest rates, exchange rates or equity prices.

Initial recognition

Purchases and sales of financial assets and liabilities held at fair value through profit or loss or which are available-for-sale are initially recognised using trade date accounting (the date on which the Bank and its subsidiaries commit to purchase or sell the asset). Loans and receivables are recognised when cash is advanced to the borrowers. Other financial assets and financial liabilities are initially recognised on value date at fair value plus directly attributable transaction costs.

Subsequent measurement

Financial assets and liabilities held at fair value through profit or loss are subsequently carried at fair value, with gains and losses arising from changes in fair value taken directly to the income statement.

Available-for-sale financial assets are subsequently carried at fair value, with gains and losses arising from changes in fair value taken to a separate component of equity until the asset is sold, or is impaired, when the cumulative gain or loss is transferred to the income statement.

Loans and receivables are subsequently carried at amortised cost using the effective interest method.

The fair values of quoted financial assets or financial liabilities in active markets are based on current prices. If the market for a financial asset or financial liability is not active, and for unlisted securities, the Bank and its subsidiaries establish fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Reclassifications

Reclassifications of financial assets, other than as disclosed below, or of financial liabilities between measurement categories are not permitted following their initial recognition.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(i) Financial assets and liabilities (excluding derivatives) (continued)**

Held for trading non-derivative financial assets can only be transferred out of the held at fair value through profit or loss category in the following circumstances: (i) to the available-for-sale category, where, in rare circumstances, they are no longer held for the purpose of selling or repurchasing in the near term; or (ii) to the loans and receivables category, where they are no longer held for the purpose of selling or repurchasing in the near term and they would have met the definition of a loan and receivable on initial recognition and the Bank and its subsidiaries have the intent and ability to hold the assets for the foreseeable future or until maturity.

Financial assets can only be transferred out of the available-for-sale category to the loans and receivables category, where they would have met the definition of a loan and receivable on initial recognition and the Bank and its subsidiaries have the intent and ability to hold the assets for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. For financial assets reclassified out of the available-for-sale category into loans and receivables, any gain or loss on those assets recognised in shareholders' equity prior to the date of reclassification is amortised to the income statement over the remaining life of the financial asset, using the effective interest method.

Renegotiated loans

Loans and receivables with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank and its subsidiaries have made concessions that they would not otherwise consider. Renegotiated loans and receivables are subject to ongoing monitoring to determine whether they remain impaired or past due.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank and its subsidiaries have transferred substantially all risks and rewards of ownership. Financial liabilities are derecognised when they are extinguished, i.e. when the obligation is discharged, cancelled or expires.

(j) Derivative financial instruments and hedge accounting

Derivatives are categorised as trading unless they are designated as hedging instruments.

Derivative contracts are initially recognised at fair value on the date on which they are entered into and are subsequently re-measured at their fair value. Fair values are obtained from market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and option pricing models, as appropriate. All derivatives are carried as assets when their fair values are positive and as liabilities when their fair values are negative.

Certain derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(j) Derivative financial instruments and hedge accounting (continued)**

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Bank and its subsidiaries designate certain derivatives as either: (1) hedges of the fair value of recognised assets or liabilities, or commitments (fair value hedge); or, (2) hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

The Bank and its subsidiaries document, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Bank and its subsidiaries also document the assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(i) Fair value hedge

Changes in the fair value of derivatives that are designated and that qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity or derecognition.

(ii) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled to the income statement in the periods in which the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derivatives that do not qualify for hedge accounting

Certain derivative transactions do not qualify for hedge accounting. Changes in the fair value of any derivative transaction that does not qualify for hedge accounting are recognised immediately in the income statement.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(k) Impairment of financial assets**

The Bank and its subsidiaries assess at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The following factors are considered in assessing objective evidence of impairment:

- whether the counterparty is in default of principal or interest payments;
- a counterparty files for bankruptcy protection (or the local equivalent) where this would avoid or delay repayment of its obligation;
- the Bank and its subsidiaries file to have the counterparty declared bankrupt or files a similar order in respect of a credit obligation;
- the Bank and its subsidiaries consent to a restructuring of the obligation, resulting in a diminished financial obligation, demonstrated by a material forgiveness of debt or postponement of scheduled payments;
- the Bank and its subsidiaries sell a credit obligation at a material credit-related economic loss; or
- there is observable data indicating that there is a measurable decrease in the estimated future cash flows of a group of financial assets, although the decrease cannot yet be identified with specific individual financial assets.

Assets carried at amortised cost

The Bank and its subsidiaries first assess whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank and its subsidiaries determine that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Bank and its subsidiaries may measure impairment on the basis of an instrument's fair value using observable market price.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(k) Impairment of financial assets (continued)***Assets carried at amortised cost (continued)*

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable. For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

To the extent a loan is irrecoverable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

Available-for-sale assets

A significant or prolonged decline in the fair value of an equity security below its cost is considered in determining whether the equity security is impaired. Where objective evidence of impairment exists for available-for-sale financial assets, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss) is removed from equity and recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

(l) Offsetting financial transactions

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

(m) Fiduciary activities

The Bank and its subsidiaries commonly act as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. The assets and income arising thereon are excluded from these financial statements, as they are not assets of the Bank and its subsidiaries.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(n) Cash and cash equivalents**

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and balances with banks, central banks and other financial institutions, trading assets, placements with banks and other financial institutions, and amounts due from immediate holding company and fellow subsidiaries.

(o) Revenue recognition**(i) Interest income and expense**

Interest income and expense on available-for-sale assets, financial assets or liabilities held at amortised cost and financial assets and liabilities held at fair value through profit or loss excluding derivatives is recognised in the income statement using the effective interest rate method.

The effective interest rate method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank and its subsidiaries estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all amounts paid or received between parties to the contract that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised at the original effective interest rate of the financial asset applied to the impaired carrying amount.

(ii) Fees and commissions

Fees and commissions are generally recognised on an accrual basis when the service has been provided or significant act performed. Loan syndication fees are recognised as revenue when the syndication has been completed and the Bank and its subsidiaries have retained no part of the loan package for itself or has retained a part at the same effective interest rate as for the other participants. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis.

(iii) Other income from financial assets and liabilities

Gains and losses arising from changes in the fair value of financial assets and liabilities held at fair value through profit or loss, as well as any interest receivable or payable, are included in the income statement in the period in which they arise.

Gains and losses arising from changes in the fair value of available-for-sale financial assets other than foreign exchange gains and losses from monetary items, are recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in the income statement.

Dividends on equity instruments are recognised in the income statement when the Bank and its subsidiaries' right to receive payment is established.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(p) Income tax**

Income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and that are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Current and deferred tax relating to items which are charged or credited directly to equity, are credited or charged directly to equity and are subsequently recognised in the income statement together with the current or deferred gain or loss.

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if the Bank and its subsidiaries have a legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Bank or its subsidiaries intend either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or
- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities for which a legal right of set off exists.

(q) Provisions

Provisions for restructuring costs and legal claims are recognised when the Bank and its subsidiaries have a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

(r) Employee benefits**(i) Short term employee benefits**

Salaries, annual bonuses, and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees.

(ii) Pension obligations

The Bank and its subsidiaries operate a number of defined contribution and defined benefit plans.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(r) Employee benefits (continued)****(ii) Pension obligations (continued)**

For defined contribution plans, the Bank and its subsidiaries pay contributions to publicly or privately administered pension insurance plans on a mandatory, contractual or voluntary basis, and such amounts are charged to operating expenses. The Bank and its subsidiaries have no further payment obligations once the contributions have been paid.

For funded defined benefit plans, the net liability recognised in the balance sheet represents the present value of the defined benefit obligations at the balance sheet date less the fair value of plan assets. The defined benefit obligations are calculated annually by independent actuaries using the projected unit method. The present value of the defined benefit obligations is determined by discounting the estimated future cash outflows using an interest rate equal to the yield on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have a term to maturity approximating to the term of the related pension liability.

Actuarial gains and losses that arise are recognised in shareholders' equity and presented in the consolidated statement of other comprehensive income in the period they arise. Past service costs are recognised immediately to the extent that benefits are vested and are otherwise recognised over the average period until benefits are vested on a straight-line basis. Current service costs and any past service costs, together with the unwinding of the discount on plan liabilities, offset by the expected return on plan assets where applicable, are charged to operating expenses.

(iii) Share-based compensation

The Group operates equity-settled share-based compensation plans in which the Bank and its subsidiaries' employees participate. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. For deferred share awards granted as part of an annual performance award, the expense is recognised over the performance period together with the vesting period. For all other awards the expense is recognised over the vesting period.

For equity-settled awards, the total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and growth targets). The fair value of equity instruments granted is based on market prices, if available, at the date of grant. In the absence of market prices, the fair value of the instruments is estimated using an appropriate valuation technique, such as a binomial option pricing model.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the Bank and its subsidiaries revise its estimates of the number of options that are expected to vest. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period. Forfeitures prior to vesting attributable to factors other than the failure to satisfy a non-market vesting condition are treated as a cancellation and the remaining unamortised charge is debited to the income statement at the time of cancellation.

(s) Translation of foreign currencies

Foreign currency transactions are translated into Hong Kong dollars using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions, and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies, are recognised in the income statement.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

2 Significant accounting policies (continued)**(s) Translation of foreign currencies (continued)**

Non-monetary assets and liabilities are translated at historical exchange rates if held at historical cost or year-end exchange rates if held at fair value, and the resulting foreign exchange gains and losses are recognised in either the income statement or shareholders' equity depending on the treatment of the gain or loss on the asset or liability.

The results and financial position of all foreign operations that have a functional currency different from the Bank's presentation currency are accounted for as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the balance sheet date.
- income and expenses for each income statement are translated at average exchange rates or at rates on the date of the transaction where exchange rates fluctuate significantly; and
- all resulting exchange differences are recognised as a separate component of equity.

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

(t) Related parties

For the purposes of these financial statements, parties are considered to be related to the Bank and its subsidiaries if the Bank and its subsidiaries have the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Bank and its subsidiaries and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include (i) associates and joint ventures of the Group, (ii) entities which are under the significant influence of related parties of the Bank where those parties are individuals, and (iii) post-employment benefit plans which are for the benefit of employees of the Bank or of any entity that is a related party of the Bank.

(u) Segment reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the Bank and its subsidiaries' most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Bank and its subsidiaries' various lines of business and geographical locations.

(v) Sale and repurchase agreements

Where securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to re-sell ('reverse repos') are not recognised on the balance sheet and the consideration paid is recorded in 'Advances to customers' or 'Placements with banks and other financial institutions' as appropriate. The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

3 Changes in accounting policies

(a) Amendments to HKFRSs/IFRSs and new Interpretations

The HKICPA/IASB has issued a number of amendments to HKFRSs/IFRSs and one new Interpretation that are first effective for the current accounting period commencing 1 January 2011 or are available for early adoption.

New accounting standards adopted

On 1 January 2011, the Bank and its subsidiaries adopted retrospectively HKAS 24 (revised)/IAS 24 (revised) 'Related Parties'. HKAS 24 (revised)/IAS 24 (revised) widens the scope of the definition of related parties to include an investor, its subsidiaries and associates as related parties to each other. These changes do not have a material impact on the Bank and its subsidiaries' financial statements.

On 1 January 2011, the Bank and its subsidiaries adopted improvements to HKFRS (2010)/IFRS (2010), a collection of amendments to a number of HKFRSs/IFRSs. The amendments to HKFRS 7/IFRS 7, HKAS 1/IAS 1, HKAS 34/IAS 34 and HKFRIC 13/IFRIC 13 were applied on a retrospective basis and amendments to HKFRS 3/IFRS 3 were applied on a prospective basis. The amendments to HKFRS 7/IFRS 7 require the Bank and its subsidiaries to quantify the value of collateral held against assets on the balance sheet of Bank and its subsidiaries, and clarifies that disclosures relating to the maximum exposure to credit risk are required only for those financial instruments where the carrying value and maximum exposure to credit risk are different and removes the disclosure requirements for the carrying amount of renegotiated loans. Note 38(a) provides credit risk related disclosures required by HKFRS 7/IFRS 7. None of the other amendments had a material impact on the Bank and its subsidiaries' financial statements.

(b) Investment properties

In prior years, investment properties were depreciated over their estimated useful lives on a straight-line basis. With effect from 1 January 2011, the Bank and its subsidiaries have changed their accounting policy for investment properties from a cost model to a fair value model. Under the new policy, investment properties are initially measured at cost, including transaction costs. Subsequently investment properties are stated at fair value with any gains or losses in fair value reported in the income statement as they arise. The change in accounting policy has been applied retrospectively with comparative amounts restated.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***3 Changes in accounting policies (continued)***(b) Investment properties (continued)*

The effect of the change in accounting policy for investment properties at 31 December 2009 is not shown in a separate column in the primary financial statements in view of its immaterial impact on the balance sheet as a whole. The affected primary statement lines are presented together as follows:-

Consolidated

	<i>As previously reported</i> HK\$'M	<i>Adjustments</i> HK\$'M	<i>Restated</i> HK\$'M
Year ended 31 December 2010			
Profit after taxation	6,227	(40)	6,187
Total comprehensive income	6,310	(40)	6,270
As at 31 December 2010			
Fixed assets	3,035	68	3,103
Reserves	38,807	68	38,875
As at 31 December 2009			
Fixed assets	2,938	108	3,046
Reserves	39,592	108	39,700

Bank

	<i>As previously reported</i> HK\$'M	<i>Adjustments</i> HK\$'M	<i>Restated</i> HK\$'M
As at 31 December 2010			
Fixed assets	2,870	68	2,938
Reserves	36,327	68	36,395
As at 31 December 2009			
Fixed assets	2,852	108	2,960
Reserves	38,230	108	38,338

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***4 Operating profit**

The operating profit for the year is stated after taking into account the following:

	2011 HK\$'M	2010 HK\$'M
(a) Interest income		
Interest income on listed securities	457	330
Interest income on unlisted securities	2,501	2,242
Other interest income	12,242	9,158
	<u>15,200</u>	<u>11,730</u>
Amount shown in the income statement	15,200	11,730
Less: interest income arising from trading assets	(194)	(333)
Less: interest income on financial assets designated at fair value	(166)	(22)
	<u>14,840</u>	<u>11,375</u>
Total interest income on financial assets that are not measured at fair value through profit or loss	<u>14,840</u>	<u>11,375</u>

Other interest income includes interest income on unwinding of discounts on loan impairment charges of HK\$23 million (note 16) (2010: HK\$25 million), and fair value losses of HK\$31 million transferred from reserves on cash flow hedges (2010: fair value losses of HK\$3 million).

	2011 HK\$'M	Restated 2010 HK\$'M
(b) Interest expense		
Interest expense on customer deposits, deposits of banks, certificates of deposit issued, debt securities issued, trading liabilities and financial liabilities designated at fair value	3,067	1,725
Interest expense on subordinated liabilities	410	198
	<u>3,477</u>	<u>1,923</u>
Amount shown in the income statement	3,477	1,923
Less: interest expense arising from trading liabilities	(14)	(190)
Less: interest expense arising from financial liabilities designated at fair value	(7)	(32)
	<u>3,456</u>	<u>1,701</u>
Total interest expense on financial liabilities that are not measured at fair value through profit or loss	<u>3,456</u>	<u>1,701</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***4 Operating profit (continued)**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
(c) Net fee and commission income		
Net fee and commission income (other than amounts included in determining the effective interest rate arising from financial assets or financial liabilities that are not held for trading or designated at fair value		
– fee and commission income	2,866	2,804
– fee and commission expense	285	221
	<u>2,866</u>	<u>2,804</u>
Net fee and commission income from trust and other fiduciary activities where the Bank and its subsidiaries hold or invest assets on behalf of its customers		
– fee and commission income	471	444
– fee and commission expense	128	101
	<u>471</u>	<u>444</u>
	<i>2011</i> <i>HK\$'M</i>	<i>Restated</i> <i>2010</i> <i>HK\$'M</i>
(d) Net trading income		
Gains less losses from dealing in foreign currencies	2,293	2,031
Gains less losses from trading securities	147	126
Gains less losses from other dealing activities	191	210
	<u>2,293</u>	<u>2,031</u>
Amount shown in the income statement	2,631	2,367
Add: interest income arising from trading assets	194	333
Less: interest expense arising from trading liabilities	(14)	(190)
	<u>194</u>	<u>333</u>
	<u>(14)</u>	<u>(190)</u>
Net income from trading instruments	<u>2,811</u>	<u>2,510</u>
	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
(e) Net (losses)/gains from financial instruments designated at fair value		
Net (losses)/gains as shown in the income statement	(30)	39
Add: interest income arising from financial assets designated at fair value	166	22
Less: interest expense arising from financial liabilities designated at fair value	(7)	(32)
	<u>(30)</u>	<u>39</u>
	<u>166</u>	<u>22</u>
	<u>(7)</u>	<u>(32)</u>
	<u>129</u>	<u>29</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***4 Operating profit (continued)**

	2011 HK\$'M	Restated 2010 HK\$'M
(f) Other operating income		
Rental income from operating lease assets	229	–
Dividend income from listed available-for-sale securities	1	1
Dividend income from unlisted available-for-sale securities	18	15
Gains on disposal of fixed assets	20	32
Net gains/(losses) on disposal of financial instruments measured at amortised cost	109	(9)
Net gains/(losses) on revaluation of investment properties	5	(51)
Others	68	71
	<u>450</u>	<u>59</u>

	2011 HK\$'M	Restated 2010 HK\$'M
(g) Operating expenses		
Staff costs		
– contributions to defined contribution plans	166	140
– expense in respect of the defined benefits plans (note 31(d))	24	26
– equity-settled share-based payment expenses	501	400
– salaries and other staff costs	5,581	5,188
Depreciation (note 21)	315	189
Premises and equipment expense, excluding depreciation		
– rental of premises	680	605
– others	348	274
Amortisation		
– other intangible assets (note 22)	93	93
Auditor's remuneration	13	12
Others	3,647	4,082
	<u>11,368</u>	<u>11,009</u>

5 Net gains from disposal of available-for-sale securities

	2011 HK\$'M	2010 HK\$'M
Net gains transferred from reserves	<u>307</u>	<u>156</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***6 Impairment charges**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
(a) Impairment charges on advances to banks and customers		
Individual impairment provisions (note 16)		
– additions	803	762
– releases	(81)	(99)
– recoveries	(211)	(241)
	<u>511</u>	<u>422</u>
Portfolio impairment charges/(releases) (note 16)	<u>81</u>	<u>(30)</u>
	<u>592</u>	<u>392</u>
(b) Other impairment charges/(releases)		
Releases for contingent liabilities	(7)	(9)
Charges/(releases) relating to debt securities classified as loans and receivables	148	(3)
	<u>141</u>	<u>(12)</u>

7 Taxation in the consolidated income statement**(a) Taxation in the consolidated income statement represents:**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
<i>Current tax</i>		
Hong Kong profits tax	1,321	881
Overseas taxation	102	96
(Over)/under-provision in respect of prior years	(39)	6
	<u>1,384</u>	<u>983</u>
<i>Deferred tax (note 28)</i>		
Origination/reversal of temporary differences	190	197
Under/(over)-provision in respect of prior years	45	(29)
	<u>235</u>	<u>168</u>
	<u>1,619</u>	<u>1,151</u>

The provision for Hong Kong profits tax for 2011 is calculated at 16.5% (2010: 16.5%) of the estimated assessable profits for the year. Taxation for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***7 Taxation in the consolidated income statement (continued)****(b) Reconciliation between tax expenses and accounting profit at applicable tax rates:**

	2011 HK\$'M	<i>Restated</i> 2010 HK\$'M
Profit before taxation	9,963	7,338
Notional tax on profit before taxation, calculated at Hong Kong profits tax rate of 16.5%	1,644	1,211
Tax effect of non-deductible expenses	86	49
Tax effect of non-taxable revenue	(154)	(121)
Under/(over)-provision in prior years	6	(23)
Tax effect of different tax rates of subsidiaries operating in other jurisdictions	32	44
Others	5	(9)
Actual tax expense	1,619	1,151

8 Directors' remuneration

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	<i>Bank</i>	
	2011 HK\$'M	2010 HK\$'M
Fees	1	2
Salaries and other emoluments	44	38
	45	40

9 Segmental reporting

The Bank and its subsidiaries manage its businesses using two main business segments:

- Consumer Banking which provides financial services to customers including lending and deposit taking activities, credit card facilities and investment services; and
- Wholesale Banking which provides financial services to corporations and institutions, including lending and deposit taking activities, structured finance products, syndicated loans, cash management, investment advice, distributing fixed income and equity investments, brokerage services, interbank and capital market activities and proprietary trading.

In addition, certain items which do not fall within the two main business segments, including unallocated central costs and share of profits/(losses) of certain associates are reported in "Other Banking". Financial information is presented internally to the Bank's senior management using these three business segments.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***9 Segmental reporting (continued)**

The Bank and its subsidiaries comprise only one geographical segment as over 90% of the business is based in Hong Kong. Geographical segment is classified by the location of the principal operations of the subsidiary or, in the case of the Bank, the location of the branch responsible for reporting the results or advancing the funds.

