

# **HSBC Bank Malta p.l.c.**

## **Statement of Compliance with the Code of Principles of Good Corporate Governance**

## Statement of Compliance with the Code of Principles of Good Corporate Governance

The Board of Directors (the 'Board') of HSBC Bank Malta p.l.c. is committed to the HSBC global values of dependability, openness to different ideas and cultures, and connection with customers, communities, regulators and each other. The Board ensures that each employee, through ongoing training, is aware of the obligation to ensure that his or her conduct consistently matches the bank values so as to serve positively the customers who entrust their financial needs to HSBC.

The Board is proud of the fact that the bank and its subsidiaries (the 'local group') has a solid corporate governance framework that is built around the principles of control and accountability. This culture stems from a philosophy that puts the protection of investors and the interest of customers at the forefront.

Corporate governance is subject to regulation by the Malta Financial Services Authority Listing Rules. As a company whose equity securities are listed on a regulated market, HSBC Bank Malta p.l.c. endeavours to adopt the Code of Principles of Good Corporate Governance (the 'Code' or 'Principles') embodied in Appendix 5.1 to Chapter 5 of the Listing Rules. In terms of Listing Rule 5.94, the bank is obliged to disclose compliance and non-compliance with the provisions of the said Code. The bank strives to maintain the highest standards of disclosure in reporting the effective measures adopted to ensure compliance with the Principles, and to explain the instances of non-compliance.

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### Compliance with the Code

#### Principle 1: The Board

The bank is headed by an effective Board that leads and controls the business. The Board is composed of members who are honest, competent and solvent, and thus fit and proper to direct the business of the bank. Directors, individually and collectively, are of the appropriate calibre, having the necessary skills and experience to provide leadership, integrity and judgement in directing the bank. The courageous integrity, honesty and diligence of the Directors guarantee that the bank adheres to HSBC Group's (the 'Group') highly ethical business values and this is reflected in the bank's decision and policy-making process. Through their effective contribution Directors enhance shareholders value, protect the bank's assets and safeguard the interest of third parties.

Board members are accountable for their performance and that of their delegates to shareholders and other relevant stakeholders. Besides having a broad knowledge of the bank's business they are also conversant with the statutory and regulatory requirements regulating this business. Directors regularly attend Board meetings and allocate sufficient time to perform their duties.

The Board determines the bank's strategic aims and organisational structures and regularly reviews management performance. It ensures that the bank has the appropriate financial and human resources to meet its objectives. Moreover, it exercises prudent and effective controls which enable risk to be assessed and managed in order to achieve the short and long term sustainability of the business.

As part of a larger international group the Board assesses the compatibility of Group policy with local legal and regulatory requirements, and where appropriate, amends those policies.

During the year the Board delegated specific responsibilities to a number of committees, namely the Audit Committee, the Risk Committee, the Remuneration and Nomination Committee and the Executive Committee. Further detail in relation to the committees and their responsibilities can be found under principle 4 of this statement.

The process of appointment of Directors is conducted in terms of the Memorandum and Articles of Association of the company which state that the Board is to consist of not more than nine Directors who are appointed/elected by the shareholders. Every shareholder owning 11 per cent of the ordinary share capital is entitled to appoint one Director for each 11 per cent shareholding. The majority shareholder therefore has the right to appoint six Directors. Furthermore, any excess fractional shareholding not so utilised may be used to participate in the voting for the election of further Directors. Shareholders who own less than 11 per cent of the ordinary share capital participate in the election of the remaining three Directors. The largest single shareholder (subject to a minimum 33 per cent holding of the ordinary issued share capital of the bank) is entitled to appoint a Chairman from amongst the Directors appointed or elected to the Board.

#### Principle 2: Chairman and Chief Executive Officer

The position of the Chairman and that of the Chief Executive Officer are occupied by different individuals. There is a clear division of responsibilities between the running of the Board and the Chief Executive Officer's responsibility in managing the bank's business. This separation of roles of the Chairman and Chief Executive Officer avoids concentration of authority and power in one individual and differentiates the function of leadership of the Board from that of running the business.

