

HSBC remuneration practices and governance

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Introduction

Our pay strategy is designed to reward competitively the achievement of long-term sustainable performance and attract and motivate the very best people, regardless of gender, ethnicity, age, disability or any other factor unrelated to performance or experience with the Group, while performing their role in the long-term interests of our stakeholders.

To achieve this objective, we believe that effective governance of our remuneration practices is a key requirement. The design and implementation of remuneration policies are overseen by the Group Remuneration Committee to ensure what we pay our people is aligned to our business performance and strategy. Performance is judged not only on what is achieved over the period but more importantly on how it is achieved, as we believe the latter contributes to the long-term sustainability of the business.

Total compensation (fixed pay and variable pay) is the key focus of our remuneration framework, with variable pay (namely annual incentive and long-term incentives) differentiated by performance and adherence to HSBC values.

Our remuneration strategy is delivered through HSBC's reward package, consisting of five key elements:

Key elements	Purpose
Fixed pay	◆ Attract and retain employees by paying market competitive pay for the role, skills and experience required for the business. ◆ This may include salary, fixed pay allowance, cash in lieu of pension and other cash allowances in accordance with local market practices. ◆ These payments are fixed and do not vary with performance.
Benefits	◆ Ensure market competitiveness and provide benefits in accordance with local market practice. ◆ This may include, but not limited to, the provision of pensions, medical insurance, life insurance, health assessment and relocation allowances.
Annual incentive	◆ Drive and reward performance based on annual financial and non-financial measures consistent with the medium- to long-term strategy, stakeholder interests and adherence to HSBC values. ◆ Awards vary with performance achievement and we have the discretion to assess the extent to which performance has been achieved. ◆ Awards can be in the form of cash and/or shares. A portion of the annual incentive award may be deferred and vests over a period of three years, five years or seven years. All deferred awards are subject to malus. ◆ Share-based awards are subject to a retention period of up to one year after vesting. ◆ Awards granted to employees identified as material risk takers ('MRTs') are subject to clawback.

Key elements	Purpose
Long-term incentive awards ('LTI')	◆ Incentivise sustainable long-term performance through the use of both pre- and post-grant performance measures. ◆ Awards are subject to malus and clawback and we have the discretion to assess the extent to which performance has been achieved. ◆ Awards are in shares and subject to a three-year performance period. At the end of the performance period, the awards that vest will be dependent on the outcome of the performance condition. The vesting for executive Directors is in five equal annual installments with the first vesting occurring on the third anniversary of the grant date and the final vesting occurring on the seventh anniversary of the grant. ◆ LTI awards are subject to a retention period of up to one-year after vesting.
Shareholding requirement	◆ Align interests of senior management with shareholders' interests through a shareholding requirement during their employment at HSBC.

Governance framework and oversight

The Group Remuneration Committee ('the Committee') oversees the Group's reward policy and its application to Group businesses and functions. All members of the Committee are independent non-executive Directors of HSBC Holdings plc.

The Committee is responsible for:

- ◆ Reviewing and approving the principles, parameters and governance framework of the Group's remuneration framework applicable to all Group employees;
- ◆ Setting the Directors' Remuneration Policy and remuneration for non-executive and executive Directors, and approving the remuneration for other Senior Executives of the Group;
- ◆ Reviewing and satisfying itself that the remuneration structure for MRTs is in accordance with prevailing regulatory requirements;
- ◆ Ensuring that remuneration for employees in Risk and Compliance functions is determined independently of other business areas;
- ◆ Ensuring that no executive Director or member of senior management is involved in deciding their own remuneration;
- ◆ Reviewing any matters relating to remuneration that need to be reported to shareholders, regulators and others; and
- ◆ Assessing that there are effective safeguards in place to ensure that remuneration practices are clearly aligned with the Group's risk appetite and the regulatory and other legislative requirements that the Group is required to comply with.