(a) Segment results, assets and liabilities

Revenue and expenses are allocated to the reportable segments with reference to income generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

	Consumer banking		Wholesale banking		Other banking		Inter-segment eliminations		Consolidated Total	
	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M
Operating income										
– Net interest income	5,961	5,168	6,038	4,640	(76)	(90)			11,923	9,718
– Other operating income	4,227	3,520	7,071	5,975	(17)	–			11,281	9,495
	10,188	8,688	13,109	10,615	(93)	(90)			23,204	19,213
Operating expenses	(5,442)	(5,524)	(5,502)	(4,912)	53	(60)			(10,891)	(10,496)
Operating profit before impairment	4,746	3,164	7,607	5,703	(40)	(150)			12,313	8,717
Impairment charges	(552)	(352)	(250)	25	(1)	5			(803)	(322)
Profit before taxation	4,194	2,812	7,357	5,728	(41)	(145)			11,510	8,395
Total assets	217,638	206,195	621,646	565,612	85,107	50,997	(42,112)	(39,160)	882,279	783,644
Segment liabilities	323,749	301,946	497,985	460,027	62,473	22,015	(42,112)	(39,160)	842,095	744,828

(b) Reconciliation of reportable segment revenues, profit before taxation, assets and liabilities**Revenue**

	Consolidated	
	2011 HK\$'M	Restated 2010 HK\$'M
Reportable segment revenue	23,204	19,213
Income relating to Financial Market products	(1,025)	(1,009)
Cost of free funds	203	206
Others	(888)	(9)
Total operating income	21,494	18,401

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***9 Segmental reporting (continued)****(b) Reconciliation of reportable segment revenues, profit before taxation, assets and liabilities (continued)**

	<i>Consolidated</i>	
	<i>2011</i>	<i>Restated 2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Profit before taxation		
Reportable segment profit before taxation	11,510	8,395
Income relating to Financial Market products	(1,025)	(1,009)
Cost of free funds	203	206
Reallocations of impairment charges	(55)	–
Others	(670)	(254)
	<u>9,963</u>	<u>7,338</u>

	<i>Consolidated</i>	
	<i>2011</i>	<i>Restated 2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Assets		
Reportable segment assets	882,279	783,644
Assets of subsidiaries not included in consolidated total assets	(3,264)	(2,186)
Others	(25,161)	(22,835)
	<u>853,854</u>	<u>758,623</u>

	<i>Consolidated</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Liabilities		
Reportable segment liabilities	842,095	744,828
Liabilities of subsidiaries not included in consolidated total liabilities	(2,701)	(2,335)
Others	(26,041)	(22,911)
	<u>813,353</u>	<u>719,582</u>

Income and profit before taxation recognised in the consolidated financial statements represent an arm's length compensation for the services provided and risks borne. For internal management reporting purposes, income and profit before taxation are allocated on a global perspective. In addition, for internal management reporting purposes, a charge is allocated to reportable segments for the use of interest-free funds.

Reportable segment assets and liabilities include assets and liabilities which are not booked on the Bank and its subsidiaries' balance sheets but which contribute to the reportable segment's income and profit before taxation.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***10 Cash and balances with banks, central banks and other financial institutions**

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Cash in hand	1,737	1,307	1,714	1,297
Balances with central banks	9,036	12,879	9,036	12,879
Balances with banks and other financial institutions	11,004	15,716	10,926	15,716
	<u>21,777</u>	<u>29,902</u>	<u>21,676</u>	<u>29,892</u>

11 Placements with banks and other financial institutions**(a) Placements with banks and other financial institutions**

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross placements with banks and other financial institutions				
– maturing within one month	53,814	58,671	53,778	58,404
– maturing between one month to one year	81,198	38,285	81,198	38,285
– maturing between one year to five years	1,504	213	1,504	213
	<u>136,516</u>	<u>97,169</u>	<u>136,480</u>	<u>96,902</u>
Less: impairment charges individually assessed (note 16(b))	<u>(3)</u>	<u>(2)</u>	<u>(3)</u>	<u>(2)</u>
	<u>136,513</u>	<u>97,167</u>	<u>136,477</u>	<u>96,900</u>
Of which:				
Balances under collateralised reverse repurchase agreements	<u>10,771</u>	<u>29,941</u>	<u>10,771</u>	<u>29,941</u>

(b) Impaired placements with banks and other financial institutions

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross impaired advances to banks	64	65
Impairment charges – individually assessed	<u>(3)</u>	<u>(2)</u>
	<u>61</u>	<u>63</u>
Gross impaired advances to banks as a % of gross advances to banks	<u>0.05%</u>	<u>0.07%</u>

There is no collateral held against impaired advances to banks.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***12 Hong Kong SAR Government certificates of indebtedness and currency notes in circulation**

The Hong Kong Special Administrative Region currency notes in circulation are secured by the deposit of funds in respect of which the Government of Hong Kong Special Administrative Region certificates of indebtedness are held.

13 Trading assets

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Trading securities	34,381	46,451
Placements with banks and other financial institutions	21	333
Advances to customers	185	1,155
Positive fair values of trading derivatives	790	780
	<u>35,377</u>	<u>48,719</u>
Trading securities:		
Treasury bills (including Exchange Fund Bills)	13,738	25,165
Certificates of deposit held	2,120	368
Debt securities	18,513	20,918
Equity securities	10	–
	<u>34,381</u>	<u>46,451</u>
Issued by:		
Central governments and central banks	30,360	44,969
Public sector entities	71	13
Banks and other financial institutions	2,956	1,090
Corporate entities	994	379
	<u>34,381</u>	<u>46,451</u>
By place of listing:		
Listed in Hong Kong	13,827	13,692
Listed outside Hong Kong	2,999	5,945
	<u>16,826</u>	<u>19,637</u>
Unlisted	17,555	26,814
	<u>34,381</u>	<u>46,451</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***14 Financial assets designated at fair value**

	<i>Consolidated and Bank</i>	
	<i>Restated</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Debt securities	4,275	6,560
Issued by:		
Banks and other financial institutions	–	158
Corporate entities	4,275	6,402
	<u>4,275</u>	<u>6,560</u>
Analysed by place of listing:		
Listed outside Hong Kong	3,216	5,172
Unlisted	1,059	1,388
	<u>4,275</u>	<u>6,560</u>

The above financial assets designated at fair value represent certain debt securities with embedded derivatives that are not separately recognised.

15 Advances to customers**(a) Advances to customers****Consolidated**

	<i>2011</i>	<i>Restated</i>
	<i>2010</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Gross advances to customers	379,110	326,872
Trade bills	11,787	9,230
	<u>390,897</u>	<u>336,102</u>
Less : Impairment charges		
– individually assessed (note 16(a))	(580)	(775)
– collectively assessed (note 16(a))	(554)	(473)
	<u>389,763</u>	<u>334,854</u>
Of which:		
Balances under collateralised reverse repurchase agreements	<u>2,327</u>	<u>6,728</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***15 Advances to customers (continued)****(a) Advances to customers (continued)****Bank**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
Gross advances to customers	366,712	317,509
Trade bills	11,787	9,230
	<u>378,499</u>	<u>326,739</u>
Less : Impairment charges		
– individually assessed (note 16(a))	(578)	(774)
– collectively assessed (note 16(a))	(444)	(374)
	<u>377,477</u>	<u>325,591</u>
Of which:		
Balances under collateralised reverse repurchase agreements	<u>2,327</u>	<u>6,728</u>

(b) Impaired advances to customers**Consolidated**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
Gross impaired advances to customers	971	1,152
Impairment charges – individually assessed	(580)	(775)
	<u>391</u>	<u>377</u>
Gross impaired advances to customers as a % of gross advances to customers	<u>0.25%</u>	<u>0.34%</u>
Fair value of collateral held against the covered portion of impaired advances to customers	<u>577</u>	<u>185</u>
Covered portion of impaired advances to customers	249	116
Uncovered portion of impaired advances to customers	<u>722</u>	<u>1,036</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***15 Advances to customers (continued)****(b) Impaired advances to customers (continued)****Bank**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
Gross impaired advances to customers	962	1,088
Impairment charges – individually assessed	(578)	(774)
	<u>384</u>	<u>314</u>
Gross impaired advances to customers as a % of gross advances to customers	<u>0.25%</u>	<u>0.33%</u>
Fair value of collateral held against the covered portion of impaired advances to customers	<u>577</u>	<u>157</u>
Covered portion of impaired advances to customers	249	105
Uncovered portion of impaired advances to customers	<u>713</u>	<u>983</u>

The covered portion of impaired advances to customers represents the amount of collateral held against outstanding balances. It does not include any collateral held over and above outstanding exposures.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***15 Advances to customers (continued)****(c) Net investment in finance leases**

Advances to customers include the net investment in equipment leased to customers under finance leases. The total minimum lease payments receivable under finance leases and their present values at the year end, are as follows:

Consolidated

	2011			2010		
	<i>Present value of the minimum lease payments receivable</i>	<i>Interest income relating to future periods</i>	<i>Total minimum lease payments</i>	<i>Present value of the minimum lease payments receivable</i>	<i>Interest income relating to future periods</i>	<i>Total minimum lease payments</i>
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Within 1 year	58	2	60	164	9	173
After 1 year but within 5 years	12	1	13	90	3	93
After 5 years	1	–	1	4	1	5
	<u>71</u>	<u>3</u>	<u>74</u>	<u>258</u>	<u>13</u>	<u>271</u>
Impairment charges:						
– individually assessed	–			–		
Net investment in finance leases	<u>71</u>			<u>258</u>		

Bank

	2011			2010		
	<i>Present value of the minimum lease payments receivable</i>	<i>Interest income relating to future periods</i>	<i>Total minimum lease payments</i>	<i>Present value of the minimum lease payments receivable</i>	<i>Interest income relating to future periods</i>	<i>Total minimum lease payments</i>
	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M	HK\$'M
Within 1 year	1	–	1	4	–	4
After 1 year but within 5 years	–	–	–	1	–	1
After 5 years	–	–	–	–	–	–
	<u>1</u>	<u>–</u>	<u>1</u>	<u>5</u>	<u>–</u>	<u>5</u>
Impairment charges:						
– individually assessed	–			–		
Net investment in finance leases	<u>1</u>			<u>5</u>		

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***16 Movement in impairment charges on advances to banks and customers****(a) Advances to customers****Consolidated**

	2011		Total HK\$'M
	<i>Individually assessed HK\$'M</i>	<i>Collectively assessed HK\$'M</i>	
At 1 January 2011	775	473	1,248
Amounts written off	(893)	–	(893)
Recoveries of advances written off in previous years	211	–	211
Net charge to the income statement (note 6(a))	508	81	589
Unwind of discount on loan impairment charges (note 4(a))	(21)	–	(21)
	<u>580</u>	<u>554</u>	<u>1,134</u>
At 31 December 2011 (note 15(a))	<u>580</u>	<u>554</u>	<u>1,134</u>
		2010	
	<i>Individually assessed HK\$'M</i>	<i>Collectively assessed HK\$'M</i>	Total HK\$'M
At 1 January 2010	1,203	503	1,706
Amounts written off	(1,064)	–	(1,064)
Recoveries of advances written off in previous years	241	–	241
Net charge/(release) to the income statement (note 6(a))	419	(30)	389
Unwind of discount on loan impairment charges (note 4(a))	(24)	–	(24)
	<u>775</u>	<u>473</u>	<u>1,248</u>
At 31 December 2010 (note 15(a))	<u>775</u>	<u>473</u>	<u>1,248</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***16 Movement in impairment charges on advances to banks and customers (continued)****(a) Advances to customers (continued)****Bank**

	2011		Total HK\$'M
	Individually assessed HK\$'M	Collectively assessed HK\$'M	
At 1 January 2011	774	374	1,148
Amounts written off	(688)	–	(688)
Recoveries of advances written off in previous years	180	–	180
Net charge to the income statement	333	70	403
Unwind of discount on loan impairment charges	(21)	–	(21)
	<u>578</u>	<u>444</u>	<u>1,022</u>
At 31 December 2011 (note 15(a))			
	2010		Total HK\$'M
	Individually assessed HK\$'M	Collectively assessed HK\$'M	
At 1 January 2010	1,196	421	1,617
Amounts written off	(912)	–	(912)
Recoveries of advances written off in previous years	217	–	217
Net charge/(release) to the income statement	297	(47)	250
Unwind of discount on loan impairment charges	(24)	–	(24)
	<u>774</u>	<u>374</u>	<u>1,148</u>
At 31 December 2010 (note 15(a))			

(b) Placements with banks and other financial institutions**Consolidated and Bank**

	Individually assessed	
	2011 HK\$'M	2010 HK\$'M
At 1 January	2	–
Charge to the income statement (note 6(a))	3	3
Unwind of discount on loan impairment charges (note 4(a))	(2)	(1)
	<u>3</u>	<u>2</u>
At 31 December (note 11(a))		

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***17 Investment securities**

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
Available-for-sale securities				
Treasury bills (including Exchange Fund Bills)	34,516	30,898	34,516	30,898
Certificates of deposit held	23,787	15,098	23,787	15,098
Debt securities	66,320	78,827	66,320	78,827
Equity shares	423	241	423	241
Less: impairment charges	(6)	(6)	(6)	(6)
	<u>125,040</u>	<u>125,058</u>	<u>125,040</u>	<u>125,058</u>
Loans and receivables – Debt securities	10,084	9,999	8,253	8,480
Less: impairment charges	(34)	(38)	(30)	(38)
	<u>10,050</u>	<u>9,961</u>	<u>8,223</u>	<u>8,442</u>
	<u>135,090</u>	<u>135,019</u>	<u>133,263</u>	<u>133,500</u>
Issued by:				
Central governments and central banks	42,689	41,651	42,689	41,651
Public sector entities	3,143	2,423	3,143	2,423
Banks and other financial institutions	72,757	75,755	72,757	75,755
Corporate entities	16,501	15,190	14,674	13,671
	<u>135,090</u>	<u>135,019</u>	<u>133,263</u>	<u>133,500</u>
By place of listing:				
Listed in Hong Kong	2,540	4,746	2,540	4,746
Listed outside Hong Kong	34,104	26,893	34,104	26,893
	<u>36,644</u>	<u>31,639</u>	<u>36,644</u>	<u>31,639</u>
Unlisted	98,446	103,380	96,619	101,861
	<u>135,090</u>	<u>135,019</u>	<u>133,263</u>	<u>133,500</u>

Included within loans and receivables – debt securities held by the Bank and its subsidiaries are HK\$1,715 million (2010: HK\$1,835 million) issued by banks and other financial institutions and HK\$8,335 million (2010: HK\$8,126 million) issued by corporate entities. The corresponding amounts held by the Bank are HK\$1,715 million (2010: HK\$1,835 million) issued by banks and other financial institutions and HK\$6,508 million (2010: HK\$ 6,607 million) issued by corporate entities. All loans and receivables – debt securities are unlisted (2010: unlisted).

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank**

During the year, the Bank and its subsidiaries entered into transactions with related parties in the ordinary course of its banking business including lending, acceptance and placement of inter-bank deposits, correspondent banking transactions, banking operation/outsourcing activities and off-balance sheet transactions.

Consolidated

The amounts of material transactions during the year are set out below:

	<i>Immediate holding company</i>		<i>Fellow subsidiaries</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Operating income	655	741	172	228
Operating expenses	1,048	1,208	653	513

The amounts due from/to immediate holding company and fellow subsidiaries stated on the consolidated balance sheet included the following:

	<i>2011</i>		<i>2010 Restated</i>	
	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Assets				
Listed debt securities designated at fair value	–	221	–	344
Unlisted trading debt securities	17	–	–	–
Listed available-for-sale debt securities	–	2,119	–	2,965
Positive fair values of trading derivatives	2,569	103	1,490	2
Positive fair values of hedging derivatives	802	99	291	–
Liabilities				
Other debt securities in issue, measured at amortised cost	–	1,084	–	1,028
Negative fair values of trading derivatives	3,377	12	1,666	199
Negative fair values of hedging derivatives	1,358	16	666	90

The contractual amounts of contingent liabilities and commitments to the immediate holding company and fellow subsidiaries are set out below:

	<i>2011</i>		<i>2010</i>	
	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Financial guarantees and other credit related contingent liabilities	11,943	108	8,576	1,557
Loan commitments and other credit related commitments	2,004	41,330	1,945	37,872

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***18 Amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank (continued)****Bank**

The amounts of material transactions during the year are set out below:

	<i>Immediate holding company</i>		<i>Fellow subsidiaries</i>		<i>Subsidiaries of the Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Operating income	622	784	218	184	1,053	440
Operating expenses	1,048	1,208	653	513	–	–

The amounts due from/to immediate holding company, fellow subsidiaries and subsidiaries of the Bank stated on the balance sheet included the following:

	<i>2011</i>			<i>2010 Restated</i>		
	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Subsidiaries of the Bank</i>	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Subsidiaries of the Bank</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Assets						
Listed debt securities designated at fair value	–	221	–	–	344	–
Unlisted trading debt securities	17	–	–	–	–	–
Listed available-for-sale debt securities	–	2,119	–	–	2,965	–
Placements with a subsidiary	–	–	7,311	–	–	7,510
Subordinated loan	–	–	363	–	–	293
Positive fair values of trading derivatives	2,566	103	–	1,490	2	–
Positive fair values of hedging derivatives	802	99	–	291	–	–
Liabilities						
Other debt securities in issue, measured at amortised cost	–	1,084	–	–	1,028	–
Negative fair values of trading derivatives	3,377	12	–	1,666	199	–
Negative fair values of hedging derivatives	1,358	16	–	666	90	–

The contractual amounts of contingent liabilities and commitments to the immediate holding company, fellow subsidiaries and subsidiaries of the Bank are set out below:

	<i>2011</i>			<i>2010</i>		
	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Subsidiaries of the Bank</i>	<i>Immediate holding company</i>	<i>Fellow subsidiaries</i>	<i>Subsidiaries of the Bank</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Financial guarantees and other credit related contingent liabilities	11,943	108	131	8,576	1,557	115
Loan commitments and other credit related commitments	2,004	41,330	21,479	1,945	37,872	2,490

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***19 Investments in subsidiaries of the Bank**

	<i>Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Unlisted shares, at cost less impairment charges, if any	<u>1,096</u>	<u>1,092</u>

The following list contains only the particulars of subsidiaries which principally affected the results, assets or liabilities of the Bank and its subsidiaries.

<i>Name of company</i>	<i>Place of incorporation</i>	<i>Particulars of issued and paid up capital and securities</i>	<i>Proportion of ownership interest held by the Bank</i>	<i>Principal activity</i>
Standard Chartered APR Limited	United Kingdom	21,971,715 ordinary shares of US\$1 each	100%	Investment holdings
Standard Chartered Securities (Hong Kong) Limited	Hong Kong	1,000,000 ordinary shares of HK\$10 each	100%	Equity capital markets, corporate finance and institutional brokerage
Prime Credit Limited ("PCL")	Hong Kong	400,000 ordinary shares of HK\$100 each	100%	Provision of banking and related financial services
Standard Chartered Leasing Group Limited	Hong Kong	30,000 ordinary shares of US\$1 each	100%	Provision of leasing services

20 Interest in associates***Consolidated***

	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Share of net assets	4,902	2,796
Goodwill	<u>1,717</u>	<u>1,717</u>
	<u>6,619</u>	<u>4,513</u>

Bank

	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Unlisted investments, at cost less impairment losses, if any	3,168	1,755
Listed investment, at cost less impairment losses, if any	<u>1,646</u>	<u>1,607</u>
	<u>4,814</u>	<u>3,362</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***20 Interest in associates (continued)**

The associated companies of the Bank and its subsidiaries are:

<i>Name of associate</i>	<i>Place of establishment and operation</i>	<i>Particulars of issued and paid up capital</i>	<i>Proportion of ownership interest</i>	<i>Principal activity</i>
Asia Commercial Joint Stock Bank ("ACB")	Vietnam	937,696,506 ordinary shares of VND10,000 each	15%	Provision of banking and related financial services
China Bohai Bank Company Limited ("Bohai")	The People's Republic of China	13,855,000,000 ordinary shares of RMB1 each	20%	Provision of banking and related financial services
Merchant Solutions Private Limited ("MS")	Singapore	560,000 "A" shares and 440,000 "B" shares	44%	Credit card merchant acquiring business

Shareholdings in associated companies include a listed investment of HK\$2,457 million (2010: HK\$2,298 million). At the balance sheet date, the investment based on quoted market prices was valued at HK\$1,142 million (2010: HK\$1,220 million). Impairment testing on the investment has been carried out and this demonstrates that there is no impairment.

The Bank and its subsidiaries' investment in ACB is less than 20% but it has been accounted for as an associate, as the Bank has representation on the Board of Directors and also through a Technical Support and Assistance Agreement, which includes the secondment of staff to ACB, is able to exercise significant influence over the company's management, financial and operating policies.

In respect of the year ended 31 December 2011, the share of the results of MS and ACB was included in these financial statements based on accounts drawn up to 30 September 2011, but taking into account any changes in the subsequent period from 1 October 2011 to 31 December 2011 that would materially affect the results. Bohai's result was included in the financial statements based on accounts drawn up to 30 November 2011. The Bank and its subsidiaries have taken advantage of the provision contained in HKAS 28/IAS 28 "Investments in Associates" whereby it is permitted to include the attributable share of associates' results based on accounts drawn up to a non-coterminous period and where the difference is not greater than three months.

The Bank and its subsidiaries' unrecognised share of profits of associates for the year is HK\$7 million (2010: losses of HK\$24 million). Where there are accumulated unrecognised share of associates' losses, subsequent profits earned are not recognised until previously unrecognised losses are extinguished. The Bank and its subsidiaries' unrecognised share of losses of associates net of unrecognised profits on a cumulative basis is HK\$78 million (2010: HK\$85 million).