The Chairman leads the Board, sets the agenda and ensures that the Directors receive precise, timely and objective information and at the same time ensures effective communication with shareholders. During Board meetings, he encourages active engagement by all Board members and ensures that Directors constructively challenge senior management. The Chairman also facilitates the effective contribution of non-executive Directors and ensures constructive relations between executive and non-executive Directors.

The Chief Executive Officer develops, drives and delivers performance within strategic goals, commercial objectives and business plans agreed by the Board. He effectively leads the senior management in the day-to-day running of the bank, ensures compliance with appropriate policies and procedures and maintains an effective framework of internal controls over risk in relation to the business. He makes decisions in all matters affecting the operations, performance and strategy of the business, with the exception of those matters reserved for the Board or specifically delegated by the Board to its Committees. He is also responsible for the recruitment and appointment of senior management, after consultation with the Remuneration and Nomination Committee.

## Statement of Compliance with the Code of Principles of Good Corporate Governance

### Principle 3: Composition of the Board

Experience has shown that the size of the Board is appropriate to facilitate the effective oversight over the bank's operations. Each of the Directors is skilful, competent, knowledgeable and experienced to fulfil one's role diligently. The Directors who held office during the year possess the requisite ability to assess business risk, to identify key performance indicators and participate in critical debate in the decision-making process.

Ethnicity, age, culture, and gender diversity, underpinned by meritocracy, are areas of strategic focus for the employee base and the same principle is applied to the composition of the Board in accordance with the Board Diversity Policy reviewed and approved in May 2018. The reviewed policy established a target for 33% of directors to be female by 2020 (presently there is one female director on the Board), together with an aspiration to target gender parity on the Board over the long term while abiding by the principle of meritocracy. Indeed the bank remains committed to meritocracy in the Boardroom, which requires a diverse and inclusive culture where Directors believe that their views are heard, their concerns are attended to and they serve in an environment where bias, discrimination and harassment on any matter are not tolerated. The benefits of diversity, including that in educational and professional backgrounds, continue to influence the Remuneration and Nomination Committee's Board succession planning and Board candidates' selection process. This has resulted in a diverse Board composition with meets the diversity criteria in its widest aspect of ethnicity, age, culture, gender and educational and professional backgrounds.

As at 31 December 2018 the Board was composed of a non-executive Chairman, an executive Director, a designate executive Director and six non-executive Directors, five of whom are deemed to be independent. The non-executive Directors bring an external perspective to the Board when they constructively challenge and help develop proposals on strategy, scrutinise the performance of management, and monitor the risk profile and the reporting of performance. They are proactive in ensuring that financial controls and risk management systems are well established and in satisfying themselves with the integrity of financial information.

Following the appropriate due diligence, the European Central Bank had given its non-objection to all the bank's Directors. The letter of appointment issued to non-executive Directors stipulates the minimum time commitment expected to be dedicated to the bank. Non-executive Directors undertake that they will have sufficient time to meet what is expected of them. Any other significant commitments are disclosed to the Board before their appointment and subsequent changes are notified as they arise.

In accordance with the Code Provision 3.2, the independent non-executive Directors as at 31 December 2018 were the following:

John Bonello  
Gordon Cordina  
Yiannos Michaelides  
Andrew Muscat  
Sue Vella

In determining the independence or otherwise of its Directors, the Board has considered, inter alia, the principles relating to independence embodied in the Code, the local group's own practice as well as general principles of good practice.

The Board has determined that the fact that Professor Muscat is a partner in a Law firm which provides legal services to the bank and the fact that an economic consultancy firm in which Dr Gordon Cordina is executive director, provides consultancy services to the bank, do not influence these Directors' objective and balanced judgement or in any way reduce their ability to take decisions independently. On the other hand, in accordance with Code Provision 3.2.1, the Board believes that the employment of Chris Davies with the Group renders him non-independent from the bank. This should not however, in any manner, detract from the non-independent Director's ability to maintain independence of free judgement and character at all times and is able to make his own sound, objective, judgment and independent decisions and judgments when performing his functions and responsibilities.