To ensure the alignment of remuneration and risk:

- ◆ The Group Chief Risk Officer attends all Committee meetings to inform the Committee of risk related issues across the Group so they are considered by the Committee in applying the remuneration framework and making remuneration decisions. The Group Chief Risk Officer also updates the Committee on the Group's performance against the Risk Appetite Statement ('RAS'), which describes and measures the amount and types of risk that HSBC is prepared to take in executing its strategy. The Committee uses these updates in applying the remuneration policy and considering the risk related adjustments made to the variable pay pool, to ensure that return, risk and remuneration are aligned.
- ◆ The Committee consults with the Group Risk Committee ('GRC') on the alignment of risk and remuneration and on risk adjustments to be applied in setting annual variable pay pool.
- ◆ The Financial System Vulnerabilities Committee ('FSVC') provide input to the Committee's decision of any adjustment for risks that are under the FSVC's oversight.
- ◆ The Committee also considers material issues raised by the Group Audit Committee ('GAC') resulting from the work of Internal Audit, including communication of relevant internal audit findings on remuneration matters. The Committee provides feedback to the GAC on these matters.

The Committee reviews its terms of reference annually and its own effectiveness as well as the quality of information it receives and recommends any necessary change. A copy of the terms of reference is available on our website: <https://www.hsbc.com/our-approach/corporate-governance/board-committees>

Remuneration practices promoting sound and effective risk management and supporting our business objectives

Under our remuneration framework, remuneration decisions are made based on a combination of:

- ◆ Business results, including performance against strategic objectives and metrics in the Group RAS. This statement is a formal written articulation of the aggregate level and types of risks that the bank is willing to accept in its business activities in order to achieve its medium to long-term strategic objectives;
- ◆ Performance against Group's strategic objectives set out in performance scorecards. Core aspects of the RAS are also incorporated into the scorecards of executive Directors and Group Management Board ('GMB') and cascaded to global business lines and regions;
- ◆ Adherence to the HSBC values, business principles, Group risk-related policies and procedures and Global Standards. Risk objectives are included into the performance scorecard of senior management and there is a mandatory global risk objective applied for all employees below the GMB in order to highlight the importance of managing risk and ensure its consistent reinforcement;
- ◆ Individual performance; and
- ◆ Local market position and practice.

The key features of our remuneration framework that enable us to achieve alignment between risk, performance and reward are summarised below. Further details can be found in the HSBC Holdings plc *Annual Report and Accounts*:

Scorecards	◆ Assessment of performance with reference to clear and relevant objectives set within a performance scorecard framework. ◆ Global Standards including risk and compliance measures set at a minimum of 25% of the scorecard for GMB members.
Group variable pay pool calculation	◆ Fines and penalties are automatically included in the Committee's definition of profit. ◆ Performance against metrics in the Group RAS and conduct framework is taken into consideration.
Deferral of variable pay	◆ A Group-wide deferral approach is applicable to all employees across the Group, where deferral is applied to annual incentive award above a certain level. ◆ Deferral of variable pay into HSBC shares and/or other instruments to tie recipients to the future performance of the Group and business units.
Malus/adjustment policy	◆ Allows cancellation/reduction of unvested deferred variable pay awards. Longer deferral period for MRTs under the UK's Prudential Regulation Authority's ('PRA') Remuneration Rules increases the time period over which malus can be applied. ◆ This is in addition to in-year variable pay adjustments and other disciplinary actions that can be taken.
Clawback policy	◆ Subject to compliance with local labour laws, clawback can be applied to vested or paid awards granted to MRTs on or after 1 January 2015 for a period of seven years. ◆ This can be extended to 10 years for individuals in PRA designated Senior Management Function roles.
Sales incentives	◆ We generally do not operate commission-based sales plans.