Summary of financial information of associates

	<i>Assets HK\$'M</i>	<i>Liabilities HK\$'M</i>	<i>Equity HK\$'M</i>	<i>Revenue HK\$'M</i>	<i>Profit HK\$'M</i>
2011					
100 per cent	439,969	414,542	25,427	16,501	3,115
Effective interest of the Bank and its subsidiaries	<u>82,933</u>	<u>78,031</u>	<u>4,902</u>	<u>2,844</u>	<u>570</u>
	<i>Assets HK\$'M</i>	<i>Liabilities HK\$'M</i>	<i>Equity HK\$'M</i>	<i>Revenue HK\$'M</i>	<i>Profit HK\$'M</i>
2010					
100 per cent	373,688	358,511	15,177	10,334	1,831
Effective interest of the Bank and its subsidiaries	<u>71,079</u>	<u>68,283</u>	<u>2,796</u>	<u>1,758</u>	<u>326</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***21 Fixed assets****Consolidated**

	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>2011 Operating lease assets HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost or valuation:						
At 1 January 2011, as previously reported	2,862	389	–	3,251	518	3,769
Effect of change in accounting policy	–	–	–	–	23	23
As restated	2,862	389	–	3,251	541	3,792
Additions	150	180	7,359	7,689	110	7,799
Disposals and write-offs	(52)	(83)	–	(135)	(70)	(205)
Reclassifications	(2)	2	–	–	–	–
Net gains on revaluation	–	–	–	–	5	5
At 31 December 2011	2,958	488	7,359	10,805	586	11,391
Representing:						
Cost	2,958	488	7,359	10,805	–	10,805
Valuation	–	–	–	–	586	586
	2,958	488	7,359	10,805	586	11,391
Accumulated depreciation:						
At 1 January 2011, as previously reported	492	197	–	689	45	734
Effect of change in accounting policy	–	–	–	–	(45)	(45)
As restated	492	197	–	689	–	689
Charge for the year (note 4(g))	95	127	93	315	–	315
Attributable to assets sold or written off	(52)	(83)	–	(135)	–	(135)
At 31 December 2011	535	241	93	869	–	869
Net book value:						
At 31 December 2011	2,423	247	7,266	9,936	586	10,522

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***21 Fixed assets (continued)****Consolidated (continued)**

	2010				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost or valuation:					
At 1 January 2010, as previously reported	2,733	513	3,246	518	3,764
Effect of change in accounting policy	—	—	—	74	74
As restated	2,733	513	3,246	592	3,838
Additions	97	84	181	—	181
Disposals and write-offs	(77)	(238)	(315)	—	(315)
Reclassifications	(30)	30	—	—	—
Net losses on revaluation	—	—	—	(51)	(51)
Transfer from property held for sale	139	—	139	—	139
At 31 December 2010	2,862	389	3,251	541	3,792
Representing:					
Cost	2,862	389	3,251	—	3,251
Valuation	—	—	—	541	541
	2,862	389	3,251	541	3,792
Accumulated depreciation:					
At 1 January 2010, as previously reported	454	338	792	34	826
Effect of change in accounting policy	—	—	—	(34)	(34)
As restated	454	338	792	—	792
Charge for the year (note 4(g))	95	94	189	—	189
Attributable to assets sold or written off	(64)	(235)	(299)	—	(299)
Transfer from property held for sale	7	—	7	—	7
At 31 December 2010	492	197	689	—	689
Net book value:					
At 31 December 2010	2,370	192	2,562	541	3,103

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***21 Fixed assets (continued)****Bank**

	2011				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost or valuation:					
At 1 January 2011,					
as previously reported	2,686	372	3,058	518	3,576
Effect of change in accounting policy	—	—	—	23	23
As restated	2,686	372	3,058	541	3,599
Additions	42	157	199	106	305
Disposals and write-offs	(32)	(75)	(107)	(106)	(213)
Reclassifications	(2)	2	—	—	—
Net losses on revaluation	—	—	—	(10)	(10)
At 31 December 2011	2,694	456	3,150	531	3,681
Representing:					
Cost	2,694	456	3,150	—	3,150
Valuation	—	—	—	531	531
	2,694	456	3,150	531	3,681
Accumulated depreciation:					
At 1 January 2011,					
as previously reported	473	188	661	45	706
Effect of change in accounting policy	—	—	—	(45)	(45)
As restated	473	188	661	—	661
Charge for the year	86	122	208	—	208
Attributable to assets sold or written off	(32)	(75)	(107)	—	(107)
At 31 December 2011	527	235	762	—	762
Net book value:					
At 31 December 2011	2,167	221	2,388	531	2,919

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***21 Fixed assets (continued)****Bank (continued)**

	2010				
	<i>Buildings and leasehold land held for own use HK\$'M</i>	<i>Equipment, furniture & fixtures HK\$'M</i>	<i>Sub-total HK\$'M</i>	<i>Investment properties HK\$'M</i>	<i>Total fixed assets HK\$'M</i>
Cost or valuation:					
At 1 January 2010,					
as previously reported	2,634	494	3,128	518	3,646
Effect of change in accounting policy	–	–	–	74	74
As restated	2,634	494	3,128	592	3,720
Additions	18	75	93	–	93
Disposals and write-offs	(75)	(227)	(302)	–	(302)
Reclassifications	(30)	30	–	–	–
Net losses on revaluation	–	–	–	(51)	(51)
Transfer from property held for sale	139	–	139	–	139
At 31 December 2010	2,686	372	3,058	541	3,599
Representing:					
Cost	2,686	372	3,058	–	3,058
Valuation	–	–	–	541	541
	2,686	372	3,058	541	3,599
Accumulated depreciation:					
At 1 January 2010,					
as previously reported	436	324	760	34	794
Effect of change in accounting policy	–	–	–	(34)	(34)
As restated	436	324	760	–	760
Charge for the year	92	88	180	–	180
Attributable to assets sold or written off	(62)	(224)	(286)	–	(286)
Transfer from property held for sale	7	–	7	–	7
At 31 December 2010	473	188	661	–	661
Net book value:					
At 31 December 2010	2,213	184	2,397	541	2,938

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***21 Fixed assets (continued)***Buildings and leasehold land held for own use:*

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Leasehold in Hong Kong, at cost				
– long-term leases	33	34	–	–
– medium-term leases	2,114	2,174	2,095	2,157
– short-term leases	72	162	72	56
	<u>2,219</u>	<u>2,370</u>	<u>2,167</u>	<u>2,213</u>
Freehold outside Hong Kong, at cost	204	–	–	–
	<u>2,423</u>	<u>2,370</u>	<u>2,167</u>	<u>2,213</u>

Investment properties:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Freehold outside Hong Kong, at fair value	<u>586</u>	<u>541</u>	<u>531</u>	<u>541</u>

Investment properties were revalued as at 31 December 2011 on an open market value basis. The valuation was carried out by an independent firm which has among its staff, members of the Royal Institute of Chartered Surveyors with recent experience in the location and category of the property being valued.

Operating lease assets:

Assets leased to customers under operating leases consist of commercial aircrafts and vessels. At 31 December, total future minimum lease receivables under operating leases are as follows:

	<i>Consolidated</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Within 1 year	747	–
After 1 year but within 5 years	2,807	–
After 5 years	4,486	–
	<u>8,040</u>	<u>–</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***22 Goodwill and intangible assets****Consolidated**

	2011		
	<i>Capitalised software and other intangible assets HK\$'M</i>	<i>Goodwill HK\$'M</i>	<i>Total HK\$'M</i>
Cost:			
At 1 January 2011	373	1,507	1,880
Additions	115	–	115
Disposals and write-offs	(107)	–	(107)
	<u>381</u>	<u>1,507</u>	<u>1,888</u>
At 31 December 2011	----- 381	----- 1,507	----- 1,888
Accumulated amortisation:			
At 1 January 2011	159	–	159
Charge for the year (note 4(g))	93	–	93
Attributable to intangible assets sold or written off	(105)	–	(105)
	<u>147</u>	<u>–</u>	<u>147</u>
At 31 December 2011	----- 147	----- –	----- 147
Carrying amount:			
At 31 December 2011	<u>234</u>	<u>1,507</u>	<u>1,741</u>
	=====	=====	=====
	2010 Restated		
	<i>Capitalised software and other intangible assets HK\$'M</i>	<i>Goodwill HK\$'M</i>	<i>Total HK\$'M</i>
Cost:			
At 1 January 2010	366	1,487	1,853
Additions	88	20	108
Disposals and write-offs	(81)	–	(81)
	<u>373</u>	<u>1,507</u>	<u>1,880</u>
At 31 December 2010	----- 373	----- 1,507	----- 1,880
Accumulated amortisation:			
At 1 January 2010	116	–	116
Charge for the year (note 4(g))	93	–	93
Attributable to intangible assets sold or written off	(50)	–	(50)
	<u>159</u>	<u>–</u>	<u>159</u>
At 31 December 2010	----- 159	----- –	----- 159
Carrying amount:			
At 31 December 2010	<u>214</u>	<u>1,507</u>	<u>1,721</u>
	=====	=====	=====

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***22 Goodwill and intangible assets (continued)****Bank**

	2011		
	<i>Capitalised software and other intangible assets</i> HK\$'M	<i>Goodwill</i> HK\$'M	<i>Total</i> HK\$'M
Cost:			
At 1 January 2011	280	729	1,009
Additions	115	–	115
Disposals and write-offs	(97)	–	(97)
	<u>298</u>	<u>729</u>	<u>1,027</u>
At 31 December 2011	298	729	1,027
Accumulated amortisation:			
At 1 January 2011	123	–	123
Charge for the year	80	–	80
Attributable to intangible assets sold or written off	(97)	–	(97)
	<u>106</u>	<u>–</u>	<u>106</u>
At 31 December 2011	106	–	106
Carrying amount:			
At 31 December 2011	<u>192</u>	<u>729</u>	<u>921</u>
	2010		
	<i>Capitalised software and other intangible assets</i> HK\$'M	<i>Goodwill</i> HK\$'M	<i>Total</i> HK\$'M
Cost:			
At 1 January 2010	288	729	1,017
Additions	73	–	73
Disposals and write-offs	(81)	–	(81)
	<u>280</u>	<u>729</u>	<u>1,009</u>
At 31 December 2010	280	729	1,009
Accumulated amortisation:			
At 1 January 2010	96	–	96
Charge for the year	77	–	77
Attributable to intangible assets sold or written off	(50)	–	(50)
	<u>123</u>	<u>–</u>	<u>123</u>
At 31 December 2010	123	–	123
Carrying amount:			
At 31 December 2010	<u>157</u>	<u>729</u>	<u>886</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***22 Goodwill and intangible assets (continued)*****Impairment tests for cash-generating units containing goodwill***

Goodwill is allocated to the Bank and its subsidiaries' cash-generating units ("CGUs") as follows:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>Restated 2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Lending	611	611	611	611
Private Banking	118	118	118	118
Standard Chartered Securities (Hong Kong) Limited	253	253	–	–
Prime Credit Limited ("PCL")	525	525	–	–
	<u>1,507</u>	<u>1,507</u>	<u>729</u>	<u>729</u>

The recoverable amounts of the CGUs are determined based on value in use calculations. The key assumptions and approach to determining value in use calculations, as set out below, are solely estimates for the purpose of assessing impairment on acquired goodwill. These calculations use cash flow projections based on budgets and forecasts approved by management covering one year and extrapolated for a further 19 years using steady growth rates of 4.3 per cent (2010: 5 per cent).

In assessing impairment of goodwill, the Bank and its subsidiaries assumed growth at a steady rate in line with long-term forecast GDP growth. A discount rate of 18.0 per cent (2010: 15.8 per cent) was used.

23 Other assets

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Prepayments and accrued income	2,480	1,771	2,306	1,564
Sundry debtors	2,222	3,104	1,990	3,053
Acceptances and endorsements	4,777	4,611	4,777	4,611
Positive fair values of hedging derivatives	56	1	56	1
Others	2,431	1,322	1,849	766
	<u>11,966</u>	<u>10,809</u>	<u>10,978</u>	<u>9,995</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***24 Business combinations****2010 acquisition**

On 12 April 2010 and 18 June 2010, Prime Credit Limited (“PCL”) (which became a wholly owned subsidiary of the Bank on 1 July 2010) acquired the personal loan portfolios of GE Capital Trade Services Limited and GE Capital (Hong Kong) Limited (“GECHK”) respectively. On 3 July 2010, PCL also acquired the other consumer finance businesses of GECHK.

Goodwill of HK\$20 million (restated) was recognised and HK\$14 million of customer relationship intangibles identified.

If the acquisitions had occurred on 1 January 2010, the operating income of the Bank and its subsidiaries would have been approximately HK\$18,503 million (restated) and profit before taxation would have been approximately HK\$7,426 million (restated).

The assets and liabilities arising from the acquisitions were as follows:

	<i>Restated Fair value HK\$'M</i>
Cash and balances with banks and other financial institutions	958
Advances to customers	5,546
Intangibles other than goodwill	14
Other assets	6
Total assets	6,524
Other liabilities	12
Total liabilities	12
Net assets acquired	6,512
Purchase consideration settled in cash	(6,532)
Cash and cash equivalents acquired	958
Cash outflow on acquisitions	(5,574)
Purchase consideration – cash paid	6,532
Less: Fair value of net assets acquired	(6,512)
Goodwill	20
Intangible assets acquired:	
Customer relationships	14
Contribution from acquisitions to 31 December 2010:	
Operating income	94
Profit before taxation	59

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***24 Business combinations (continued)****2010 acquisitions (continued)**

The fair value of advances to customers is HK\$5,546 million (restated). The gross contractual amount due is HK\$5,622 million, of which HK\$76 million (restated) is the best estimate of the contractual cash flows not expected to be collected.

Goodwill arising on the above acquisitions is attributable to the synergies expected to arise from their integration with the Bank and its subsidiaries.

25 Deposits from customers

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Current accounts	96,528	74,727	96,528	74,727
Savings accounts	318,359	303,112	318,359	303,112
Time, call and notice deposits	252,626	183,370	252,111	182,906
Deposits and balances of central banks	5,427	12,068	5,427	12,068
	<u>672,940</u>	<u>573,277</u>	<u>672,425</u>	<u>572,813</u>

26 Debt securities in issue

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Certificates of deposit, measured at amortised cost	<u>13,265</u>	<u>–</u>

27 Financial liabilities designated at fair value

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Structured customer deposits	2,615	3,052
Debt securities issued	<u>872</u>	<u>–</u>
	<u>3,487</u>	<u>3,052</u>

The Bank designates certain financial liabilities at fair value where either the liabilities:

- have fixed rates of interest and interest rate swaps or other interest related derivatives have been transacted with the intention of significantly reducing interest rate risk; or
- are exposed to equity price risk or foreign currency risk and derivatives have been transacted with the intention of significantly reducing exposure to market changes;

At 31 December 2011, the contractual amount payable at maturity of these financial liabilities exceeded the carrying amount by HK\$56 million (2010: HK\$45 million). This change is attributable to changes in market rates.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***28 Taxation in the balance sheet (continued)*****Deferred tax assets and liabilities (continued):***

The components of gross deferred tax (assets)/liabilities recognised in the balance sheet and the movements during the year are as follows: (continued)

Bank

	<i>Depreciation allowances in excess of related depreciation HK\$'M</i>	<i>Impairment losses on financial assets HK\$'M</i>	<i>Available for-sale securities HK\$'M</i>	<i>Structured investments HK\$'M</i>	<i>Others HK\$'M</i>	<i>Total HK\$'M</i>
<i>2011</i>						
<i>Deferred tax arising from:</i>						
At 1 January 2011	(3)	(62)	11	–	(258)	(312)
Charge/(release) to income statement	15	(12)	–	–	252	255
Release to reserves	–	–	(178)	–	(40)	(218)
	<u>12</u>	<u>(74)</u>	<u>(167)</u>	<u>–</u>	<u>(46)</u>	<u>(275)</u>
	<i>2010</i>					
At 1 January 2010	(5)	(70)	38	(305)	(146)	(488)
Charge/(release) to income statement	2	8	–	305	(101)	214
Release to reserves	–	–	(27)	–	(11)	(38)
	<u>(3)</u>	<u>(62)</u>	<u>11</u>	<u>–</u>	<u>(258)</u>	<u>(312)</u>
	<i>Consolidated</i>		<i>Bank</i>			
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>		
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>		
<i>Analysed by:</i>						
Net deferred tax asset recognised on the balance sheet	(319)	(350)	(275)	(312)		
Net deferred tax liability recognised on the balance sheet	5	17	–	–		
	<u>(314)</u>	<u>(333)</u>	<u>(275)</u>	<u>(312)</u>		

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***29 Trading liabilities**

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Short positions in securities	23,855	36,196
Negative fair values of trading derivatives	783	250
	<u>24,638</u>	<u>36,446</u>

30 Other liabilities

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Accruals and deferred income	4,372	3,121	3,960	2,719
Provision for liabilities and charges	1,082	2,267	1,082	2,267
Negative fair values of hedging derivatives	–	54	–	49
Acceptances and endorsements	4,777	4,611	4,777	4,611
Others	9,544	6,427	9,168	6,071
	<u>19,775</u>	<u>16,480</u>	<u>18,987</u>	<u>15,717</u>

31 Employee retirement benefits

The Bank and its subsidiaries made contributions to two defined benefit retirement schemes, namely Standard Chartered Bank Hong Kong Retirement Scheme (“SCB Scheme”) and Cazenove Hong Kong Retirement Scheme (“Cazenove Scheme”) which covered 18% (2010: 21%) of the Bank and its subsidiaries’ employees. The schemes are administered by trustees, with the assets held separately from those of the Bank and its subsidiaries.

In December 2011, the Bank closed the Cazenove Scheme. Members’ benefits accrued under the Cazenove Scheme were transferred to the SCB Scheme in December 2011. The assets under the Cazenove Scheme were redeemed and also transferred to the SCB Scheme in December 2011.

(a) The amounts recognised in the consolidated balance sheet are as follows:

	<i>SCB Scheme</i>		<i>Cazenove Scheme</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Fair value of plan assets	1,906	1,927	–	75
Present value of wholly or partly funded obligations	<u>(2,129)</u>	<u>(1,807)</u>	<u>–</u>	<u>(56)</u>
Net (liability)/asset recognised in the balance sheet (included in “Other liabilities”/“Other assets”)	<u>(223)</u>	<u>120</u>	<u>–</u>	<u>19</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***31 Employee retirement benefits (continued)****(b) Movements in the present value of the defined benefit obligations:**

	SCB Scheme		Cazenove Scheme	
	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M
At the beginning of the year	1,807	1,712	56	54
Current service cost	96	95	5	6
Interest cost	46	43	2	1
Benefits paid	(110)	(79)	(2)	(4)
Actuarial losses/(gains)	222	36	7	(1)
Transfer in/(out)	68	–	(68)	–
	<u>2,129</u>	<u>1,807</u>	<u>–</u>	<u>56</u>

(c) Movements in the fair value of plan assets:

	SCB Scheme		Cazenove Scheme	
	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M
At the beginning of the year	1,927	1,799	75	70
Contributions	57	56	4	5
Expected return on assets	120	115	5	4
Benefits paid	(110)	(79)	(2)	(4)
Actuarial (losses)/gains on plan assets	(159)	36	(11)	–
Transfer in/(out)	71	–	(71)	–
	<u>1,906</u>	<u>1,927</u>	<u>–</u>	<u>75</u>

(d) Movements in the net (liabilities)/assets recognised in the consolidated balance sheet are as follows:

	SCB Scheme		Cazenove Scheme	
	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M
At the beginning of the year	120	87	19	16
Contributions	57	56	4	5
Expense recognised in the income statement (note 4(g))	(22)	(23)	(2)	(3)
Actuarial (losses)/gains to pension reserve	(381)	–	(18)	1
Transfer in/(out)	3	–	(3)	–
	<u>(223)</u>	<u>120</u>	<u>–</u>	<u>19</u>

As at 31 December 2011, the Scheme did not invest in the Bank's own financial instruments and properties (2010: HK\$Nil). The Bank expects to contribute approximately HK\$64 million to the SCB Scheme in 2012.

The total cumulative amount of actuarial gains and losses recognised directly in consolidated other comprehensive income to date in respect of the SCB Scheme is a loss of HK\$549 million (2010: loss of HK\$168 million).

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***31 Employee retirement benefits (continued)****(e) The expense recognised in the consolidated income statement for the year is as follows:**

	SCB Scheme		Cazenove Scheme	
	2011 HK\$'M	2010 HK\$'M	2011 HK\$'M	2010 HK\$'M
Current service cost	96	95	5	6
Interest cost	46	43	2	1
Actuarial expected return on plan assets	(120)	(115)	(5)	(4)
	<u>22</u>	<u>23</u>	<u>2</u>	<u>3</u>

The actual return on plan assets (taking into account all changes in the fair value of plan assets) was a net expense of HK\$120 million (2010: net income of HK\$156 million).

(f) The principal actuarial assumptions used in the valuation are as follows:

	SCB Scheme		Cazenove Scheme	
	2011	2010	2011	2010
Discount rate	1.50%	2.70%	1.50%	2.70%
Expected rate of return on plan assets	6.50%	6.50%	6.50%	6.50%
Future salary increases	3.50%	3.50%	3.50%	3.50%

The expected return is based on market expectations at the beginning of the year, for the return net of administration costs, over the entire life of the related obligations.

(g) The major categories of assets as a percentage of total assets are as follows:

	SCB Scheme		Cazenove Scheme	
	2011	2010	2011	2010
Equities	47%	53%	–	61%
Bonds	46%	45%	–	35%
Cash	7%	2%	–	4%
	<u>100%</u>	<u>100%</u>	<u>–</u>	<u>100%</u>

(h) Amounts for the current and previous years**SCB Scheme**

	2011 HK\$'M	2010 HK\$'M	2009 HK\$'M	2008 HK\$'M	2007 HK\$'M
Fair value of plan assets	1,906	1,927	1,799	1,467	1,980
Present value of defined benefit obligations	<u>(2,129)</u>	<u>(1,807)</u>	<u>(1,712)</u>	<u>(1,890)</u>	<u>(1,666)</u>
Net (deficit)/surplus	<u>(223)</u>	<u>120</u>	<u>87</u>	<u>(423)</u>	<u>314</u>
Experience (losses)/gains on scheme assets	(159)	36	261	(623)	177
Experience (losses)/gains on scheme liabilities	(70)	(50)	(9)	(57)	(106)

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***31 Employee retirement benefits (continued)****(h) Amounts for the current and previous years (continued)****Cazenove Scheme**

	2011 HK\$'M	2010 HK\$'M	30 January to 31 December 2009 HK\$'M
Fair value of plan assets	–	75	70
Present value of defined benefit obligations	–	(56)	(54)
Net surplus/(deficit)	–	19	16
Experience (losses)/gains on scheme assets	(11)	–	13
Experience (losses)/gains on scheme liabilities	(2)	1	7

32 Subordinated liabilities

	<i>Consolidated and Bank</i>	
	2011 HK\$'M	2010 HK\$'M
US\$300 million Floating Rate Step-Up Notes 2017 ⁽¹⁾	2,330	2,314
US\$750 million 5.875% Fixed Rate Notes 2020 ⁽²⁾	6,427	5,741
SGD750 million 4.15% Fixed Rate Notes 2021 ⁽³⁾	4,343	–
	<u>13,100</u>	<u>8,055</u>

All subordinated liabilities are unsecured and subordinated to the claims of other creditors.

- (1) Interest rate at three-months US dollar LIBOR plus 0.25 per cent, payable quarterly, to the call option date on 13 April 2012. Thereafter, it will be reset to three-months US dollar LIBOR plus 0.75 per cent, payable quarterly.
- (2) Interest rate at 5.875 per cent per annum, payable semi-annually, to the maturity date on 24 June 2020.
- (3) Interest rate at 4.15 per cent per annum, payable semi-annually, to the maturity date on 27 October 2021.