In terms of Principle 3.4, each non-executive Director has confirmed in writing to the Board that he/she undertook:

- to maintain in all circumstances his/her independence of analysis, decision and action;
- not to seek or accept any unreasonable advantages that could be considered as compromising his/her independence; and
- to clearly express his/her opposition in the event that he/she finds that a decision of the Board may harm the bank.

### Principle 4: The Responsibilities of the Board

The Board sets the bank's strategy, policies and business plans. The Board met informally twice during 2018 specifically to focus on strategy review and development. The Board of Directors monitors the implementation of strategy and policy by management within the parameters of all relevant laws, regulations and codes of best practice. The Board ensures that a balance is maintained between enterprise and control. The Board recognizes and supports innovation within the management of the bank. The Board remains accountable to the shareholders for its performance and also ensures effective communication with the different groups of stakeholders.

The Board actively oversees the affairs of the bank and keeps up with material changes in the bank's business and the external environment as well as acts in a timely manner to protect the long-term interests of the bank. It plays a leading role in establishing the bank's corporate culture and values. The Board, together with senior management and the Chief Risk Officer establishes the bank's risk appetite, taking into account the commercial and regulatory landscape and the bank's long-term interests, risk exposure and ability to manage risk effectively. It also oversees the bank's adherence to the Risk Appetite Statement, risk policy and risk limits. The Board is also responsible for approving the approach and overseeing the implementation of key policies pertaining to the bank's capital adequacy assessment process, capital and liquidity plans, compliance policies and obligations and the internal control system. The Board, through one of its Directors who reports to the Board, oversees the integrity, independence and effectiveness, of the bank's policies and procedures for whistleblowing.

The regular evaluation of management's implementation of corporate strategy and financial obligations is based on the use of key performance indicators enabling the bank to

adopt expedient corrective measures. These key business risk and performance indicators are benchmarked against industry norms so as to ensure that the bank's performance is effectively evaluated.

The Board ensures that the bank has appropriate policies and procedures in place that guarantee that the bank and its employees adhere to the highest standards of corporate conduct and comply with the applicable laws, regulations, business and ethical standards.

An effective reporting system that enables the Directors to have relevant and timely information such that the Board can discharge its duties, exercise objective judgement and take pertinent decisions is implemented through:

- presentations during Board meetings delivered by senior management;
- updates provided by the CEO and senior management during intervals between Board / Committees' meetings; and
- accessibility to a common electronic platform hosting bank information, including Board / Committees' documentation and minutes of meetings.

The Board makes certain that its level of power is known by all Directors and the senior management of the bank. Any delegation of responsibility and functions is clearly documented in the Terms of Reference (TOR) embodied in the corporate governance framework.

The Board delegates specific responsibilities to Committees, which operate under their respective formal TOR:

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### Audit Committee

The terms of reference of this Committee are compliant with the Listing Rules and Banking Rule 12, the European Banking Authority and are modelled on the recommendations in the Cadbury Report and the UK Walker Review.

The Committee protects the interests of the bank's shareholders and assists Directors in conducting their role effectively so that the bank's decision-making capability and the accuracy of its reporting and financial results are maintained at the highest level at all times. It ensures that the bank maintains a robust finance function responsible for accounting and financial data. This Committee has non-executive responsibility for oversight of, and advice to, the Board on matters relating to financial reporting. Hence, it monitors the integrity of the bank's financial statements, and any formal announcements relating to the bank's financial performance or supplementary, regulatory information, reviewing significant financial reporting judgements contained in them.

An important function of the Audit Committee is to monitor and review the effectiveness of the Internal Audit function, consider major findings of internal investigations and management's response, and ensure that the Internal Audit Function is adequately resourced and is free from constraint by management.

This Committee approves the internal audit work plan, which will include assessment of controls relating to financial reporting, conduct financial crime and other risks as appropriate.

The Audit Committee also has the responsibility to review and monitor the external auditor's independence and the effectiveness of the audit process. In this regard the Committee

has also to satisfy itself that there is the appropriate co-ordination between the internal and external auditors.

This Committee scrutinises and approves related party transactions. It considers the materiality and the nature of the related party transactions carried out by the bank to ensure that the arms' length principle is adhered to at all times and that business resources are not misapplied.