The following programmes help to embed values in our remuneration structure and ensure greater global consistency in our approach to achieving alignment between risk and reward:

Behavioural rating for all employees	◆ Subject to compliance with local labour laws, employees receive a behaviour rating based on their adherence to HSBC values to ensure performance is judged not only on what is achieved, but also on how it is achieved.
Performance Management	◆ Performance objectives define what you need to achieve, how and by when. Creating performance objectives is a key part of Everyday Performance and Development, enabling employees and managers to agree actions and targets in line with business and role priorities. They should be updated throughout the year as priorities change. ◆ Everyday Performance and Development involves frequent, holistic and meaningful conversations throughout the year between a manager and employee. They provide an opportunity to discuss progress, provide feedback and recognition, identify any support that may be needed and address any issues that could be affecting the employee's sense of well-being.
Employee Recognition and Conduct framework	◆ The framework provides a set of guidelines designed to reward exceptional conduct and handle any conduct breaches consistently across the Group. ◆ Rewarding positive conduct may take the form of use of our global recognition programme 'At Our Best', or via positive adjustments to performance and behaviour ratings and variable pay. ◆ The framework also provides guidance on applying negative adjustments to performance and behavior ratings and to variable pay, alongside disciplinary sanctions, where conduct breaches have been identified.

Prudential Regulation Authority's Remuneration Rules

The table below sets out how our remuneration practice and governance framework complies with the requirements of PRA's Remuneration Rules. Further details are provided in our Pillar 3 Remuneration disclosures within our Annual Report and Accounts (Directors' Remuneration Report): <https://www.hsbc.com/investors/results-and-announcements/annual-report>.

Remuneration principles	How we comply
Principle 1: Remuneration policy promotes sound and effective risk management	◆ Performance scorecards of GMB align business objectives and risk objectives and cascaded to global business lines and regions. ◆ Risk and compliance is a critical part of the performance rating and variable pay assessment process. ◆ Material Risk Takers ('MRT') are identified based on the qualitative and quantitative criteria set out in the Regulatory Technical Standard ('RTS') EU 604/2014.
Principle 2: Remuneration policy supports business strategy, objectives, values and long-term interests of the firm	◆ Remuneration decisions based on a combination of performance against business objectives and general individual performance of the role. ◆ Adherence to the HSBC values, business principles, Group risk-related policies and procedures and Global Standards are key considerations taken into account for determining variable pay awards.
Principle 3: Remuneration policy includes measures to avoid conflicts of interest	◆ All variable pay and incentive schemes are required to adhere to a set of policy principles and require approval of Finance, Risk, Legal, Compliance and HR Functions. ◆ No executive Director or member of GMB is involved in deciding their own remuneration. ◆ The Committee is responsible for agreeing individual remuneration packages (including variable pay awards) for executive Directors, Group Managing Directors and other senior Group employees, including the heads of control functions.
Principle 4: Governance of remuneration policy and oversight of policy implementation	◆ All members of the Committee are independent non-executive Directors. ◆ The Committee sets the principles, parameters and governance framework of the Group's remuneration policy applicable to all Group employees. ◆ The Committee periodically reviews the adequacy and effectiveness of the Group's remuneration policy. ◆ The Group Chief Risk Officer updates the Committee and informs the Committee of risk related incidents and performance against risk appetite for the purpose of making remuneration decisions. ◆ The Group Head of Financial Crime Risk, Group Head of Audit and Group Head of Operational Risk provide inputs to the Committee for remuneration decisions related to risk/audit incidents. ◆ The GRC, GAC and FSVC updates the Committee on issues which may impact the variable pay recommendations for senior management prior to the Committee's approval as part of the Group's governance.