33 Share capital

	<i>2011 and 2010</i>	
	<i>No. of shares in millions</i>	<i>HK\$'M</i>
Authorised:		
'A' ordinary shares of HK\$0.05 each	780	39
'B' ordinary shares of HK\$0.05 each	1,231	62
	<u>2,011</u>	<u>101</u>
Preference shares of HK\$1.00 each	3,800	3,800
	<u>5,811</u>	<u>3,901</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***33 Share capital (continued)**

	<i>2011 and 2010</i>	
	<i>No. of shares in millions</i>	<i>HK\$'M</i>
<i>Issued and fully paid:</i>		
'A' ordinary shares of HK\$0.05 each	706	35
'B' ordinary shares of HK\$0.05 each	1,231	62
	<hr/>	<hr/>
	1,937	97
Preference shares of HK\$1.00 each	–	–
	<hr/>	<hr/>
	1,937	97
	<hr/> <hr/>	<hr/> <hr/>

The preference shares bear a non-cumulative preferential dividend at a rate of 8.25% per annum on their nominal amount and rank in priority to the 'A' ordinary shares and the 'B' ordinary shares with respect to the payment of dividends and any return of capital. The 'B' ordinary shares rank in priority to the 'A' ordinary shares with respect to any return of capital.

34 Reserves***Nature and purpose of reserves*****(i) Share premium**

The application of the share premium account is governed by Section 48B of the Hong Kong Companies Ordinance.

(ii) Capital redemption reserve

The capital redemption reserve represents the repurchase of the Bank's own shares.

(iii) Available-for-sale investment reserve

The available-for-sale investment reserve comprises the cumulative net change in the fair value of available-for-sale securities held at the balance sheet date and is dealt with in accordance with the accounting policy in note 2(i).

(iv) Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments used in cash flow hedges pending subsequent recognition of the hedged cash flow in accordance with the accounting policy adopted for cash flow hedges in note 2(j).

(v) Pension reserve

The pension reserve comprises the cumulative net effect of the actuarial gains and losses for the defined benefit plans.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***34 Reserves (continued)**

(vi) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policy set out in note 2(s).

(vii) Revaluation reserve

The revaluation reserve comprises the share of the change in fair value of an associate's identifiable net assets prior to the Bank and its subsidiaries obtaining significant influence in a step-acquisition.

(viii) Merger reserve

The merger reserve arises on the acquisition of Prime Credit Limited ("PCL"). On 1 July 2010, the Bank acquired 100 per cent of the share capital of PCL at a cost of HK\$204 million. (Note 2).

(ix) Share option equity reserve

The Group operates equity-settled share-based compensation plans in which the Bank and its subsidiaries' employees participate. The fair value of the employee services received in exchange for the grant of the share awards is recognized as an expense with the corresponding amount credited to the share option equity reserve.

The HKMA requires the Bank and its subsidiaries to maintain a minimum level of impairment allowances which is in excess of the impairment allowances required under Hong Kong Financial Reporting Standards. Of the retained earnings as at 31 December 2011, an amount of HK\$5,309 million (2010: HK\$1,366 million) has been reserved for this purpose.

35 Cash and cash equivalents

	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
(a) Components of cash and cash equivalents in the cash flow statement		
Cash and balances with banks, central banks and other financial institutions	21,777	29,902
Trading assets with original maturity within three months	14,856	18,503
Placements with banks and other financial institutions with original maturity within three months	67,301	33,718
Amounts due from immediate holding company and fellow subsidiaries with original maturity within three months	44,789	42,329
Less: Overdrafts included in "deposits and balances of banks and other financial institutions"	(77)	(46)
Less: Overdrafts included in "amounts due to immediate holding company"	(121)	(98)
	<u>148,525</u>	<u>124,308</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***35 Cash and cash equivalents (continued)**

	<i>2011</i> <i>HK\$'M</i>	<i>2010</i> <i>HK\$'M</i>
(b) Reconciliation with the consolidated balance sheet		
Cash and balances with banks, central banks, and other financial institutions	21,777	29,902
Placements with banks and other financial institutions	136,513	97,167
Trading assets	35,377	48,719
Amounts due from immediate holding company and fellow subsidiaries	68,488	54,325
Overdrafts included in "deposits and balances of banks and other financial institutions"	(77)	(46)
Overdrafts included in "amounts due to immediate holding company"	(121)	(98)
	<hr/>	<hr/>
Amounts shown in the balance sheet	261,957	229,969
Less: amounts with an original maturity of beyond three months	(113,432)	(105,661)
	<hr/>	<hr/>
Cash and cash equivalents in the consolidated cash flow statement	<u>148,525</u>	<u>124,308</u>

36 Derivative financial instruments

The use of derivatives for trading and their sale to customers as risk management products is an integral part of the Bank's business activities. These instruments are also used to manage the Bank's own exposures to market risk as part of its asset and liability management process. The principal derivative instruments used by the Bank are foreign exchange related and interest rate related contracts, which are primarily over-the-counter derivatives. Most of the Bank's derivative positions have been entered into to meet customer demand and to hedge these and other trading positions. For accounting purposes, derivatives are classified as either held for trading or held for hedging.

(a) Notional amounts of derivatives

Derivatives are financial instruments that derive their value in reference to changes in interest or exchange rates, credit risk, financial instrument prices and indices. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***36 Derivative financial instruments (continued)****(a) Notional amounts of derivatives (continued)**

The following is a summary of the notional amounts of each significant type of derivative entered into by the Bank and its subsidiaries:

Consolidated

	2011			Total HK\$'M
	Qualifying for hedge accounting HK\$'M	Managed in conjunction with financial instruments designated at fair value through profit or loss HK\$'M	Others, including held for trading HK\$'M	
Exchange rate contracts				
Forwards	–	795	690,004	690,799
Cross currency swaps	12,502	1,372	20,756	34,630
Options purchased	–	382	15,177	15,559
Options written	–	2,233	15,600	17,833
Interest rate contracts				
Forwards	–	–	–	–
Swaps	105,278	593	11,924	117,795
Options purchased	–	416	350	766
Options written	–	480	350	830
Other derivatives	–	99	14,035	14,134
	<u>117,780</u>	<u>6,370</u>	<u>768,196</u>	<u>892,346</u>
<i>2010 Restated</i>				
Exchange rate contracts				
Forwards	–	367	401,545	401,912
Cross currency swaps	11,757	–	8,032	19,789
Options purchased	–	36	8,965	9,001
Options written	–	3,234	8,786	12,020
Interest rate contracts				
Forwards	–	–	3,054	3,054
Swaps	51,519	222	17,250	68,991
Options purchased	–	–	382	382
Options written	–	1,930	350	2,280
Other derivatives	–	2	643	645
	<u>63,276</u>	<u>5,791</u>	<u>449,007</u>	<u>518,074</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***36 Derivative financial instruments (continued)****Bank**

	2011			Total HK\$'M
	Qualifying for hedge accounting HK\$'M	Managed in conjunction with financial instruments designated at fair value through profit or loss HK\$'M	Others, including held for trading HK\$'M	
Exchange rate contracts				
Forwards	–	795	690,004	690,799
Cross currency swaps	12,502	1,372	20,756	34,630
Options purchased	–	382	15,177	15,559
Options written	–	2,233	15,600	17,833
Interest rate contracts				
Forwards	–	–	–	–
Swaps	105,278	593	11,384	117,255
Options purchased	–	416	350	766
Options written	–	480	350	830
Other derivatives	–	99	14,035	14,134
	<u>117,780</u>	<u>6,370</u>	<u>767,656</u>	<u>891,806</u>
<i>2010 Restated</i>				
Exchange rate contracts				
Forwards	–	367	401,545	401,912
Cross currency swaps	11,757	–	8,032	19,789
Options purchased	–	36	8,965	9,001
Options written	–	3,234	8,786	12,020
Interest rate contracts				
Forwards	–	–	3,054	3,054
Swaps	50,319	222	17,250	67,791
Options purchased	–	–	382	382
Options written	–	1,930	350	2,280
Other derivatives	–	2	643	645
	<u>62,076</u>	<u>5,791</u>	<u>449,007</u>	<u>516,874</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***36 Derivative financial instruments (continued)****(b) Fair values and credit risk weighted amounts of derivatives****Consolidated**

	2011			2010		
	<i>Fair value assets</i>	<i>Fair value liabilities</i>	<i>Credit risk weighted amount</i>	<i>Fair value assets</i>	<i>Fair value liabilities</i>	<i>Credit risk weighted amount</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Exchange rate contracts	2,644	3,088	1,135	2,382	2,309	1,104
Interest rate contracts	1,759	2,438	295	174	609	142
Other derivatives	16	20	7	8	7	5
	<u>4,419</u>	<u>5,546</u>	<u>1,437</u>	<u>2,564</u>	<u>2,925</u>	<u>1,251</u>

Bank

	2011			2010		
	<i>Fair value assets</i>	<i>Fair value liabilities</i>	<i>Credit risk weighted amount</i>	<i>Fair value assets</i>	<i>Fair value liabilities</i>	<i>Credit risk weighted amount</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Exchange rate contracts	2,644	3,088	1,135	2,382	2,309	1,104
Interest rate contracts	1,756	2,438	294	174	604	142
Other derivatives	16	20	7	8	7	5
	<u>4,416</u>	<u>5,546</u>	<u>1,436</u>	<u>2,564</u>	<u>2,920</u>	<u>1,251</u>

Credit risk weighted amount refers to the amount as computed in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance. The amount calculated is dependent upon the status of the counterparty and maturity characteristics of each type of contract.

The fair values and credit risk weighted amounts do not take into account any bilateral netting arrangements entered into during the year and accordingly these amounts are shown on a gross basis.

(c) Fair value of derivative financial instruments designated as hedging instruments

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Bank and its subsidiaries as at 31 December 2011:

As at 31 December 2011

Consolidated and Bank

	<i>Assets (Included in Other assets and Amounts due from immediate holding company and fellow subsidiaries)</i>	<i>Liabilities (Included in Amounts due to immediate holding company and fellow subsidiaries)</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Exchange rate contracts	269	30
Interest rate contracts	688	1,344
	<u>957</u>	<u>1,374</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***36 Derivative financial instruments (continued)****(c) Fair value of derivative financial instruments designated as hedging instruments (continued)**

As at 31 December 2010

Consolidated

	<i>Assets (Included in Other assets and Amounts due from immediate holding company) HK\$'M</i>	<i>Liabilities (Included in Other liabilities and Amounts due to immediate holding company and fellow subsidiaries) HK\$'M</i>
Exchange rate contracts	251	331
Interest rate contracts	41	479
	292	810

Bank

	<i>Assets (Included in Other assets and Amounts due from immediate holding company) HK\$'M</i>	<i>Liabilities (Included in Other liabilities and Amounts due to immediate holding company and fellow subsidiaries) HK\$'M</i>
Exchange rate contracts	251	331
Interest rate contracts	41	474
	292	805

Fair value hedges

The fair value hedges principally consist of interest rate swaps and cross currency swaps. The interest rate swaps are used to protect against changes in the fair value of certain fixed rate assets and liabilities due to movements in market interest rates. The cross currency swaps are used to manage foreign exchange exposures. At 31 December 2011, the net negative fair value of derivatives held as fair value hedges was HK\$338 million (2010: negative HK\$424 million) comprising assets of HK\$917 million (2010: HK\$260 million) and liabilities of HK\$1,255 million (2010: HK\$684 million). The losses on the hedging instruments for the year were HK\$501 million (2010: losses of HK\$929 million). The gains on the hedged item attributable to the hedged risk were HK\$501 million (2010: gains of HK\$924 million).

Cash flow hedges

The cash flow hedges principally consist of interest rate swaps and cross currency swaps that are used to hedge against the variability in cash flows of certain floating rate assets and liabilities. At 31 December 2011, the net negative fair value of derivatives held as cash flow hedges was HK\$79 million (2010: negative HK\$94 million) comprising assets of HK\$40 million (2010: HK\$32 million) and liabilities of HK\$119 million (2010: HK\$126 million). The derivatives will mature within 5 years (2010: within 5 years) from the balance sheet date. During the year, there was no ineffectiveness recognised in the income statement that arose from cash flow hedges (2010: HK\$ Nil).

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***37 Contingent liabilities and commitments****(a) The following is a summary of the contractual amounts of each significant contingent liability and commitment:**

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>Restated 2010</i>	<i>2011</i>	<i>Restated 2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Direct credit substitutes	16,520	14,325	16,615	14,437
Transaction-related contingencies	13,755	19,608	13,755	19,608
Trade-related contingencies	26,517	24,713	26,549	24,713
Forward asset purchases	622	2,283	622	2,283
Forward forward deposits placed	–	700	–	700
Other commitments: which are not unconditionally cancellable:				
with original maturity of not more than one year	11,479	9,908	10,096	9,908
with original maturity of more than one year	13,436	13,267	13,309	13,267
which are unconditionally cancellable	303,223	281,392	323,993	283,382
	<u>385,552</u>	<u>366,196</u>	<u>404,939</u>	<u>368,298</u>
Credit risk weighted amount	<u>33,198</u>	<u>35,012</u>	<u>33,364</u>	<u>35,179</u>

Contingent liabilities and commitments are credit-related instruments, which include letters of credit, guarantees and commitments to extend credit. The risk involved is similar to the credit risk involved in extending loan facilities to customers. These transactions are, therefore, subject to the same credit application, portfolio maintenance and collateral requirements as for customers applying for loans. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client defaults. As the facilities may expire without being drawn upon, the contracted amounts do not represent expected future cash flows.

(b) Capital commitments

Capital commitments outstanding at 31 December in respect of fixed asset purchases not provided for in the financial statements were as follows:

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Contracted for	66	11
Authorised but not contracted for	76	12
	<u>142</u>	<u>23</u>

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

37 Contingent liabilities and commitments (continued)

(c) Lease commitments

The Bank and its subsidiaries lease a number of properties under operating leases. The leases typically run for an initial period of two to ten years, with an option to renew the lease when all terms are renegotiated. At 31 December, total future minimum lease payments under non-cancellable operating leases are payable as follows:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Within 1 year	710	692	691	671
After 1 year but within 5 years	1,433	972	1,425	962
After 5 years	931	31	931	31
	<u>3,074</u>	<u>1,695</u>	<u>3,047</u>	<u>1,664</u>

During the year HK\$707 million (2010: HK\$701 million) was recognised as an expense in the income statement in respect of operating leases. The Bank and its subsidiaries lease various premises and equipment under non-cancellable operating lease agreements.

(d) Contingencies

The Bank and its subsidiaries are named in and are defending a number of legal actions arising from its banking activities. Management of the Bank believes that the resolution of these actions and proceedings will not be material to the financial position of the Bank and its subsidiaries.

38 Risk management

The management of risk lies at the heart of the Bank's business. One of the principal risks the Bank incurs arises from extending credit to customers through its trading and lending operations. Beyond credit risk, the Bank is also exposed to a range of other risk types such as country, market, liquidity, operational, regulatory and reputational risks which are inherent to the Bank's strategy, product range and geographical coverage.

Risk management framework

Effective risk management is fundamental to being able to generate profits consistently and sustainably – and is thus a central part of the financial and operational management of the Bank.

Through its risk management framework the Bank manages enterprise-wide risks, with the objective of maximising risk-adjusted returns while remaining within its risk appetite.

As part of this framework, the Bank uses a set of principles that describe the risk management culture the Bank wishes to sustain:

- Balancing risk and reward: risk is taken in support of the requirements of the Bank's stakeholders, in line with the Bank's strategy and within its risk appetite;

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)*Risk management framework (continued)*

- Responsibility: it is the responsibility of all employees to ensure that risk-taking is disciplined and focused. The Bank takes account of its social responsibilities, and its commitment to customers in taking risk to produce a return;
- Accountability: risk is taken only within agreed authorities and where there is appropriate infrastructure and resource. All risk-taking must be transparent, controlled and reported;
- Anticipation: the Bank seeks to anticipate future risks and ensure awareness of all known risks; and
- Competitive advantage: the Bank seeks competitive advantage through efficient and effective risk management and control.

(a) Credit risk

Credit risk is the potential for loss due to the failure of a counterparty to meet its obligations to pay in accordance with agreed terms. Credit exposures may arise from both the banking and trading books.

Credit risk is managed through a framework which sets out policies and procedures covering the measurement and management of credit risk. There is a clear segregation of duties between transaction originators in the businesses and the approvers in the Risk function. All credit exposure limits are approved within a defined credit approval authority framework.

Group-wide credit policies and standards are considered and approved by the Group Risk Committee (“GRC”), which also oversees the delegation of credit approval and loan impairment provisioning authorities.

Policies and procedures specific to each business are established by authorised risk committees within Wholesale and Consumer Banking. These are consistent with the Group-wide credit policies, but are more detailed and adapted to reflect the different risk environments and portfolio characteristics.

Based on the policies and standards approved by the GRC, the Bank’s Risk Committee, which is chaired by the Country Chief Risk Officer and reporting to the Bank’s Board of Directors, is responsible for the management of all risks, excepting those for which the Asset and Liability Committee and the Pensions Executive Committee have direct responsibility. Risk limit and risk exposure delegated approval authority frameworks are approved by the Risk Committee. It also takes into account the requirements of the Hong Kong Banking Ordinance and the guidelines issued by the HKMA with respect to large exposures and provisioning requirements.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)**(a) Credit risk (continued)**

The Risk function is responsible for upholding the integrity of the Group's risk/return decisions, and in particular for ensuring that risks are properly assessed, that risk/return decisions are made transparently on the basis of this proper assessment, and are controlled in accordance with the Group's standards. The Risk function is independent of the business functions to ensure that the necessary balance in risk/return decisions is not compromised by short-term pressures to generate revenues.

Credit rating and measurement

Risk measurement plays a central role, along with judgement and experience, in informing risk-taking and portfolio management decisions. It is a primary target for sustained investment and senior management attention.

Since 1 January 2008, the Bank has used the advanced Internal Ratings Based (IRB) approach under the Basel II regulatory framework to calculate credit risk capital.

For IRB portfolios, a standard alphanumeric credit risk-grading system is used in both Wholesale and Consumer Banking. The grading is based on the Group's internal estimate of probability of default over a one year horizon, with customers or portfolios assessed against a range of quantitative and qualitative factors. The numeric grades run from 1 to 14 and each grade is sub-classified A, B or C. Lower credit grades are indicative of a lower likelihood of default. Credit grades 1A to 12C are assigned to performing customers or accounts, while credit grades 13 and 14 are assigned to non-performing or defaulted customers.

The Bank's credit grades in Wholesale Banking are not intended to replicate external credit grades, and ratings assigned by external ratings agencies are not used in determining the Bank's internal credit grades. Nonetheless, as the factors used to grade a borrower may be similar, a borrower rated poorly by an external rating agency is typically assigned a worse internal credit grade.

Advanced IRB models cover a substantial majority of the Bank's loans and are used extensively in assessing risks at customer and portfolio level, setting strategy and optimising the Bank's risk-return decisions.

IRB risk measurement models are approved by the Risk Committee, on the recommendation of the Group Model Assessment Committee ('MAC') and the Bank's MAC. The Bank's MAC supports the Risk Committee in ensuring risk identification and measurement capabilities are objective and consistent, so that risk control and risk origination decisions are properly informed. Prior to review by the MAC, all IRB models are validated in detail by a model validation team, which is separate from the teams which develop and maintain the models. Models undergo a detailed annual review. Reviews are also triggered if the performance of a model deteriorates materially against predetermined thresholds during the ongoing model performance monitoring process.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)**(a) Credit risk (continued)***Credit Approval*

The Bank has been locally incorporated since 1 July 2004. Since then, the approval process reflects that strategic decisions are being made by the Bank's personnel in accordance with their delegated authorities and the terms of reference of the appropriate committees. It is recognised that, as a major part of the Group, all significant risk decisions emanating from Hong Kong will have an impact to the Group, be it regulatory, concentration, strategic, etc. It is therefore recognised that it is essential for the Group to consider such transactions to ensure that these Group issues are included as part of the decision making process. Delegated authorities approved by the Risk Committee of the Bank are delegated to the key risk managers to ensure that all risk decisions are made within the Bank. Where proposals fall outside of the individual's authorities, the advice and guidance of the Group is sought. In such cases, the relevant Group entity, whether an individual or a committee (including but not limited to the GRC), will review the proposal from a Group perspective and give their recommendation. On receipt of such recommendation, the Bank's Excess Approval Committee, being a sub-committee of the Risk Committee, will meet to consider such advice and reach a suitable decision. All the credit applications approved by the Excess Approval Committee will be reported at each Risk Committee meeting for noting.

Concentration risk

Credit concentration risk is managed within concentration caps set by counterparty or groups of connected counterparties, by country and industry in Wholesale Banking; and tracked by product and country in Consumer Banking. Additional targets are set and monitored for concentrations by credit rating.

Credit concentrations are monitored by the Risk Committee and concentration limits that are material to the Bank are reviewed and approved at least annually by the Risk Committee.

Credit monitoring

The Bank and its subsidiaries regularly monitor credit exposures, portfolio performance, and external trends that may impact risk management outcomes.

Internal risk management reports are presented to risk committees, containing information on key environmental, political and economic trends across major portfolios and countries; portfolio delinquency and loan impairment performance; as well as IRB portfolio metrics including credit grade migration.

The Bank's Wholesale Banking Credit Issues Forum meets regularly to assess the impact of external events and trends on the Wholesale Banking credit risk portfolio and to define and implement the Bank's response in terms of appropriate changes to portfolio shape, portfolio and underwriting standards, risk policy and procedures.

Corporate accounts are placed on Early Alert when they display signs of weakness or financial deterioration, for example where there is a decline in the customer's position within the industry, a breach of covenants, non-performance of an obligation, or there are issues relating to ownership or management.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)**(a) Credit risk (continued)**

Such accounts and portfolios are subjected to a dedicated process overseen by an Early Alert Committee. Account plans are re-evaluated and remedial actions are agreed and monitored. Remedial actions include, but are not limited to, exposure reduction, security enhancement, exiting the account or immediate movement of the account into the control of Group Special Assets Management (GSAM), the Bank's specialist recovery unit.

In Consumer Banking, portfolio delinquency trends are monitored continuously at a detailed level. Individual customer behaviour is also tracked and is considered for lending decisions. Accounts which are past due are subject to a collections process, managed independently by the Risk function. Charged-off accounts are managed by a specialist recovery team.