The Committee met seven times during 2018 and was composed of Mr John Bonello as Chairman, and Dr Gordon Cordina and Professor Andrew Muscat as Members.

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#### Attendance at Audit Committee meetings

	<b>Attended</b>
John Bonello	<b>7 out of 7</b>
Gordon Cordina	<b>7 out of 7</b>
Andrew Muscat	<b>7 out of 7</b>

During the year regular informal meetings were held between the Chairman of this Committee and Members of Senior Management especially the Chief Executive Officer, the Head of Internal Audit and the Chief Financial Officer. Moreover, a number of informal meetings were held to discuss inter alia IFRS 9, General Data Protection Regulation and related party transactions.

Senior Managers of the bank are invited to attend any of the Audit Committee's meetings as directed by the Committee.

The Chief Executive Officer, the Chief Risk Officer, the Chief Financial Officer and representatives of the external auditors attend all the meetings. In line with Listing Rule 5.131, the Head of Internal Audit is also always present for its meetings and has a right of direct access to the Chairman of the Committee at all times.

Mr Bonello was appointed by the Board as the Director who is independent and competent in accounting and/or auditing in terms of Listing Rule 5.117 on the basis that he is a Fellow of the Institute of Chartered Accountants in England and Wales and is also a Certified Public Accountant, Auditor and Fellow of the Malta Institute of Accountants. He was formerly the Chairman and Senior Partner of PricewaterhouseCoopers in Malta from where he retired in 2009.

In terms of Listing Rule 5.127.7, the Audit Committee is responsible for developing and implementing policy on the engagement of the external auditor to supply non-audit services. The provision of non-audit services to EU Public Interest Entities (PIEs) and to parent and controlled undertakings in the EU are regulated in terms of EU rules. Under the regulations there are also certain prohibitions to controlled entities outside the EU.

In addition, since HSBC Holdings plc is a Securities Exchange Commission (SEC) registered company, non-audit services provided by the external auditor are also regulated in terms of the SEC rules.

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### Risk Committee

This Committee is responsible for advising the Board on high level risk related matters. In providing such oversight and advice to the Board, the Committee oversees: current and forward looking risk exposures, the bank's risk appetite and future risk strategy, including capital and liquidity management strategy, and management of risk within the bank.

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In undertaking its responsibility to review the effectiveness of the bank's risk management framework and internal controls it has to inter alia satisfy itself that there are adequate procedures and internal controls for monitoring in a sufficiently timely and accurate manner, large exposures or risk types whose relevance may become of critical importance. It also has to consider any material findings from regulatory reviews and interactions with regulators in relation to risk governance or risk assessment or management process.

The Committee met six times during 2018 and was composed of Dr Gordon Cordina as Chairman, and Mr John Bonello and Mr Yiannos Michaelides as Members.

### Attendance at Risk Committee meetings

	<b>Attended</b>
Gordon Cordina	<b>6 out of 6</b>
John Bonello	<b>6 out of 6</b>
Yiannos Michaelides	<b>5 out of 6</b>

Senior Managers of the bank are invited to attend any of the meetings as directed by the Committee.

The Chief Executive Officer, the Chief Risk Officer, the Chief Financial Officer, the Head of Financial Crime Compliance and the Head of Regulatory Compliance and representatives of the external auditors are invited to attend the meetings. During the year Dr Manfred Galdes was appointed Advisor to the Committee on Financial Crime Compliance matters.

### Remuneration and Nomination Committee ('REMNUM' Committee)

The remuneration aspect of this Committee is dealt with under the Remuneration Report, which also includes the Remuneration Statement in terms of Code Provision 8.A.4.

In its nomination function, the Committee is primarily tasked with identifying and nominating new Board and Board Committees' candidates for the approval of the Board and to periodically assess the structure, size, composition and performance of the Board and make recommendations to the Board with regard to any changes. It is also tasked with considering issues related to succession planning and reviewing the policy of the Board for selection and appointment of senior management. This Committee is also responsible to periodically assess the skills, knowledge and experience of individual Directors and report on this to the Board.