Remuneration principles	How we comply
Principle 5: Employees in control functions are independent, have appropriate authority and are remunerated adequately and based on functional objectives	◆ Individuals in control functions have a direct reporting line through the functions rather than through the business to ensure conflicts of interest are avoided. ◆ Control functions are represented at the most senior levels within the Group, including on the GMB. ◆ Senior individuals in control functions, including Group Chief Risk Officer, provide inputs for remuneration decisions, specifically in relation to individuals involved in any Group-wide notable events. ◆ The performance and remuneration of control function staff is determined according to a balanced scorecard of objectives specific to the functional role they undertake. ◆ Remuneration for control function staff is carefully benchmarked with the market and internally to ensure that it is set at an appropriate level. ◆ The Committee is responsible for agreeing individual remuneration packages (including variable pay awards) for the heads of control functions.
Principle 6: Total variable remuneration does not limit the firm's ability to strengthen its capital base	◆ Group's variable pay pool is determined based on evaluation of financial performance and performance against risk metrics in the RAS. ◆ Funding of the Group's variable pay pool is sized in relation to overall Group performance, Global Business performance, performance against the RAS, market benchmarks and overall affordability. Capital strength and shareholder returns are also taken into account. ◆ The Group's target policy is for the vast majority of post-tax profit to be allocated to capital and to shareholders. ◆ All deferred awards are subject to malus (awards made to MRTs are also subject to clawback provisions) and therefore can be reduced, cancelled or paid back in appropriate circumstances including (but not limited to): • Individual or business unit conduct is considered detrimental; • Restatement, correction or amendment of any financial statements; • Past performance being materially worse than originally understood; and/or • Improper or inadequate risk management.
Principle 7: Limitation and restructuring of variable remuneration and ban on variable remuneration for firms benefiting from exceptional government intervention	◆ In the event that the Group received exceptional government intervention it would apply this principle.
Principle 8: Variable pay components or pools determined based on profits and adjustment for all types of current and future risks	◆ Group's variable pay pool is determined in the context of Group profitability. ◆ Profit measures used to determine variable pay pool is adjusted for appropriate current and future risks. The Committee also takes into consideration the Prudential Valuation Adjustment ('PVA') in determining the variable pay pool. ◆ The Committee exercises its judgement to ensure the variable pay pool reflects the overall performance of the Group including performance against qualitative risk objectives.

Remuneration principles	How we comply
Principle 9: Pension policy is in line with business strategy, objectives, values and long-term interests and discretionary pension benefits are in the form of shares or other instruments	◆ Group pensions policies are reviewed to ensure they are in line with market practice and sustainable. ◆ The Group policy is not to award any discretionary pension benefits.
Principle 10: Employees undertake not to use personal investment strategies to undermine the risk alignment effects of remuneration arrangements	◆ Our policy requires employees not to use personal hedging strategies or remuneration or liability related contracts of insurance in connection with any unvested deferred remuneration awards or any vested awards subject to a retention period.
Principle 11: Variable remuneration is not paid through vehicles that facilitate non-compliance with the Remuneration Rules	◆ The PRA and the Financial Conduct Authority ('FCA') Remuneration Rules are applied on a Group-wide basis. ◆ All variable pay awards are currently delivered in the form of cash or shares/share-linked instruments in accordance with the requirements of the PRA Remuneration Rules.
Principle 12: Remuneration structure is consistent with and complies with the PRA/FCA Remuneration Rules	◆ For all employees, remuneration decisions are based on a combination of business results, performance against objectives set out in performance scorecards, general individual performance of the role and adherence to the HSBC values, business principles, Group risk-related policies and procedures and Global Standards. ◆ Guaranteed bonuses are paid exceptionally and limited to the first year of employment. ◆ Buy-out awards may be offered if an individual holds any outstanding unvested awards that are forfeited on resignation from the previous employer. The terms of the buy-out awards will not be more generous than the terms attached to the awards forfeited on cessation of employment with the previous employer. ◆ The variable pay awards for MRTs are structured as follows: • Variable pay is capped to a maximum of 200% of total fixed pay, after application of any discount permitted under the PRA Remuneration Rules. • The higher of any regulatory deferral requirement and the Group deferral requirement is applied for all variable pay awards. • In general, 40% of total variable pay award (annual incentive plus any long-term incentive award) is deferred for three years, five years or seven years. This increases to 60% for a high variable pay amount in line with regulatory requirements. • At least 50% of annual incentive award (both deferred and non-deferred component) is generally delivered in shares and subject to a retention period of up to one-year on vesting. • Long-term incentive awards are subject to a three-year performance period, and vesting is dependent on performance achieved against pre-defined performance targets. The awards for executive Directors vest in five equal instalments after the end of the performance period and subject to a retention period of up to one year.

Remuneration principles	How we comply
	• Variable pay awards are subject to malus provisions and can be reduced or cancelled in appropriate circumstances. • Variable pay awards will be subject to clawback for a minimum period of seven years from the date of grant and may extend to 10 years for employees under the Senior Manager Regime in the event of on-going internal/regulatory investigation.