The small and medium-sized enterprise (SME) business is managed within Consumer Banking in two distinct customer sub-segments: small businesses and medium enterprises, differentiated by the annual turnover of the counterparty. The credit processes are further refined based on exposure at risk. Larger exposures are managed through the Discretionary Lending approach, in line with Wholesale Banking procedures, and smaller exposures are managed through Programmed Lending, in line with Consumer Banking procedures. Discretionary Lending and private banking past due accounts are managed by GSAM.

Credit mitigation

Potential credit losses from any given account, customer or portfolio are mitigated using a range of tools such as collateral, credit insurance, credit derivatives and other guarantees. The reliance that can be placed on these mitigants is carefully assessed in light of issues such as legal enforceability, market value and counterparty risk of the guarantor.

Risk mitigation policies determine the eligibility of collateral types. Collateral types which are eligible for risk mitigation include: cash; residential, commercial and industrial property; fixed assets such as motor vehicles, aircraft, plant and machinery; marketable securities; commodities; bank guarantees; and letters of credit. Risk mitigation policies control the approval of collateral types.

Collateral is valued in accordance with the Group's risk mitigation policy, which prescribes the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure.

In Wholesale Banking the effectiveness of credit mitigation is ensured by policies which govern eligibility criteria such as monitoring of concentration of collateral, correlation of the collateral to underlying assets, adjustments for currency fluctuations for collateral. For all credit risk mitigation that meets the policy criteria, a clear set of procedures are applied to ensure that the value of the underlying collateral is appropriately recorded and updated regularly.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)**(a) Credit risk (continued)**

In Consumer Banking effective collateral management is used to mitigate credit risk. All eligible collateral accepted by Consumer Banking is covered by a product proposal approved by senior credit officers delegated with the relevant authority. New collateral types have to be vetted through a stringent 'New Business Approval' process and are approved in accordance with the delegated authorities within Consumer Banking Risk or by the Excess Approval Committee under advice of the Group's Consumer Banking Risk Committee as appropriate. In order to be recognized as security and for the loan to be classified as secured, all items pledged must be valued and there must exist an active secondary resale market for the collateral. Documentation must be held to enable Consumer Banking to realize the asset without the cooperation of the asset owner in the event that this is necessary. Regular valuation of collateral is required in accordance with the Group's risk mitigation policy, which prescribes both the process of valuation and the frequency of valuation for different collateral types. The valuation frequency is driven by the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure. Stress tests are performed on changes in collateral values for key portfolios to assist senior management in managing the risks in those portfolios. Physical collateral is required to be insured at all times and against all risks, with the Bank as the loss payee under the insurance policy.

Detailed procedures over collateral management must be in place for each business.

Traded Products

Credit risk from traded products is managed within the overall credit risk appetite for corporates and financial institutions.

The credit risk exposure from traded products is derived from the positive mark-to-market value of the underlying instruments, and an additional component to cater for potential market movements.

For derivative contracts, the Bank limits its exposure to credit losses in the event of default by entering into master netting agreements with certain counterparties. As required by HKAS 32/IAS 32, exposures are presented on a gross basis in the financial statements as such transactions are not intended to be settled net in the ordinary course of business.

In addition, the Bank enters into Credit Support Annexes ('CSA') with counterparties where collateral is deemed a necessary or desirable mitigant to the exposure. Under a variation margin process, additional collateral is called from the counterparty if total uncollateralised mark-to-market exposure exceeds the threshold and minimum transfer amount specified in the CSA. With certain counterparties, the CSA is reciprocal and requires the Bank to post collateral if the overall mark-to-market value of positions is in the counterparty's favour and exceeds an agreed threshold.

Securities

Within Wholesale Banking, the Excess Approval Committee under advice of the Group's Underwriting Committee (as approved by the Bank's Board) approves the portfolio limits and parameters for the underwriting and purchase of all pre-defined securities assets to be held for sale. The Underwriting Committee is established under the authority of the Risk Committee under advice of the Group. Wholesale Banking operates within set limits, which include country, single issuer, holding period and credit grade limits.

Day to day credit risk management activities for traded securities are carried out by Traded Credit Risk Management whose activities include oversight and approval within the levels delegated by the Underwriting Committee. Issuer credit risk, including settlement and pre-settlement risk, is controlled by Wholesale Banking Risk, while price risk is controlled by Group Market Risk.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)**

The Underwriting Committee approves individual proposals to underwrite new corporate security issues. Where an underwritten security is held for a period longer than the target sell-down period, the final decision on whether to sell the position rests within the Risk function.

Maximum exposure to credit risk

The maximum exposures to credit risk of on-balance sheet financial instruments, before taking account of any collateral or other credit enhancements is the carrying amount reported on the balance sheet. For off-balance sheet instruments, the maximum exposure to credit risk is the contractual nominal amounts as set out below:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>Restated</i>	<i>2011</i>	<i>Restated</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Financial guarantees and other credit related contingent liabilities	56,792	58,646	56,919	58,758
Loan commitments and other credit related commitments	25,537	26,158	24,027	26,158
	<u>82,329</u>	<u>84,804</u>	<u>80,946</u>	<u>84,916</u>

Collateral

Collateral is held to mitigate credit risk exposures and risk mitigation policies determine the eligibility of collateral types.

For certain types of lending – typically mortgages and asset financing – the right to take charge over physical assets is significant in terms of determining appropriate pricing and recoverability in the event of default.

As discussed on page 77, collateral is valued in accordance with our risk mitigation policy, which prescribes the frequency of valuation for different collateral types, based on the level of price volatility of each type of collateral and the nature of the underlying product or risk exposure. Where appropriate, collateral values are adjusted to reflect current market conditions, probability of recovery and the period of time to realise the collateral in the event of possession. The collateral values reported below reflect this conservative basis and are also adjusted for the effects of over-collateralisation.

(i) Loans and advances

The requirement for collateral is not a substitute for the ability to pay, however, which is the primary consideration for any lending decisions. In determining the financial effect of collateral held against loans neither past due nor impaired, we have assessed the significance of the collateral held in relation to the type of lending.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)***Loans neither past due nor impaired*

At 31 December 2011, the Bank and its subsidiaries have HK\$153,707 million (2010: HK\$149,202 million) of mortgage loans in Consumer Banking that are neither past due nor impaired. These are generally fully secured exposures (2010: fully secured).

In Wholesale Banking, the Bank and its subsidiaries have HK\$178,402 million (2010: HK\$142,283 million) corporate exposures that are neither past due nor impaired. 24% (2010: 22%) of these exposures are secured by tangible collaterals.

The Bank and its subsidiaries also undertake collateralised lending and borrowing (reverse repo and repo) arrangements, and the collateral held against these types of loans are set out in note 40 to the financial statements.

Non-tangible collateral – such as guarantees and letters of credit – may also be held against corporate exposures although the financial effect of this type of collateral is less significant in terms of recoveries. It is not practicable to quantify the effect of this collateral as the value of the collateral is conditional on circumstances at the time of default.

Loans past due or impaired

The fair value of collateral held against past due or impaired loans is detailed in the table below as at 31 December 2011 and 2010:

Consolidated

	2011		2010	
	<i>Advances to customers</i>	<i>Advances to banks</i>	<i>Advances to customers</i>	<i>Advances to banks</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Estimated fair value of collateral (Note):				
Held against impaired advances	249	–	116	–
Held against past due but not impaired advances	2,650	–	1,361	–
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

Bank

	2011		2010	
	<i>Advances to customers</i>	<i>Advances to banks</i>	<i>Advances to customers</i>	<i>Advances to banks</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Estimated fair value of collateral (Note):				
Held against impaired advances	249	–	105	–
Held against past due but not impaired advances	2,510	–	1,188	–
	<u> </u>	<u> </u>	<u> </u>	<u> </u>

(Note) The fair value of the collateral held represents fair value, after taking into account the effects of over-collateralisation where it is not available for offset against other loans.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)***Repossessed Collateral*

As at 31 December, the amounts of assets obtained by taking possession of collateral held as security were as follows:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Property, plant and equipment	48	41	31	38

Loan collateral acquired from borrowers due to restructuring or their inability to repay, continues to be recorded as "Advances to customers" in the balance sheet at the lower of fair value (less costs to sell) and the carrying amount of the loan (net of any impairment allowances), until the collateral is realised.

Repossessed collaterals obtained are intended to be realised in an orderly fashion to repay the impaired loans and are not held for the own use of the Bank and its subsidiaries.

(ii) Off-balance sheet exposures

For certain types of exposures such as letters of credit and guarantees, the Bank and its subsidiaries obtain collateral such as cash depending on internal credit risk assessments. However, for trade finance products such as letters of credit, the Bank and its subsidiaries will also hold legal title to the underlying assets should a default takes place.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)**Credit quality*(i) Analysis of the loan portfolio***Consolidated**

	2011		Restated 2010	
	<i>Advances to customers HK\$'M</i>	<i>Advances to banks HK\$'M</i>	<i>Advances to customers HK\$'M</i>	<i>Advances to banks HK\$'M</i>
Loans and advances				
– neither past due nor impaired	386,145	135,967	333,071	97,068
– past due but not impaired	3,781	485	1,879	36
– impaired, net of individually assessed impairment charges	391	61	377	63
Less: collectively assessed impairment charges	(554)	–	(473)	–
	<u>389,763</u>	<u>136,513</u>	<u>334,854</u>	<u>97,167</u>

Bank

	2011		2010	
	<i>Advances to customers HK\$'M</i>	<i>Advances to banks HK\$'M</i>	<i>Advances to customers HK\$'M</i>	<i>Advances to banks HK\$'M</i>
Loans and advances				
– neither past due nor impaired	374,011	135,931	324,046	96,801
– past due but not impaired	3,526	485	1,605	36
– impaired, net of individually assessed impairment charges	384	61	314	63
Less: collectively assessed impairment charges	(444)	–	(374)	–
	<u>377,477</u>	<u>136,477</u>	<u>325,591</u>	<u>96,900</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)***(i) Analysis of the loan portfolio (continued)*

The following tables set out an analysis of the internal credit gradings for advances which are not past due and for which no individual impairment provision has been raised. The credit gradings set out in the tables below are based on a probability of default measure as set out on page 75.

Consolidated

	2011		Restated 2010	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Credit grades:				
1 to 5	225,102	134,828	191,266	93,562
6 to 8	115,332	1,095	98,374	3,413
9 to 11	44,226	44	42,300	68
12	1,485	–	1,131	25
	<u>386,145</u>	<u>135,967</u>	<u>333,071</u>	<u>97,068</u>

Bank

	2011		2010	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Credit grades:				
1 to 5	223,420	134,792	191,211	93,295
6 to 8	108,114	1,095	93,035	3,413
9 to 11	41,374	44	38,911	68
12	1,103	–	889	25
	<u>374,011</u>	<u>135,931</u>	<u>324,046</u>	<u>96,801</u>

The following tables set out the ageing of advances which are past due and for which no individual impairment provision has been raised. A loan is considered to be past due when the counterparty has failed to make a principal or interest payment when contractually due. Past due does not necessarily mean that the counterparty is impaired.

Consolidated

	2011		2010	
	Advances to customers HK\$'M	Advances to banks HK\$'M	Advances to customers HK\$'M	Advances to banks HK\$'M
Past due				
– up to 30 days	3,474	485	1,651	36
– 31-60 days	176	–	109	–
– 61-90 days	55	–	58	–
– 91-120 days	13	–	34	–
– 121-150 days	63	–	27	–
	<u>3,781</u>	<u>485</u>	<u>1,879</u>	<u>36</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)***(i) Analysis of the loan portfolio (continued)***Bank**

	2011		2010	
	<i>Advances to customers</i>	<i>Advances to banks</i>	<i>Advances to customers</i>	<i>Advances to banks</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Past due				
– up to 30 days	3,274	485	1,424	36
– 31-60 days	138	–	74	–
– 61-90 days	38	–	46	–
– 91-120 days	13	–	34	–
– 121-150 days	63	–	27	–
	<u>3,526</u>	<u>485</u>	<u>1,605</u>	<u>36</u>

*(ii) Analysis of debt securities (including certificates of deposit), equity shares and treasury bills***Consolidated**

	2011			
	<i>Treasury bills</i>	<i>Debt securities</i>	<i>Equity shares</i>	<i>Total</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Impaired securities	–	44	6	50
Impairment provisions	–	(34)	(6)	(40)
Net impaired securities	–	10	–	10
Securities neither past due nor impaired	<u>48,254</u>	<u>127,412</u>	<u>427</u>	<u>176,093</u>

	2010			
	<i>Treasury bills</i>	<i>Debt securities</i>	<i>Equity shares</i>	<i>Total</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Impaired securities	–	38	6	44
Impairment provisions	–	(38)	(6)	(44)
Net impaired securities	–	–	–	–
Securities neither past due nor impaired	<u>56,063</u>	<u>135,041</u>	<u>235</u>	<u>191,339</u>

Bank

	2011			
	<i>Treasury bills</i>	<i>Debt securities</i>	<i>Equity shares</i>	<i>Total</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
Impaired securities	–	36	6	42
Impairment provisions	–	(30)	(6)	(36)
Net impaired securities	–	6	–	6
Securities neither past due nor impaired	<u>48,254</u>	<u>125,589</u>	<u>427</u>	<u>174,270</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(a) Credit risk (continued)**

- (ii) *Analysis of debt securities (including certificates of deposit), equity shares and treasury bills (continued)*

Bank (continued)

	2010			
	<i>Treasury bills</i> HK\$'M	<i>Debt securities</i> HK\$'M	<i>Equity shares</i> HK\$'M	<i>Total</i> HK\$'M
Impaired securities	–	38	6	44
Impairment provisions	–	(38)	(6)	(44)
Net impaired securities	–	–	–	–
Securities neither past due nor impaired	56,063	133,522	235	189,820

The following table analyses debt securities (including certificates of deposit) and treasury bills which are neither past due nor impaired by external credit rating. The standard credit ratings used by the Bank are those used by Standard & Poors or their equivalent. Debt securities held which have a short-term rating are reported against the long-term rating of the issuer.

Consolidated

	2011		2010	
	<i>Treasury bills</i> HK\$'M	<i>Debt securities</i> HK\$'M	<i>Treasury bills</i> HK\$'M	<i>Debt securities</i> HK\$'M
AAA	–	12,704	–	19,226
AA - to AA +	48,254	50,658	56,063	83,232
A - to A +	–	58,012	–	24,240
Lower than A-	–	890	–	750
Unrated	–	5,148	–	7,593
	48,254	127,412	56,063	135,041

Bank

	2011		2010	
	<i>Treasury bills</i> HK\$'M	<i>Debt securities</i> HK\$'M	<i>Treasury bills</i> HK\$'M	<i>Debt securities</i> HK\$'M
AAA	–	12,704	–	19,226
AA - to AA +	48,254	50,658	56,063	83,232
A - to A +	–	58,012	–	24,240
Lower than A-	–	890	–	750
Unrated	–	3,325	–	6,074
	48,254	125,589	56,063	133,522

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)

(b) Market risk management

Market risk

The Bank recognises market risk as the potential loss of earnings or economic value due to adverse changes in financial market rates or prices. The Bank's exposure to market risk arises principally from customer-driven transactions. The objective of the Bank's market risk policies and processes is to obtain the best balance of risk and return whilst meeting customers' requirements.

The Bank transacts in the money market, foreign exchange markets, equity markets, and capital markets giving rise to market risk exposures. Financial instruments transacted include debt and other securities and certain off-balance sheet ("derivatives") financial instruments. Derivatives are contracts with characteristics and value derived from underlying financial instruments, interest and exchange rates or indices. They include futures, forwards, swaps, and options transactions in the foreign exchange and interest rate markets. The Bank enters into derivative contracts in the normal course of business to meet customer demand and for hedging purposes. Derivative contracts entered into by the Bank are primarily over-the-counter derivatives which the mark-to-market values are readily determinable by reference to independent prices and valuation quotes.

The Bank has established a market risk management framework and policies, including limits setting, monitoring and reporting and control procedures, which are reviewed regularly by the Risk Committee. Market risk limits are proposed by the business within the terms of agreed policy. The Risk Committee approves the limits and Market Risk department monitors exposure against these limits and approves temporary limits within the delegated authorities. Additional limits are placed on specific instruments and position concentrations where appropriate. Sensitivity measures are used in addition to VaR as risk management tools. For example, interest rate sensitivity is measured in terms of exposure to a one basis point increase in yields.

Value at Risk

VaR, in general, is a quantitative measure of market risk that applies recent historical market conditions to estimate the potential future loss in market value that will not be exceeded in a set time period at a set statistical confidence level. VaR provides a consistent measure that can be applied across trading businesses and products over time and can be set against actual daily trading profit and loss outcome.

VaR is calculated for expected movements over a minimum of one business day and to a confidence level of 97.5 per cent. This confidence level suggests that potential daily losses, in excess of the VaR measure, are likely to be experienced six times per year.

The Bank applies two VaR methodologies, historic simulation and Monte Carlo simulation, with a historical observation period of one year. Historic simulation is applied for general market risk factors. This approach involves the revaluation of all existing positions to reflect the effect of historically observed changes in market risk factors on the valuation of the current portfolio. Monte Carlo simulation is applied for credit spread VaR. This approach is similar to historic simulation but with considerably more input risk factor observations. These are generated by random sampling techniques, but the results retain the essential variability and correlations of historically observed risk factor changes.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)

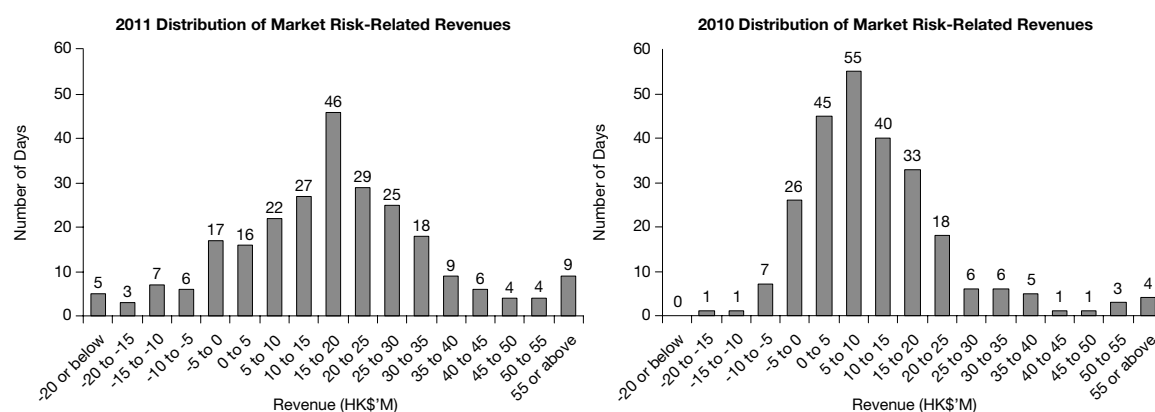
(b) Market risk management (continued)

Stress Testing

Losses beyond the confidence interval are not captured by a VaR calculation, which therefore gives no indication of the size of unexpected losses in these situations.

VaR is complemented by weekly stress testing of market risk exposures to highlight potential risk that may arise from extreme market events that are rare but plausible. Stress testing is an integral part of the market risk management framework and considers both historical market events and forward looking scenarios. A consistent stress testing methodology is applied to trading and non-trading books. The stress testing methodology assumes that scope for management action would be limited during a stress event, reflecting the decrease in liquidity that often occurs.

Stress scenarios are regularly updated to reflect changes in risk profile and economic events. The Risk Committee reviews stress test results on a regular basis. Ad hoc scenarios are also prepared reflecting specific market conditions and for particular concentrations of risk that arise within the business.



Trading and Non-trading (VaR at 97.5%, 1 day)

Value at risk (HK\$'M):	2011				2010			
	Average	High	Low	Actual*	Average	High	Low	Actual*
Interest rate risk ^	45.2	54.2	35.8	51.7	34.5	47.1	26.3	46.4
Foreign exchange risk	3.5	6.6	0.9	1.8	2.4	14.1	0.3	4.5
Total ^^	45.4	54.3	36.0	51.7	34.7	47.4	26.4	46.6

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(b) Market risk management (continued)**Trading (VaR at 97.5%, 1 day)

<i>Value at risk (HK\$'M):</i>	2011				2010			
	<i>Average</i>	<i>High</i>	<i>Low</i>	<i>Actual*</i>	<i>Average</i>	<i>High</i>	<i>Low</i>	<i>Actual*</i>
Interest rate risk	12.3	16.6	9.1	9.2	5.8	22.8	3.1	5.6
Foreign exchange risk	3.5	6.6	0.9	1.8	2.4	14.1	0.3	4.5
Total ^^	<u>13.0</u>	<u>18.6</u>	<u>9.3</u>	<u>10.1</u>	<u>6.7</u>	<u>23.8</u>	<u>3.3</u>	<u>7.8</u>

Non-trading (VaR at 97.5%, 1 day)

<i>Value at risk (HK\$'M):</i>	2011				2010			
	<i>Average</i>	<i>High</i>	<i>Low</i>	<i>Actual*</i>	<i>Average</i>	<i>High</i>	<i>Low</i>	<i>Actual*</i>
Interest rate risk ^	<u>43.4</u>	<u>52.8</u>	<u>34.0</u>	<u>50.8</u>	<u>33.9</u>	<u>46.7</u>	<u>26.0</u>	<u>46.0</u>

Average daily income earned from market risk related activities are as follows:

	2011 HK\$'M	2010 HK\$'M
Trading		
Interest rate risk	3.8	4.6
Foreign exchange risk	<u>9.8</u>	<u>7.7</u>
Total	<u>13.6</u>	<u>12.3</u>
Non-Trading		
Interest rate risk	<u>4.0</u>	<u>5.1</u>

The highest and lowest VaR are independent and usually occur on different days.

* This represents the actual one day VaR as at 31 December.

^ Interest rate risk VaR includes credit spread risk arising from securities held by ALM.

^^ The total VaR shown in the table above is not a sum of the component risks due to offsets between them.

Interest rate risk from the non-trading book portfolios is transferred to the Financial Markets' Asset and Liability Management desk ("ALM"). ALM manages these risks with oversight by the Asset and Liability Committee ("ALCO") and within limits approved by the Market Risk department. VaR and stress tests are applied to non-trading book interest rate exposures in the same way as for the Trading book.

Foreign exchange risk on the non-trading book portfolios is minimised by match funding assets and liabilities in the same currency.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(c) Foreign exchange risk**

The foreign exchange positions of the Bank and its subsidiaries arise from foreign exchange trading and commercial banking operations. Foreign exchange trading exposures are principally derived from customer driven transactions. The Market Risk department approves foreign exchange limits within delegated authorities and monitors exposures against these limits. The net option position is calculated on the basis of the delta-weighted positions of all foreign exchange option contracts.

The Bank and its subsidiaries had the following non-structural foreign currency positions which exceeded 10% of the net non-structural position in all foreign currencies:

	<i>Consolidated</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>	<i>HK\$'M</i>
US dollars exposure				
Spot assets	311,090	278,985	311,090	278,984
Spot liabilities	(262,066)	(225,106)	(262,066)	(225,106)
Forward purchases	328,649	192,556	328,649	192,556
Forward sales	(378,787)	(246,149)	(378,787)	(246,149)
Net option position	–	112	–	112
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Net (short)/long non-structural position	<u>(1,114)</u>	<u>398</u>	<u>(1,114)</u>	<u>397</u>
			<i>Consolidated and Bank</i>	
			<i>2011</i>	<i>2010</i>
			<i>HK\$'M</i>	<i>HK\$'M</i>
Chinese renminbi exposure				
Spot assets			87,053	22,165
Spot liabilities			(63,195)	(31,889)
Forward purchases			162,096	49,258
Forward sales			(185,047)	(37,053)
Net option position			–	(114)
			<u> </u>	<u> </u>
Net long non-structural position			<u>907</u>	<u>2,367</u>
			<i>Consolidated and Bank</i>	
			<i>2011</i>	<i>2010</i>
			<i>HK\$'M</i>	<i>HK\$'M</i>
Euro exposure				
Spot assets			21,046	20,068
Spot liabilities			(19,868)	(17,987)
Forward purchases			5,495	15,248
Forward sales			(6,601)	(17,297)
Net option position			–	1
			<u> </u>	<u> </u>
Net long non-structural position			<u>72</u>	<u>33</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(c) Foreign exchange risk (continued)**

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Australian dollars exposure		
Spot assets	6,800	10,621
Spot liabilities	(15,005)	(10,473)
Forward purchases	10,833	10,023
Forward sales	(2,977)	(10,541)
Net option position	—	—
	<u> </u>	<u> </u>
Net short non-structural position	<u>(349)</u>	<u>(370)</u>

The Bank and its subsidiaries had the following structural foreign currency positions which exceeded 10% of the net structural position in all foreign currencies:

	<i>Consolidated and Bank</i>	
	<i>2011</i>	<i>Restated 2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Chinese Renminbi	4,163	2,216
United Arab Emirates Dirham	531	541
Vietnamese Dong	740	581
US dollars	363	469
	<u> </u>	<u> </u>
	<u>5,797</u>	<u>3,807</u>

(d) Interest rate risk

The Bank's interest rate exposures comprise trading exposures and non-trading structural interest rate exposures. Structural interest rate risk generally arises from the differing re-pricing characteristics of commercial banking assets and liabilities.

The Bank has established principles, policies and techniques for managing interest rate risk. Interest rate risk management is governed by the ALCO.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk**

The Bank defines liquidity risk as the risk that it either does not have sufficient financial resources available to meet all its obligations and commitments as they fall due, or can only secure them at excessive cost.

The Bank has established standards, principles, policies and techniques for managing liquidity risk. Liquidity risk management is governed by the ALCO. It is the policy of the Bank to maintain adequate liquidity at all times and hence to be in a position to meet all obligations as they fall due. The tools used for the management of liquidity risk range from key balance sheet ratios and medium-term funding requirements for ensuring balance sheets are not developing structural imbalances, to short term cash flow limits, controls on borrowing in the wholesale markets and guidelines on commitments. They are supplemented by the establishment of regular stress testing of liquidity positions and a liquidity crisis contingency plan.

The Bank has significant levels of marketable securities, principally government securities and bank paper, which can be realised in the event that there is a need for liquidity in a crisis. The Bank also prescribes a liquidity stress scenario that assumes accelerated withdrawal of deposits over a period of time and needs to ensure that cash inflows exceed outflows under such scenario. The liquidity crisis management plan lays out trigger points and actions in the event of a liquidity crisis to ensure that there is an effective response by senior management in case of such an event.

Financial Markets is responsible for the day-to-day management of all the liquidity risk in the Bank, executing liquidity directives and operating within the liquidity policy and approved limits. Liquidity limits are regularly monitored by a Market Risk function that is independent from the business. Liquidity profiles are reviewed by the ALCO on a regular basis.

Customer deposits form a significant part of the Bank's overall funding. Its composition has remained relatively diversified and stable. The ALCO monitors trends in the balance sheet and ensures that any concerns that might impact the stability of these deposits are addressed effectively. The ALCO also reviews balance sheet plans to ensure that asset growth plans are matched by growth in the stable funding base. Moreover, professional markets are accessed for the purposes of providing additional funding, maintaining a presence in local money markets and optimising asset and liability maturities.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity**

The following maturity profile is based on the remaining period to the contractual maturity date as at the balance sheet date, on a discounted basis. The disclosure does not imply that the assets will be held to maturity or that the liabilities will be withdrawn on maturity.

Consolidated

	Repayable on demand HK\$'M	2011					Undated HK\$'M	Total HK\$'M
		Due within 1 month HK\$'M	Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M		
Assets								
Cash and balances with banks, central banks and other financial institutions	21,777	-	-	-	-	-	-	21,777
Placements with banks and other financial institutions	510	53,304	36,128	45,070	1,504	-	(3)	136,513
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	-	31,401	31,401
Trading assets	-	6,406	4,531	10,294	10,109	4,027	10	35,377
Financial assets designated at fair value	-	-	-	38	344	3,893	-	4,275
Advances to customers	9,476	57,041	42,141	57,247	109,954	115,038	(1,134)	389,763
Investment securities	1,827	12,021	25,611	45,430	48,144	1,640	417	135,090
Amounts due from group companies	6,519	33,642	12,287	4,984	8,051	3,005	-	68,488
Others	322	3,789	6,739	510	326	56	19,428	31,170
Total Assets	40,431	166,203	127,437	163,573	178,432	127,659	50,119	853,854
Liabilities								
Hong Kong SAR currency notes in circulation	-	-	-	-	-	-	31,401	31,401
Deposits and balances of banks and other financial institutions	11,156	3,584	256	13	720	-	-	15,729
Deposits from customers	415,667	130,939	85,872	39,022	1,422	18	-	672,940
Trading liabilities	-	23,972	109	543	13	1	-	24,638
Financial liabilities designated at fair value	-	194	1,329	1,353	611	-	-	3,487
Debt securities in issue	-	8,634	2,930	1,701	-	-	-	13,265
Amounts due to group companies	2,882	2,738	5,166	3,248	2,366	1,696	-	18,096
Subordinated liabilities	-	-	-	-	-	13,100	-	13,100
Others	5,521	3,618	8,820	2,358	27	130	223	20,697
Total Liabilities	435,226	173,679	104,482	48,238	5,159	14,945	31,624	813,353

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Consolidated (continued)**

	2011							Total
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	
Of which:								
Certificates of deposit held								
- included in Trading assets	-	52	54	1,502	412	100	-	2,120
- included in Investment securities as available-for-sale securities	-	4,532	6,861	7,979	4,415	-	-	23,787
	-	4,584	6,915	9,481	4,827	100	-	25,907
Treasury bills (including Exchange Fund Bills)								
- included in Trading assets	-	5,828	3,183	4,727	-	-	-	13,738
- included in Investment securities as available-for-sale securities	-	1,418	15,833	17,265	-	-	-	34,516
	-	7,246	19,016	21,992	-	-	-	48,254
Debt securities								
- included in Trading assets	-	280	979	3,706	9,640	3,908	-	18,513
- included in Financial assets designated at fair value	-	-	-	38	344	3,893	-	4,275
- included in Investment securities classified as:								
- available-for-sale securities	-	5,801	2,567	19,546	38,406	-	-	66,320
- loans and receivables	1,827	270	350	640	5,323	1,640	-	10,050
- included in Amounts due from immediate holding company as trading securities	-	-	-	-	2	15	-	17
- included in Amounts due from fellow subsidiaries classified as:								
- available-for-sale securities	-	-	-	-	-	2,119	-	2,119
- financial assets designated at fair value	-	-	-	-	-	221	-	221
	1,827	6,351	3,896	23,930	53,715	11,796	-	101,515

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Consolidated (continued)**

	Repayable on demand HK\$'M	Due within 1 month HK\$'M	2010 Restated				Undated HK\$'M	Total HK\$'M
			Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M		
Assets								
Cash and balances with banks, central banks and other financial institutions	29,902	-	-	-	-	-	-	29,902
Placements with banks and other financial institutions	398	58,273	19,362	18,923	213	-	(2)	97,167
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	-	31,581	31,581
Trading assets	-	8,928	11,541	12,793	11,309	4,148	-	48,719
Financial assets designated at fair value	-	-	-	-	1,713	4,847	-	6,560
Advances to customers	8,584	57,318	30,974	38,214	88,996	112,016	(1,248)	334,854
Investment securities	1,519	9,667	12,106	65,130	44,380	1,982	235	135,019
Amounts due from group companies	1,693	9,217	19,160	10,229	9,898	3,596	532	54,325
Others	201	2,924	6,562	742	520	-	9,547	20,496
Total Assets	42,297	146,327	99,705	146,031	157,029	126,589	40,645	758,623
Liabilities								
Hong Kong SAR currency notes in circulation	-	-	-	-	-	-	31,581	31,581
Deposits and balances of banks and other financial institutions	9,987	9,180	385	193	-	-	-	19,745
Deposits from customers	380,642	112,593	49,237	30,297	386	122	-	573,277
Trading liabilities	-	36,446	-	-	-	-	-	36,446
Financial liabilities designated at fair value	-	185	289	514	1,070	994	-	3,052
Amounts due to group companies	4,164	17,750	4,975	891	1,738	1,051	-	30,569
Subordinated liabilities	-	-	-	-	-	8,055	-	8,055
Others	4,822	3,558	5,557	2,770	72	59	19	16,857
Total Liabilities	399,615	179,712	60,443	34,665	3,266	10,281	31,600	719,582

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Consolidated (continued)**

	2010							Total
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	
Of which:								
Certificates of deposit held								
- included in Trading assets	-	-	-	193	53	122	-	368
- included in Investment securities as available-for-sale securities	-	795	-	12,003	2,300	-	-	15,098
	-	795	-	12,196	2,353	122	-	15,466
Treasury bills (including Exchange Fund Bills)								
- included in Trading assets	-	7,185	10,801	7,179	-	-	-	25,165
- included in Investment securities as available-for-sale securities	-	1,800	8,268	20,830	-	-	-	30,898
	-	8,985	19,069	28,009	-	-	-	56,063
Debt securities								
- included in Trading assets	-	345	350	5,162	11,042	4,019	-	20,918
- included in Financial assets designated at fair value	-	-	-	-	1,713	4,847	-	6,560
- included in Investment securities classified as:								
- available-for-sale securities	-	7,072	3,334	31,236	37,062	123	-	78,827
- loans and receivables	1,519	-	504	1,061	5,018	1,859	-	9,961
- included in Amounts due from fellow subsidiaries classified as:								
- available-for-sale securities	-	-	-	-	-	2,965	-	2,965
- financial assets designated at fair value	-	-	-	-	-	344	-	344
	1,519	7,417	4,188	37,459	54,835	14,157	-	119,575

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Bank**

	2011							Undated HK\$'M	Total HK\$'M
	Repayable on demand HK\$'M	Due within 1 month HK\$'M	Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M			
Assets									
Cash and balances with banks, central banks and other financial institutions	21,676	-	-	-	-	-	-	-	21,676
Placements with banks and other financial institutions	474	53,304	36,128	45,070	1,504	-	(3)	136,477	
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	-	31,401	31,401	
Trading assets	-	6,406	4,531	10,294	10,109	4,027	10	35,377	
Financial assets designated at fair value	-	-	-	38	344	3,893	-	4,275	
Advances to customers	9,384	56,002	40,464	54,663	106,539	111,447	(1,022)	377,477	
Investment securities	-	12,021	25,611	45,430	48,144	1,640	417	133,263	
Amounts due from group companies	6,335	43,052	16,279	6,213	11,512	3,439	-	86,830	
Others	322	3,789	6,349	404	275	56	9,808	21,003	
Total Assets	38,191	174,574	129,362	162,112	178,427	124,502	40,611	847,779	
Liabilities									
Hong Kong SAR currency notes in circulation	-	-	-	-	-	-	31,401	31,401	
Deposits and balances of banks and other financial institutions	11,156	3,484	81	13	-	-	-	14,734	
Deposits from customers	415,659	130,851	85,580	38,898	1,419	18	-	672,425	
Trading liabilities	-	23,972	109	543	13	1	-	24,638	
Financial liabilities designated at fair value	-	194	1,329	1,353	611	-	-	3,487	
Debt securities in issue	-	8,634	2,930	1,701	-	-	-	13,265	
Amounts due to group companies	3,333	3,028	6,104	1,782	1,916	1,696	-	17,859	
Subordinated liabilities	-	-	-	-	-	13,100	-	13,100	
Others	5,510	3,515	8,535	1,922	-	44	223	19,749	
Total Liabilities	435,658	173,678	104,668	46,212	3,959	14,859	31,624	810,658	

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Bank (continued)**

	2011							Total
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	
Of which:								
Certificates of deposit held								
- included in Trading assets	-	52	54	1,502	412	100	-	2,120
- included in Investment securities as available-for-sale securities	-	4,532	6,861	7,979	4,415	-	-	23,787
	-	4,584	6,915	9,481	4,827	100	-	25,907
Treasury bills (including Exchange Fund Bills)								
- included in Trading assets	-	5,828	3,183	4,727	-	-	-	13,738
- included in Investment securities as available-for-sale securities	-	1,418	15,833	17,265	-	-	-	34,516
	-	7,246	19,016	21,992	-	-	-	48,254
Debt securities								
- included in Trading assets	-	280	979	3,706	9,640	3,908	-	18,513
- included in Financial assets designated at fair value	-	-	-	38	344	3,893	-	4,275
- included in Investment securities classified as:								
- available-for-sale securities	-	5,801	2,567	19,546	38,406	-	-	66,320
- loans and receivables	-	270	350	640	5,323	1,640	-	8,223
- included in Amounts due from immediate holding company as trading securities	-	-	-	-	2	15	-	17
- included in Amounts due from fellow subsidiaries classified as:								
- available-for-sale securities	-	-	-	-	-	2,119	-	2,119
- financial assets designated at fair value	-	-	-	-	-	221	-	221
	-	6,351	3,896	23,930	53,715	11,796	-	99,688

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Bank (continued)**

	Repayable on demand HK\$'M	2010 Restated					Undated HK\$'M	Total HK\$'M
		Due within 1 month HK\$'M	Due between 1 month to 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M		
Assets								
Cash and balances with banks, central banks and other financial institutions	29,892	-	-	-	-	-	-	29,892
Placements with banks and other financial institutions	131	58,273	19,362	18,923	213	-	(2)	96,900
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	-	31,581	31,581
Trading assets	-	8,928	11,541	12,793	11,309	4,148	-	48,719
Financial assets designated at fair value	-	-	-	-	1,713	4,847	-	6,560
Advances to customers	8,536	56,994	30,496	36,458	85,779	108,476	(1,148)	325,591
Investment securities	-	9,667	12,106	65,130	44,380	1,982	235	133,500
Amounts due from group companies	1,693	9,217	27,596	10,229	9,898	3,597	359	62,589
Others	133	2,924	6,326	386	170	-	8,646	18,585
Total Assets	40,385	146,003	107,427	143,919	153,462	123,050	39,671	753,917
Liabilities								
Hong Kong SAR currency notes in circulation	-	-	-	-	-	-	31,581	31,581
Deposits and balances of banks and other financial institutions	9,987	8,653	385	11	-	-	-	19,036
Deposits from customers	380,642	112,515	48,913	30,235	386	122	-	572,813
Trading liabilities	-	36,446	-	-	-	-	-	36,446
Financial liabilities designated at fair value	-	185	289	514	1,070	994	-	3,052
Amounts due to group companies	4,118	17,569	6,284	673	848	1,051	-	30,543
Subordinated liabilities	-	-	-	-	-	8,055	-	8,055
Others	4,822	3,558	4,838	2,565	38	59	19	15,899
Total Liabilities	399,569	178,926	60,709	33,998	2,342	10,281	31,600	717,425

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)****(i) Contractual maturity (continued)****Bank (continued)**

	2010							Total
	Repayable on demand	Due within 1 month	Due between 1 month to 3 months	Due between 3 months to 1 year	Due between 1 year to 5 years	Due after 5 years	Undated	
Of which:								
Certificates of deposit held								
- included in Trading assets	-	-	-	193	53	122	-	368
- included in Investment securities as available-for-sale securities	-	795	-	12,003	2,300	-	-	15,098
	-	795	-	12,196	2,353	122	-	15,466
Treasury bills (including Exchange Fund Bills)								
- included in Trading assets	-	7,185	10,801	7,179	-	-	-	25,165
- included in Investment securities as available-for-sale securities	-	1,800	8,268	20,830	-	-	-	30,898
	-	8,985	19,069	28,009	-	-	-	56,063
Debt securities								
- included in Trading assets	-	345	350	5,162	11,042	4,019	-	20,918
- included in Financial assets designated at fair value	-	-	-	-	1,713	4,847	-	6,560
- included in Investment securities classified as:								
- available-for-sale securities	-	7,072	3,334	31,236	37,062	123	-	78,827
- loans and receivables	-	-	504	1,061	5,018	1,859	-	8,442
- included in Amounts due from fellow subsidiaries classified as:								
- available-for-sale securities	-	-	-	-	-	2,965	-	2,965
- financial assets designated at fair value	-	-	-	-	-	344	-	344
	-	7,417	4,188	37,459	54,835	14,157	-	118,056

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)**

(ii) Behavioural maturity of financial liabilities on a discounted basis

The cash flows presented in the tables above reflect the cash flows which will be contractually payable over the residual maturity of the instruments. In practice, however, liability instruments behave differently from their contractual terms and typically, short term customer accounts extend to a longer period than their contractual maturity. The Bank and its subsidiaries' expectation of when such liabilities are likely to become payable is provided in the table below. No information has been presented for financial liabilities which will become payable on their contractual due dates.

Consolidated

	2011				Total HK\$'M
	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	
Deposits and balances of banks and other financial institutions	14,996	13	720	-	15,729
Deposits from customers	132,251	118,875	421,814	-	672,940
Total	147,247	118,888	422,534	-	688,669

	2010				Total HK\$'M
	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	
Deposits and balances of banks and other financial institutions	19,025	193	527	-	19,745
Deposits from customers	90,823	86,412	396,042	-	573,277
Total	109,848	86,605	396,569	-	593,022

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)**

(ii) Behavioural maturity of financial liabilities on a discounted basis (continued)

Bank

	2011				Total HK\$'M
	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	
Deposits and balances of banks and other financial institutions	14,721	13	-	-	14,734
Deposits from customers	131,864	118,750	421,811	-	672,425
Total	146,585	118,763	421,811	-	687,159
	2010				Total HK\$'M
	Within 3 months HK\$'M	Between 3 months and 1 year HK\$'M	Between 1 year and 5 years HK\$'M	After 5 years HK\$'M	
Deposits and balances of banks and other financial institutions	19,025	11	-	-	19,036
Deposits from customers	90,421	86,352	396,040	-	572,813
Total	109,446	86,363	396,040	-	591,849

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)**

(iii) Financial liabilities excluding derivative financial instruments on an undiscounted basis

The following tables show the undiscounted cash flows by remaining contractual maturity on an undiscounted basis for the Bank's financial liabilities. The financial liability balances in the tables will not agree to the balances reported in the balance sheets as the tables incorporate all contractual cash flows, on an undiscounted basis, relating to both principal and interest payments. The cash flows presented in the tables reflect the cash flows which will be contractually payable over the residual maturity of the instruments. In practice, however, the liability instruments behave differently from their contractual terms and typically, for short term customer accounts, extend to a longer period than their contractual maturity.

Consolidated

	2011						Total HK\$'M
	Repayable on demand HK\$'M	Due within 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Undated HK\$'M	
Deposits and balances of banks and other financial institutions	11,156	3,845	13	720	–	–	15,734
Deposits from customers	415,667	217,161	39,481	1,451	18	–	673,778
Trading liabilities	–	23,137	–	–	–	–	23,137
Financial liabilities designated at fair value	–	1,593	1,336	618	–	–	3,547
Debt securities in issue	–	11,570	1,712	–	–	–	13,282
Amounts due to group companies	2,882	7,913	3,297	2,449	1,696	–	18,237
Subordinated liabilities	–	2	528	2,187	14,943	–	17,660
Others	5,521	11,589	2,358	27	130	31,624	51,249
	<u>435,226</u>	<u>276,810</u>	<u>48,725</u>	<u>7,452</u>	<u>16,787</u>	<u>31,624</u>	<u>816,624</u>
	2010						Total HK\$'M
	Repayable on demand HK\$'M	Due within 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Undated HK\$'M	
Deposits and balances of banks and other financial institutions	9,987	9,575	193	–	–	–	19,755
Deposits from customers	380,642	161,989	30,528	444	122	–	573,725
Trading liabilities	–	36,196	–	–	–	–	36,196
Financial liabilities designated at fair value	–	491	520	1,077	1,013	–	3,101
Amounts due to group companies	4,164	21,670	219	890	1,009	–	27,952
Subordinated liabilities	–	2	348	1,438	9,733	–	11,521
Others	4,822	8,594	2,770	66	16	31,600	47,868
	<u>399,615</u>	<u>238,517</u>	<u>34,578</u>	<u>3,915</u>	<u>11,893</u>	<u>31,600</u>	<u>720,118</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)**

(iii) Financial liabilities excluding derivative financial instruments on an undiscounted basis (continued)

Bank

	2011						Total HK\$'M
	Repayable on demand HK\$'M	Due within 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Undated HK\$'M	
Deposits and balances of banks and other financial institutions	11,156	3,569	13	–	–	–	14,738
Deposits from customers	415,659	216,780	39,356	1,448	18	–	673,261
Trading liabilities	–	23,137	–	–	–	–	23,137
Financial liabilities designated at fair value	–	1,593	1,336	618	–	–	3,547
Debt securities in issue	–	11,570	1,712	–	–	–	13,282
Amounts due to group companies	3,333	9,136	1,785	1,916	1,696	–	17,866
Subordinated liabilities	–	2	528	2,187	14,943	–	17,660
Others	5,510	11,204	1,922	–	44	31,624	50,304
	<u>435,658</u>	<u>276,991</u>	<u>46,652</u>	<u>6,169</u>	<u>16,701</u>	<u>31,624</u>	<u>813,795</u>
	2010						Total HK\$'M
	Repayable on demand HK\$'M	Due within 3 months HK\$'M	Due between 3 months to 1 year HK\$'M	Due between 1 year to 5 years HK\$'M	Due after 5 years HK\$'M	Undated HK\$'M	
Deposits and balances of banks and other financial institutions	9,987	9,046	12	–	–	–	19,045
Deposits from customers	380,642	161,587	30,467	442	122	–	573,260
Trading liabilities	–	36,196	–	–	–	–	36,196
Financial liabilities designated at fair value	–	491	520	1,077	1,013	–	3,101
Amounts due to group companies	4,118	22,798	–	–	1,009	–	27,925
Subordinated liabilities	–	2	348	1,438	9,733	–	11,521
Others	4,822	7,875	2,566	32	16	31,600	46,911
	<u>399,569</u>	<u>237,995</u>	<u>33,913</u>	<u>2,989</u>	<u>11,893</u>	<u>31,600</u>	<u>717,959</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(e) Liquidity risk (continued)**

(iv) Derivative financial instruments on an undiscounted basis

The following tables show the maturity of derivative financial instruments including those net settled derivative contracts in a net liability position, together with the pay leg of gross settled contracts regardless of whether the overall contract is in an asset or liability position. The receiving leg is not shown in this table and as a result the derivative amounts in this table are inflated by their exclusion.

Consolidated

	<i>Due within 3 months HK\$'M</i>	<i>Due between 3 months to 1 year HK\$'M</i>	<i>Due between 1 year to 5 years HK\$'M</i>	<i>Due after 5 years HK\$'M</i>	<i>Total HK\$'M</i>
	2011				
Derivative financial instruments	341,680	341,484	11,107	2,398	696,669
	2010				
Derivative financial instruments	223,956	172,393	13,276	2,465	412,090

Bank

	<i>Due within 3 months HK\$'M</i>	<i>Due between 3 months to 1 year HK\$'M</i>	<i>Due between 1 year to 5 years HK\$'M</i>	<i>Due after 5 years HK\$'M</i>	<i>Total HK\$'M</i>
	2011				
Derivative financial instruments	341,680	341,484	11,107	2,398	696,669
	2010				
Derivative financial instruments	223,956	172,388	13,276	2,465	412,085

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***38 Risk management (continued)****(f) Operational risk**

Operational risk is the potential for loss arising from the failure of people, process or technology or the impact of external events. We seek to minimize our exposure to operational risk, subject to cost trade-offs. Operational risk exposures are managed through a consistent set of management processes that drive risk identification, assessment, control and monitoring.

The Country Operational Risk Committee (“CORC”) has been established to supervise and direct the management of operational risks across the Bank. CORC is also responsible for ensuring adequate and appropriate policies and procedures are in place for identification, assessment, monitoring, control and reporting of operational risks.

The Risk Committee (as delegated by the Board) oversees the management of operational risks across the Bank, supported by business and functional level committees. This formal structure of governance provides the Board with confidence that operational risks are being proactively identified and effectively managed.

The Risk Committee is responsible for setting and maintaining standards for operational risk management and measurement. In addition, specialist operational risk control owners have responsibility for the management of operational risk arising from the following activities Bank-wide: legal processes, people management, technology management, vendor management, property management, security management, accounting and financial control, tax management, corporate authorities and structure and regulatory compliance. Each risk control owner is responsible for identifying risks that are material to the Bank and for maintaining an effective control environment, which includes defining appropriate policies and procedures for approval by authorized risk committees.

Wholesale Bank and Consumer Bank have independent teams to ensure operational risk is effectively managed. These units are responsible for approving operational controls, ensuring compliance with policies and procedures in the business, monitoring key operational risk exposures, and providing guidance to the respective business areas on operational risk management.

(g) Capital management

The HKMA sets and monitors capital requirements for the Bank and certain of its subsidiaries specified by the HKMA. In implementing current capital requirements, the HKMA requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank calculates its capital adequacy ratios in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance.

In addition to meeting the regulatory requirements, the Bank’s primary objectives when managing capital are to safeguard the Bank and its subsidiaries’ ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, by pricing products and services commensurately with the level of risk and by securing access to finance at a reasonable cost. The Bank actively and regularly reviews and manages its capital structure to maintain a balance between the higher shareholder returns that might otherwise be possible with greater gearing and the advantages and security afforded by a sound capital position, and makes adjustments to the capital structure in light of changes in economic conditions.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

38 Risk management (continued)

(g) Capital management (continued)

The process of allocating capital to specific operations and activities is undertaken by the Asset and Liability Committee and is reviewed regularly by the Board of Directors.

Consistent with industry practice, the Bank monitors its capital structure on the basis of the capital adequacy ratio and there have been no material changes in the Bank's policy on the management of capital during the year.

The Bank and its subsidiaries have complied with all externally imposed capital requirements throughout the years ended 31 December 2011 and 2010.

For the capital ratios as at 31 December 2011 and 2010, the Bank uses both the advanced internal ratings-based approach and standardized approach to calculate its credit risk for non-securitization exposures. The Bank adopts the internal ratings-based (securitization) approach to calculate its credit risk for securitization exposures.

For the calculation of its capital charge for market risk, the Bank uses an internal models approach for two guaranteed funds and the standardized (market risk) approach for other exposures. In addition, the Bank adopts the standardized (operational risk) approach for operational risk.

The Bank's consolidated capital as at 31 December 2011 and 2010 consists of core capital after deductions of HK\$28,612 million (2010 restated: HK\$32,216 million) and supplementary capital after deductions of HK\$11,708 million (2010: HK\$5,579 million). Supplementary capital includes subordinated debt, and collective impairment allowances for impaired assets.

39 Fair value information

(a) Financial instruments carried at fair value

Valuation of financial assets and liabilities held at fair value are subject to a review independent of the business by Valuation Control. For those financial assets and liabilities whose fair value is determined by reference to externally quoted prices or market observable pricing inputs to valuation models, an assessment is made against external market data and consensus services. Financial instruments held at fair value in the balance sheet have been classified into a valuation hierarchy that reflects the significance of the inputs used in the fair value measurements.

Valuation methodologies

The valuation hierarchy, and the types of instruments classified into each level within that hierarchy, is set out below:

	Level 1	Level 2	Level 3
Fair value determined using:	Unadjusted quoted price in an active market for identical assets and liabilities	Valuation models with directly or indirectly market observable inputs	Valuation models using significant non-market observable inputs
Types of financial assets	Actively traded government and agency securities Listed equities Quoted derivative instruments	Corporate and other government bonds and loans Over-the-counter derivatives Asset backed securities	Asset backed securities Corporate bonds and loans in illiquid markets Unlisted equities
Types of financial liabilities	Quoted derivative instruments	Structured customer deposits Over-the-counter derivatives	

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)**

The tables below show the classification of financial instruments held at fair value into the valuation hierarchy set out above as at 31 December 2011.

Consolidated	2011 HK\$'M			<i>Total</i>
	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	
Trading assets				
– Trading securities	30,410	3,971	–	34,381
– Placement with banks and other financial institutions	–	21	–	21
– Advances to customers	–	185	–	185
– Positive fair values of trading derivatives	45	745	–	790
Amounts due from immediate holding company				
– Trading debt securities	–	17	–	17
– Positive fair values of trading derivatives	6	2,563	–	2,569
– Positive fair values of hedging derivatives	–	802	–	802
Amounts due from fellow subsidiaries				
– Available-for-sale debt securities	–	–	2,119	2,119
– Debt securities designated at fair value	–	–	221	221
– Positive fair values of trading derivatives	–	103	–	103
– Positive values of hedging derivatives	–	99	–	99
Financial assets designated at fair value				
– Debt securities	–	2,659	1,616	4,275
Available-for-sale securities				
– Treasury bills (including Exchange Fund Bills)	32,341	2,175	–	34,516
– Certificates of deposit held	–	23,787	–	23,787
– Debt securities	15,757	50,563	–	66,320
– Equity shares, net of impairment	99	–	318	417
Other assets				
– Positive fair values of hedging derivatives	–	56	–	56
Total assets measured at fair value	78,658	87,746	4,274	170,678
Trading liabilities				
– Short positions in securities	23,855	–	–	23,855
– Negative fair values of trading derivatives	6	777	–	783
Financial liabilities designated at fair value				
– Structured customer deposits	–	2,615	–	2,615
– Debt securities issued	–	872	–	872
Amounts due to immediate holding company				
– Negative fair values of trading derivatives	2	3,375	–	3,377
– Negative fair values of hedging derivatives	–	1,358	–	1,358
Amounts due to fellow subsidiaries				
– Negative fair values of trading derivatives	–	12	–	12
– Negative fair values of hedging derivatives	–	16	–	16
Total liabilities measured at fair value	23,863	9,025	–	32,888

There were no significant transfers between level 1 and level 2 instruments in 2011.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)****Consolidated (continued)**

	2010 HK\$'M			Total
	Level 1	Level 2	Level 3	
Trading assets				
– Trading securities	45,175	1,276	–	46,451
– Placement with banks and other financial institutions	–	333	–	333
– Advances to customers	–	1,155	–	1,155
– Positive fair values of trading derivatives	86	694	–	780
Amounts due from immediate holding company				
– Positive fair values of trading derivatives	–	1,490	–	1,490
– Positive fair values of hedging derivatives	–	291	–	291
Amounts due from fellow subsidiaries				
– Available-for-sale debt securities	–	–	2,965	2,965
– Debt securities designated at fair value	–	–	344	344
– Positive fair values of trading derivatives	2	–	–	2
Financial assets designated at fair value				
– Debt securities	–	4,175	2,385	6,560
Available-for-sale securities				
– Treasury bills (including Exchange Fund Bills)	30,898	–	–	30,898
– Certificates of deposit held	–	15,098	–	15,098
– Debt securities	23,329	55,445	53	78,827
– Equity shares, net of impairment	11	–	224	235
Other assets				
– Positive fair values of hedging derivatives	–	1	–	1
Total assets measured at fair value	99,501	79,958	5,971	185,430
Trading liabilities				
– Short positions in securities	36,196	–	–	36,196
– Negative fair values of trading derivatives	6	244	–	250
Financial liabilities designated at fair value				
– Structured customer deposits	–	3,052	–	3,052
Amounts due to immediate holding company				
– Negative fair values of trading derivatives	1	1,665	–	1,666
– Negative fair values of hedging derivatives	–	666	–	666
Amounts due to fellow subsidiaries				
– Negative fair values of trading derivatives	–	199	–	199
– Negative fair values of hedging derivatives	–	90	–	90
Other liabilities				
– Negative fair values of hedging derivatives	–	54	–	54
Total liabilities measured at fair value	36,203	5,970	–	42,173

There were no significant transfers between level 1 and level 2 instruments in 2010.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)****Bank**

	Level 1	Level 2	2011 HK\$'M Level 3	Total
Trading assets				
– Trading securities	30,410	3,971	–	34,381
– Placement with banks and other financial institutions	–	21	–	21
– Advances to customers	–	185	–	185
– Positive fair values of trading derivatives	45	745	–	790
Amounts due from immediate holding company				
– Trading debt securities	–	17	–	17
– Positive fair values of trading derivatives	6	2,560	–	2,566
– Positive fair values of hedging derivatives	–	802	–	802
Amounts due from fellow subsidiaries				
– Available-for-sale debt securities	–	–	2,119	2,119
– Debt securities designated at fair value	–	–	221	221
– Positive fair values of trading derivatives	–	103	–	103
– Positive values of hedging derivatives	–	99	–	99
Financial assets designated at fair value				
– Debt securities	–	2,659	1,616	4,275
Available-for-sale securities				
– Treasury bills (including Exchange Fund Bills)	32,341	2,175	–	34,516
– Certificates of deposit held	–	23,787	–	23,787
– Debt securities	15,757	50,563	–	66,320
– Equity shares, net of impairment	99	–	318	417
Other assets				
– Positive fair values of hedging derivatives	–	56	–	56
Total assets measured at fair value	78,658	87,743	4,274	170,675
Trading liabilities				
– Short positions in securities	23,855	–	–	23,855
– Negative fair values of trading derivatives	6	777	–	783
Financial liabilities designated at fair value				
– Structured customer deposits	–	2,615	–	2,615
– Debt securities issued	–	872	–	872
Amounts due to immediate holding company				
– Negative fair values of trading derivatives	2	3,375	–	3,377
– Negative fair values of hedging derivatives	–	1,358	–	1,358
Amounts due to fellow subsidiaries				
– Negative fair values of trading derivatives	–	12	–	12
– Negative fair values of hedging derivatives	–	16	–	16
Total liabilities measured at fair value	23,863	9,025	–	32,888

There were no significant transfers between level 1 and level 2 instruments in 2011.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)****Bank (continued)**

	2010 HK\$'M			
	Level 1	Level 2	Level 3	Total
Trading assets				
– Trading securities	45,175	1,276	–	46,451
– Placement with banks and other financial institutions	–	333	–	333
– Advances to customers	–	1,155	–	1,155
– Positive fair values of trading derivatives	86	694	–	780
Amounts due from immediate holding company				
– Positive fair values of trading derivatives	–	1,490	–	1,490
– Positive fair values of hedging derivatives	–	291	–	291
Amounts due from fellow subsidiaries				
– Available-for-sale debt securities	–	–	2,965	2,965
– Debt securities designated at fair value	–	–	344	344
– Positive fair values of trading derivatives	2	–	–	2
Financial assets designated at fair value				
– Debt securities	–	4,175	2,385	6,560
Available-for-sale securities				
– Treasury bills (including Exchange Fund Bills)	30,898	–	–	30,898
– Certificates of deposit held	–	15,098	–	15,098
– Debt securities	23,329	55,445	53	78,827
– Equity shares, net of impairment	11	–	224	235
Other assets				
– Positive fair values of hedging derivatives	–	1	–	1
Total assets measured at fair value	99,501	79,958	5,971	185,430
Trading liabilities				
– Short positions in securities	36,196	–	–	36,196
– Negative fair values of trading derivatives	6	244	–	250
Financial liabilities designated at fair value				
– Structured customer deposits	–	3,052	–	3,052
Amounts due to immediate holding company				
– Negative fair values of trading derivatives	1	1,665	–	1,666
– Negative fair values of hedging derivatives	–	666	–	666
Amounts due to fellow subsidiaries				
– Negative fair values of trading derivatives	–	199	–	199
– Negative fair values of hedging derivatives	–	90	–	90
Other liabilities				
– Negative fair values of hedging derivatives	–	49	–	49
Total liabilities measured at fair value	36,203	5,965	–	42,168

There were no significant transfers between level 1 and level 2 instruments in 2010.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)**

The movements during the year for level 3 financial assets are as follows:

Consolidated and Bank

	2011 HK\$'M			Total level 3 assets
	<i>Financial assets designated at fair value</i>	<i>Amounts due from fellow subsidiaries</i>	<i>Available- for-sale securities</i>	
Financial assets				
At 1 January 2011	2,385	3,309	277	5,971
Total gains or losses recognised in the income statement	31	10	240	281
Total gains or losses recognised in available-for-sale investment reserve	–	13	(38)	(25)
Purchases	–	–	526	526
Sales	–	–	(491)	(491)
Settlements	(1,133)	(992)	(196)	(2,321)
Transferred into level 3	824	–	–	824
Transferred out of level 3	(491)	–	–	(491)
At 31 December 2011	<u>1,616</u>	<u>2,340</u>	<u>318</u>	<u>4,274</u>
Total gains recognised in the income statement relating to assets held at 31 December 2011	<u>6</u>	<u>18</u>	<u>–</u>	<u>24</u>
	2010 HK\$'M			
	<i>Financial assets designated at fair value</i>	<i>Amounts due from fellow subsidiaries</i>	<i>Available- for-sale securities</i>	<i>Total level 3 assets</i>
Financial assets				
At 1 January 2010	–	2,292	91	2,383
Total gains or losses recognised in the income statement	12	14	–	26
Total gains or losses recognised in available-for-sale investment reserve	–	129	(21)	108
Purchases	2,821	1,565	207	4,593
Sales	–	–	–	–
Settlements	(448)	(691)	–	(1,139)
At 31 December 2010	<u>2,385</u>	<u>3,309</u>	<u>277</u>	<u>5,971</u>
Total gains recognised in the income statement relating to assets held at 31 December 2010	<u>3</u>	<u>–</u>	<u>–</u>	<u>3</u>

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***39 Fair value information (continued)****(a) Financial instruments carried at fair value (continued)**

Sensitivities in respect of the fair values of level 3 assets are as follows:

Consolidated and Bank

	2011 HK\$'M					
	Financial instruments designated at fair value			Available-for-sale securities		
	Net exposure	Favourable changes	Unfavourable changes	Net exposure	Favourable changes	Unfavourable changes
Amounts due from fellow subsidiaries	221	222	220	2,119	2,126	2,112
Debt securities	1,616	1,631	1,601	–	–	–
Equity shares	–	–	–	318	350	286
	<u>1,837</u>	<u>1,853</u>	<u>1,821</u>	<u>2,437</u>	<u>2,476</u>	<u>2,398</u>
	2010 HK\$'M					
	Financial instruments designated at fair value			Available-for-sale securities		
	Net exposure	Favourable changes	Unfavourable changes	Net exposure	Favourable changes	Unfavourable changes
Amounts due from fellow subsidiaries	344	345	343	2,965	2,977	2,953
Debt securities	2,385	2,397	2,373	53	55	51
Equity shares	–	–	–	224	247	201
	<u>2,729</u>	<u>2,742</u>	<u>2,716</u>	<u>3,242</u>	<u>3,279</u>	<u>3,205</u>

Where the fair value of financial instruments are measured using valuation techniques that incorporate one or more significant input which are based on unobservable market data, we apply stresses on these unobservable parameter inputs. A 10 per cent increase or decrease in correlation and credit sensitivities has been used to generate a range of reasonably possible alternative valuations. As of 31 December 2011, these stresses could have increased or decreased the fair values of financial instruments designated at fair value by HK\$16 million (2010: HK\$13 million) and available-for-sale securities by HK\$39 million (2010: HK\$37 million).

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

39 Fair value information (continued)**(b) Instruments carried at amortized cost**

All financial instruments are stated at fair value or amounts not materially different from their fair value as at 31 December 2011 and 2010.

The following sets out the Bank's basis of establishing the fair value of its financial assets and liabilities which are not carried at fair value. The basis for establishing the fair value of financial assets and liabilities held at fair value and of derivatives is set out in note 2(i) and note 2(j), respectively.

Cash and balances with banks, central banks and other financial institutions

The fair value of cash and balances with banks, central banks and other financial institutions is their carrying amounts.

Placements with banks and other financial institutions

The fair value of floating rate placements and overnight deposits is their carrying amounts. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using the prevailing money market rates for debts with a similar credit risk and remaining maturity.

Advances to customers

Advances are net of provisions for impairment. The estimated fair value of advances represents the discounted amount of future cash flows expected to be received, including assumptions relating to prepayment rates and, where appropriate, credit spreads. Expected cash flows are discounted at current market rates to determine fair value.

Deposits and balances of banks, other financial institutions and customers

The estimated fair value of deposits with no stated maturity is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market prices is based on discounting cash flows using the prevailing market rates for debts with a similar credit risk and remaining maturity.

Debt securities in issue and subordinated liabilities

The aggregate fair values are calculated based on quoted market prices. For those securities where quoted market prices are not available, a discounted cash flow model is used based on a current market related yield curve appropriate for the remaining term to maturity.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***40 Assets pledged as security for liabilities**

Liabilities of the Bank amounting to HK\$24,245 million (2010: HK\$48,977 million) are secured by the deposit of assets, including assets pledged in respect of sale and repurchase agreements, to cover short positions and to facilitate settlement processes with clearing houses. The amount of assets pledged by the Bank to secure these liabilities is HK\$24,247 million (2010: HK\$48,880 million). These assets mainly comprise of debt securities and treasury bills.

In respect of reverse repurchase agreements, the fair value of collateral held by the Bank which was permitted to be sold or repledged amounted to HK\$11,397 million (2010: HK\$36,893 million). The fair value of such collateral actually sold or repledged by the Bank amounted to HK\$2,396 million (2010: HK\$12,684 million).

These transactions are conducted under terms that are usual and customary to standard lending, and stock borrowing and lending activities.

41 Material related party transactions

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Bank and its subsidiaries entered into the following material related party transactions. The transactions of the Bank are materially the same as those appearing in the consolidated financial statements in 2011 and 2010.

(a) Key management personnel remuneration

Remuneration for key management personnel, including amounts paid to the Bank's directors as disclosed in note 8 is as follows:

	<i>Consolidated</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Short-term employee benefits	91	85
Post-employment benefits	4	5
Equity compensation benefits	33	30
	<u>128</u>	<u>120</u>

Total remuneration is included in staff costs (see note 4(g)).

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(b) Credit facilities and loans to key management personnel**

During the year, the Bank provided credit facilities to key management personnel of the Bank and their close family members and companies controlled or significantly influenced by them. The credit facilities were provided in the ordinary course of business and on substantially the same terms as for comparable transactions with persons of a similar standing or, where applicable, with other employees.

	<i>Consolidated</i>	
	<i>2011</i>	<i>2010</i>
	<i>HK\$'M</i>	<i>HK\$'M</i>
Loan balances:		
At 1 January	1,240	852
	<u> </u>	<u> </u>
At 31 December	437	1,240
	<u> </u>	<u> </u>
Average balance during the year	901	827
	<u> </u>	<u> </u>
Income earned	8	9
	<u> </u>	<u> </u>

(c) Share based payments

The Group operates a number of share based payment schemes for its directors and employees. The scheme lives referred to below relate to the remaining period in which options may be granted under the scheme by the Bank and its subsidiaries' ultimate holding company Standard Chartered PLC (SC PLC).

2011 Standard Chartered Share Plan (the 2011 Plan)

The 2011 Standard Chartered Share Plan replace all the Group's existing discretionary share plan arrangements following approval by shareholders at the Group's Annual General Meeting on 5 May 2011. It is the Group's main share plan, applicable to all employees with flexibility to provide a variety of award types including performance shares, deferred awards (share or cash) and restricted shares. Performance and restricted share awards will generally be in the form of nil price options to acquire shares in SC PLC.

Performance shares

Performance shares awards vest after a three year period and are subject to Total Shareholder Return (TSR), Earnings per share (EPS) and Return on Risk Weighted Assets (RoRWA) performance measures. The weighting between the three elements is split equally (one third of the award depending each on the achievement of TSR, EPS and RoRWA, assessed independently of one another).

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

41 Material related party transactions (continued)**(c) Share based payments (continued)****Deferred share awards / Restricted shares**

Deferred share awards will be granted as restricted shares and are subject to a three-year deferral period, vesting equally one-third on each of the first, second and third anniversaries. On vesting, the awards will be adjusted for dividend equivalent payments.

Awards which are made outside of the annual performance process, as additional incentive or retention mechanisms, are provided as restricted shares under the 2011 Plan. These awards vest in equal instalments on the second and the third anniversaries of the award date.

Deferred and restricted share awards do not have any performance conditions, although the Group's claw-back policy will apply to deferred awards.

1997/2006 Restricted Share Scheme (2006 RSS)/ 2007 Supplementary Restricted Share Scheme (2007 SRSS)

The Group's previous plans for delivering restricted shares were the 2006 RSS and 2007 SRSS both now replaced by the 2011 Plan. There are still unvested and vested awards outstanding under these plans which were previously used to deliver the deferred portion of annual performance awards and as an incentive to motivate and retain high performing employees. Awards will generally be in the form of nil cost options and do not have any performance conditions. Generally deferred restricted share awards vest equally over three years and for non-deferred awards half vests two years after the date of grant and the balance after three years. No further awards will be granted under the 2006 RSS and 2007 SRSS.

2000 Executive Share Option Scheme (2000 ESOS)

The 2000 ESOS is designed to be internationally competitive and focus executive directors and their senior management teams on delivering long-term performance. An EPS performance criterion must be met before options can be exercised.

Executive share options to purchase ordinary shares in the ultimate holding company are exercisable after the third, but before the tenth anniversary of the date of grant. The exercise price per share is the share price at the date of grant and options can only be exercised if a performance condition is satisfied. No further awards may be granted to the employees of the Bank and its subsidiaries under the 2000 ESOS.

2001 Performance Share Plan (PSP)

The Group's previous plan for delivering performance shares was the PSP. Although the PSP was replaced in 2011, there are still outstanding vested and unvested awards under the plan.

Under the PSP, half the award is dependent upon TSR performance and the balance is subject to a target of defined EPS growth. Both measures use the same three-year period and are assessed independently. No PSP awards were granted in 2011 and no further awards can be granted under the plan.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)****2004 Deferred Bonus Plan**

Under the 2004 Deferred Bonus Plan, shares are conditionally awarded as part of the executive directors' annual performance award.

All Employee Sharesave Schemes (Sharesave)

Under the Sharesave schemes, employees have the choice of opening a three-year or five-year savings contract. Within a period of six months after the third or fifth anniversary, as appropriate, employees may purchase ordinary shares in the ultimate holding company. The price at which they may purchase shares is at a discount of up to 20 per cent on the share price at the date of invitation. There are no performance conditions attached to options granted under the Sharesave schemes.

2011 Standard Chartered Share Plan (the 2011 plan)**Performance Shares**

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period and the relevant performance condition applying to that portion of the award. The fair value of the TSR component is derived by discounting a third of the award that is subject to the TSR condition by the loss of expected dividends over the performance period together with the probability of meeting the TSR condition. The EPS fair value is derived by discounting one third of the award respectively by the loss of expected dividends over the performance period. The same approach is applied to calculate the RoRWA fair value for one third of the award. In respect of the EPS and RoRWA components only, the number of shares expected to vest is adjusted for actual performance when calculating the charge for the year. The same fair value is applied to awards made to both directors and employees of the Group.

<i>Grant Date</i>	<i>2011</i>	
	<i>20 September</i>	<i>6 May</i>
Share price at grant date	£13.52	£16.31
Shares granted	32,915	487,341
Vesting period (years)	3	3
Expected dividends (yield) (%)	4.0	3.7
Fair value (EPS) (£)	4.01	4.87
Fair value (RoRWA) (£)	4.01	4.87
Fair value (TSR) (£)	1.58	1.91

The expected dividend yield is based on the historical dividend yield over the three years prior to grant.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)**

A reconciliation of movements for the year to 31 December 2011 and 2010 is shown below:

	<u>2011</u>	<u>2010</u>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	–	–
Granted	520,256	–
Lapsed	(16,772)	–
Outstanding at 31 December	503,484	–
Weighted average remaining contractual life	9.45 years	–
Exercisable at 31 December	–	–

Restricted Share Awards

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period for non-deferred awards. The same fair value is applied for awards made to both the directors and employees of the Group.

<i>Grant Date</i>	<u>2011</u>		
	<i>14 December</i>	<i>20 September</i>	<i>22 June</i>
Share price at grant date	£14.35	£13.52	£15.75
Shares granted	19,642	65,422	51,941
Vesting period (years)	2/3	2/3	2/3
Expected dividends (yield) (%)	2.9	2.9	4.1
Fair value (£)	13.36	12.59	14.25

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

A reconciliation of movements for the year to 31 December 2011 and 2010 is shown below:

	<u>2011</u>	<u>2010</u>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	–	–
Granted	137,005	–
Outstanding at 31 December	137,005	–
Weighted average remaining contractual life	6.67 years	–
Exercisable at 31 December	–	–

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)****1997/2006 Restricted Share Scheme (2006 RSS)**

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period.

Grant Date	2011		2010		
	10 March	16 December	21 September	18 June	11 March
Share price at grant date	£16.82	£17.66	£19.12	£17.40	£17.40
Shares granted	1,811,942	6,899	75,121	171,601	1,346,239
Vesting period (years)	1/2/3	2/3	2/3	2/3	2/3
Expected dividends (yield) (%)	4.1	3.7	3.7	3.9	3.9
Fair value (£)	16.82/15.22	16.11	17.46	15.80	15.80

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

A reconciliation of movements for the year ended 31 December 2011 and 2010 is shown below:

	2011		2010	
	No. of shares		No. of shares	
Outstanding at 1 January	3,479,217		2,326,460	
Granted	1,811,942		1,599,860	
Additional shares for SC PLC rights issue	–		129,769	
Lapsed	(202,127)		(138,878)	
Exercised	(695,735)		(437,994)	
Outstanding at 31 December	4,393,297		3,479,217	
Weighted average remaining contractual life	5.28 years		5.53 years	
Exercisable at 31 December	665,964		249,193	

2007 Supplementary Restricted Share Scheme (2007 SRSS)

Valuation

The fair value is based on the market value less an adjustment to take into account the expected dividends over the vesting period.

Grant Date	2011		2010		
	10 March	16 December	21 September	18 June	11 March
Share price at grant date	£16.82	£17.66	£19.12	£17.40	£17.40
Shares granted	10,713	13,689	156,549	124,307	763,196
Vesting period (years)	2/3	2/3	2/3	2/3	1/2/3
Expected dividends (yield) (%)	4.1	3.7	3.7	3.9	2.7/3.9
Fair value (£)	15.22	16.11	17.46	15.80	16.93/15.80

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)**

The expected dividend yield is based on the historical dividend yield for three years prior to grant.

A reconciliation of movements for the year to 31 December 2011 and 2010 is shown below:

	<u>2011</u>	<u>2010</u>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	2,516,214	1,551,151
Granted	10,713	1,057,741
Additional shares for SC PLC rights issue	–	92,352
Lapsed	(20,827)	(87,493)
Exercised	(980,904)	(97,537)
Outstanding at 31 December	1,525,196	2,516,214
Weighted average remaining contractual life	4.8 years	5.7 years
Exercisable at 31 December	602,907	41,929

2000 Executive Share Option Scheme (2000 ESOS)

No share awards were granted in 2011 and 2010.

A reconciliation of option movements for the year ended 31 December 2011 and 2010 is shown below:

	<u>2011</u>		<u>2010</u>	
	<i>No. of shares</i>	<i>Weighted average exercise price</i>	<i>No. of shares</i>	<i>Weighted average exercise price</i>
Outstanding at 1 January	728,821	£6.59	1,239,834	£7.15
Additional Shares for SC PLC rights issue	–	–	27,030	£6.61
Lapsed	–	–	(70,488)	£7.62
Exercised	(187,395)	£6.16	(467,555)	£7.55
Outstanding at 31 December	541,426	£6.74	728,821	£6.59
Exercisable at 31 December	541,426	£6.74	728,821	£6.59

<i>Range of exercise price</i>	<u>2011</u>			<u>2010</u>		
	<i>Weighted average exercise price</i>	<i>No. of shares</i>	<i>Weighted average remaining contractual life</i>	<i>Weighted average exercise price</i>	<i>No. of shares</i>	<i>Weighted average remaining contractual life</i>
£5.82/£7.89						
(2010: £5.82/£7.89)	£6.74	541,426	1.07	£6.59	728,821	1.82

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)****2001 Performance Share Plan (PSP)**

Valuation

The fair value is based on the same principles as the TSR and EPS element of performance shares granted under the 2011 Plan with half the awards subject to the TSR valuation and the balance subject to the EPS valuation.

<i>Grant Date</i>	<i>2010</i>	
	<i>21 September</i>	<i>11 March</i>
Share price at grant date	£19.12	£17.40
Shares granted	3,922	119,376
Vesting period (years)	3	3
Expected dividends (yield) (%)	3.76	3.51
Fair value (EPS) (£)	8.55	7.85
Fair value (TSR) (£)	3.36	3.08

The expected dividend yield is based on the historical dividend yield over the three years prior to grant.

A reconciliation of movements for the year ended 31 December 2011 and 2010 is shown below:

	<i>2011</i>	<i>2010</i>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	889,647	963,140
Granted	–	123,298
Additional shares for SC PLC rights issue	–	33,023
Lapsed	(87,807)	(110,001)
Exercised	(153,787)	(119,813)
Outstanding at 31 December	648,053	889,647
Weighted average remaining contractual life	7.05 years	7.66 years
Exercisable at 31 December	113,877	157,446

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)****2004 Deferred Bonus Plan**

Under this plan, shares are issued directly to participants upon vesting.

A reconciliation of share movements for the year ended 31 December 2011 and 2010 is shown below:

	<u>2011</u>	<u>2010</u>
	<i>No. of shares</i>	<i>No. of shares</i>
Outstanding at 1 January	12,649	–
Shares awarded	–	12,187
Rights issue	–	462
Shares exercised	(12,649)	–
Outstanding at 31 December	–	12,649

Notes:

- The market value of Standard Chartered PLC shares on the date of awards (8 March 2011) was £16.8 (9 March 2010: £17.19).
- The shares vest one year after the date of award.
- A notional scrip dividend accrues on the shares held in the Trust. The dividend is normally delivered in the form of shares and is released on vesting.

Sharesave

Valuation

Options are valued using a binomial option-pricing model. The fair value per option granted and the assumptions used in the calculation are as follows:

	<u>2011</u>	<u>2010</u>
<i>Grant Date</i>	<i>11 October</i>	<i>11 October</i>
Share price at grant date	£14.11	£18.70
Exercise price	£10.65	£15.19 ⁽¹⁾
Shares granted	493,772	342,820
Vesting period (years)	3/5	3/5
Expected volatility (%)	45.8-53.8	46-56
Expected option life (years)	3.33-5.33	3.33-5.33
Risk free rate (%)	0.9-1.4	0.9-1.6
Expected dividends (yield) (%)	3.5-3.9	3.5-3.8
Fair value (£)	5.39-5.46	7.0-7.2

¹ The Exercise Price detailed above was pre the 2010 rights issue and was subsequently adjusted to £14.632.

The expected volatility is based on historical volatility over the last three to five years or three to five years prior to grant. The expected life is the average expected period to exercise. The risk free rate of return is the yield on zero-coupon UK Government bonds of a term consistent with the assumed option life. The expected dividend yield is based on historical dividend yield for three years prior to grant. Where two amounts are shown for volatility, risk free rates, expected dividend yield and fair values, the first relates to a three years vesting period and the second to a five years vesting period.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(c) Share based payments (continued)**

A reconciliation of option movements for the year ended 31 December 2011 and 2010 is shown below:

	2011		2010	
	No. of shares	Weighted average exercise price	No. of shares	Weighted average exercise price
Outstanding at 1 January	1,626,299	£11.50	2,164,679	£10.37
Granted	493,772	£10.65	342,820	£15.19
Additional shares for SC PLC rights issue	–	–	67,368	£11.37
Lapsed	(199,673)	£11.29	(619,253)	£9.21
Exercised	(216,409)	£9.92	(329,315)	£9.85
Outstanding at 31 December	1,703,989	£11.48	1,626,299	£11.50
Exercisable at 31 December	114,945	£9.65	154,877	£10.20

Range of exercise price	2011			2010		
	Weighted average exercise price	No. of shares	Weighted average remaining contractual life	Weighted average exercise price	No. of shares	Weighted average remaining contractual life
£8.32/£14.63						
(2010: £8.32/£14.63)	£11.48	1,703,989	2.3 years	£11.50	1,626,299	2.44 years

(d) Loans to officers

Loans to officers of the Bank disclosed pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	2011	2010
	HK\$'M	HK\$'M
Aggregate amount of relevant loans by the Bank outstanding at 31 December	101	105
Maximum aggregate amount of relevant loans by the Bank outstanding during the year	113	113

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***41 Material related party transactions (continued)****(e) Related party transactions with associates and joint ventures of the Group**

During the year, the Bank and its subsidiaries entered into transactions with associates and joint ventures of the Group in the ordinary course of its banking business. The amounts of material transactions during the year are set out below:

	<i>2011</i>	<i>Restated</i>
	<i>HK\$'M</i>	<i>2010</i>
		<i>HK\$'M</i>
Amounts due from associates and joint ventures	1,632	362
Deposits from associates and joint ventures	312	246
Interest income	1	1

42 Ultimate holding company

The Bank's ultimate holding company is Standard Chartered PLC, a company registered in England and Wales. Standard Chartered PLC has listings on the London Stock Exchange and the Stock Exchange of Hong Kong. In addition, Standard Chartered PLC is also listed on the Bombay and National stock exchanges of India in a form of Indian Depository Receipts.

43 Significant accounting estimates and judgements

In determining the carrying amounts of certain assets and liabilities, the Bank and its subsidiaries make assumptions about the effects of uncertain future events on those assets and liabilities at the balance sheet date. These estimations and assumptions are based on historical experience and expectation of future events and are reviewed periodically as actual results may differ from these estimates.

Pensions

Actuarial assumptions are made in valuing future defined pension obligations as set out in note 31 and are updated periodically.

Taxes

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. Deferred tax liabilities are recognised on all temporary differences and deferred tax assets are recognised on temporary differences where it is probable that there will be taxable revenue against which these can be offset. Management has made judgements as to the probability of future taxable revenues being generated against which tax losses will be available for offset.

Fair value of financial instruments

Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable willing parties in an arm's length transaction. Notes 2(i) and 39 provide further information on the Bank's fair value accounting policy and process.

Notes to the financial statements (continued)

(Expressed in millions of Hong Kong dollars)

43 Significant accounting estimates and judgements (continued)*Impairment of financial assets*

Policies on impairment of financial assets are set out in note 2(k).

Goodwill impairment

An annual assessment is made, as set out in note 22, as to whether the current carrying value of goodwill is impaired.

44 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting period ended 31 December 2011

Up to the date of issue of the financial statements, the HKICPA/IASB has issued a number of amendments, new standards and interpretations which are not yet effective for the accounting year ended 31 December 2011 and which have not been adopted in these financial statements.

These include:

- Amendments to HKFRS 7/IFRS 7, *Financial instruments: Disclosures – Transfers of financial assets*
- Amendments to HKAS 12/IAS 12, *Income taxes – Deferred tax: Recovery of underlying assets*
- Amendments to HKAS 1/IAS 1, *Presentation of financial statements – Presentation of items of other comprehensive income*
- HKFRS 9/IFRS 9, *Financial instruments*
- HKFRS 10/IFRS 10, *Consolidated financial statements*
- HKFRS 11/IFRS 11, *Joint arrangements*
- HKFRS 12/IFRS 12, *Disclosure of interests in other entities*
- HKFRS 13/IFRS 13, *Fair value measurement*
- HKAS 27/IAS 27, *Separate financial statements (2011)*
- HKAS 28/IAS 28, *Investments in associates and joint ventures*
- Revised HKAS 19/IAS 19, *Employee benefits*

The Bank and its subsidiaries are in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. So far it has concluded that the adoption of these standards is unlikely to have a significant impact on the Bank and its subsidiaries' results of operations and financial position except for HKFRS 9/IFRS 9, *Financial instruments*, which may have an impact on the Bank and its subsidiaries' results and financial position arising from changes in the Bank and its subsidiaries' classification and measurement of financial instruments.

Notes to the financial statements (continued)*(Expressed in millions of Hong Kong dollars)***45 Restatement of prior periods***Acquisitions*

Provisional balances relating to the acquisition of the personal loan portfolios and the consumer finance businesses of GE Capital Trade Services Limited and GE Capital (Hong Kong) Limited (“GECHK”) by Prime Credit Limited (“PCL”) in 2010 have been finalized. As a result, the fair value of the advances to customers has been revised by HK\$4 million. Goodwill at acquisition has been restated to HK\$20 million. In accordance with HKFRS 3/IFRS 3 ‘Business Combinations’, the adjustments to the provisional amounts have been made as at the date of acquisitions and the 2010 consolidated balance sheet amounts were restated as follows:-

	<i>As reported at 2010</i> <i>HK\$'M</i>	<i>Adjustment</i> <i>HK\$'M</i>	<i>Restated at 2010</i> <i>HK\$'M</i>
Advances to customers	334,850	4	334,854
Goodwill and intangible assets	1,725	(4)	1,721

Comparative figures

Certain comparative figures have been restated to conform with the current year’s presentation.

Unaudited supplementary financial information

Disclosure on Remuneration for CG-5 Guideline on a Sound Remuneration System issued by the HKMA

Pursuant to section 3 of CG-5 on Guideline on a Sound Remuneration System of the Supervisory Policy manual issued by the Hong Kong Monetary Authority and the Pillar 3 disclosure requirements for remuneration by the Basel Committee on Banking Supervisor, the following disclosures are made:

- a) Information relating to the governance structure of the remuneration system
- b) Information relating to the design and structure of the remuneration processes
- c) Description of the ways in which current and future risks are taken into account in the remuneration processes
- d) Description of the ways in which the Bank seeks to link performance during a performance measurement period with levels of remuneration
- e) Description of the ways in which the Bank seeks to adjust remuneration to take account of longer-term performance
- f) Description of the different forms of variable remuneration that the Bank utilizes and the rationale for using these different forms
- g) Number of meetings held by the Board Remuneration Committee during the financial year and remuneration paid to the members

The Bank adopts the remuneration policy and systems of Standard Chartered PLC. Please refer to the Directors' Remuneration Report in the Annual Report of Standard Chartered PLC for details of the Board Remuneration Committee, the major characteristics of the remuneration system, and how risks are taken into account in the remuneration processes.

- h) Aggregate quantitative information on remuneration for senior management and Key Personnel (note 1) for the year ended 31 December 2011 and 31 December 2010 are as follows:

	2011				2010	
	Senior Management		Key Personnel		Senior Management and Key Personnel	
	Amount (HK\$'000)	Number of Beneficiaries	Amount (HK\$'000)	Number of Beneficiaries	Amount (HK\$'000)	Number of Beneficiaries
Total amount of outstanding deferred remuneration:						
• Vested	12,584	7	1,467	4	4,985	9
• Unvested	42,785	7	14,433	4	42,134	10
Total	55,369		15,900		47,119	
Total amount of outstanding deferred remuneration:						
• Shares and share-linked instruments	55,369	7	15,900	4	47,119	10

Unaudited supplementary financial information (continued)**Disclosure on Remuneration for CG-5 Guideline on a Sound Remuneration System issued by the HKMA (continued)**

	2011				2010	
	Senior Management		Key Personnel		Senior Management and Key Personnel	
	Amount (HK\$'000)	Number of Beneficiaries	Amount (HK\$'000)	Number of Beneficiaries	Amount (HK\$'000)	Number of Beneficiaries
Total amount of deferred remuneration:						
• Awarded	19,914	7	10,958	4	21,402	10
• Paid out	(12,257)	6	(1,651)	3	(12,140)	5
• Reduced through performance adjustments	(2,268)	7	–	–	(1,266)	8
Fixed remuneration:						
• Cash-based	17,761	7	8,782	4	20,668	10
Variable remuneration:						
• Cash-based	13,508	7	4,150	2	24,184	10
• Shares and share-linked instruments	19,914	7	10,958	4	21,402	10
Total	<u>33,422</u>		<u>15,108</u>		<u>45,586</u>	
Total amount of outstanding deferred remuneration and retained remuneration exposed to ex post explicit and / or implicit adjustments (note 2)	42,785	7	14,433	4	42,134	10
Total amount of reductions during the financial year:						
• due to ex post explicit adjustments	(2,268)	7	–	–	(1,266)	8
• due to ex post implicit adjustments	(10,062)	7	(3,132)	4	–	–

In 2011, there was one case of guaranteed bonus being paid to senior management or Key Personnel which amounted to HK\$11,672,579 (2010: Nil).

No senior management or Key Personnel were awarded with sign-on awards or severance payments in 2011 (2010: Nil).

Note 1: As defined in the CG5 on Guideline on a Sound Remuneration System issued by the HKMA, senior management are those who are responsible for oversight of either the Bank's company-wide strategy or activities or those of the Bank's material business lines. Key Personnel are individual employees whose duties or activities in the course of their employment involve the assumption of material risk or the taking on of material exposures on behalf of the Bank.

Note 2: Ex post adjustments are related to adjustments made after the awards are granted.