During 2018 REMNUM met eight times and it continued to perform its role regarding 'fit and proper' assessments of present and prospective Board Members. The results of these assessments are then submitted to the Regulator as an integral part of the Regulator's due diligence exercise.

The members of the REMNUM were Mr Sonny Portelli (Chairman), Professor Andrew Muscat and Dr Sue Vella.

### Executive Committee ('EXCO')

EXCO meets on a monthly basis to oversee the overall day-to-day management of the bank in accordance with such policies and directions as the Board may from time to time determine. The Chief Executive Officer chairs this Committee which is composed of members of the senior management of the bank. EXCO is empowered by its terms of reference to delegate its powers to sub-committees:

#### • The Risk Management Meeting (RMM)

This Committee meets on a monthly basis and is chaired by the Chief Risk Officer, with the Chief Executive Officer as alternate chairman. Membership also includes the Chief Operating Officer, the Chief Financial Officer, the Head of Retail Banking and Wealth Management, the Head of Commercial Banking, the Head of Global Banking and Markets, the Head of Wholesale and Markets Risk, the Head of Internal Audit, General Counsel, Head of Regulatory Compliance and Head of Financial Crime Compliance. Other regular attendees are the Head of Credit Risk Management, Analytics and Systems, the Head of Security and Fraud Risk, Senior Manager Assurance and Oversight and Head of Communications.

The objective of this Committee is to exercise oversight of the risk/reward framework for the bank and its subsidiaries.

This Committee is responsible for all risks in all businesses, functions and subsidiaries under the ownership of HSBC Bank Malta p.l.c., including inter alia Credit Risk, Market Risk, Operational Risk, Concentration Risk, Legal and Regulatory Risk, Security and Fraud Risk and Reputational Risk. The Risk Management Committee is also responsible for the setting and monitoring of a Risk Appetite Framework for EXCO and Board approval, signing off on material credit risk models, and consideration of top and emerging risks and scenario analysis. Individual risk acceptance and approval is not within the TOR of the Committee, and continues to be approved under existing delegated authorities within the management structure of the bank.

Minutes of meetings of this Committee are circulated to the members of the Board. The Chief Risk Officer is also invited to attend Board meetings and meetings of the Audit and Risk Committees in which representations are made about the overall risk profile associated with the business including a comprehensive assessment of the bank's management of risk.

#### • The Asset and Liability Management Meeting (ALCO)

ALCO is responsible for managing the balance sheet with a view to achieve efficient allocation and utilisation of all resources.

This Committee reviews the financial risks of the local group and oversees the prudent management of interest rate risk, liquidity and funding risk, capital, foreign exchange risk, solvency risk, market sector risk and country risk. Furthermore, ALCO monitors the external environment and measures the impact on profitability of factors such as interest rate volatility, market liquidity, exchange rate volatility, monetary and fiscal policies and competitor banks' activity. ALCO monitors the liquidity and capital adequacy, making use of capital forecasts to ensure that enough capital is readily available at all times to meet the demand arising from business expansion and regulation. ALCO monitors and reviews the duration and cash flow matching of insurance assets and liabilities.

The Chief Executive Officer has primary responsibility for ensuring efficient development of Asset and Liability Management. Membership consists of senior executives with responsibility for the following functions: commercial banking, retail banking and wealth management, global banking and markets, finance, insurance services, asset and liability capital management, customer value management and payments and cash management. ALCO, which is chaired by the Chief Financial Officer and deputised by the Chief Executive Officer, meets once a month. The Chief Accounting Officer is also a member of this Committee.

- **Financial Crime Risk Management Committee ('FCRMC')**

This Committee provides on-going oversight, management and communication of Financial Crime Compliance (FCC) risks, issues and changes impacting the business lines. FCC includes Anti-Money Laundering (AML), Sanctions, Anti-Bribery and Corruption, and Fraud. The membership of this Committee, which is chaired by the bank's Chief Executive Officer, is composed of most of the bank's EXCO team and the Money Laundering Reporting Officer.

In the selection of the above Committees' chairmanship and membership, there is recognition of the value in refreshing said appointments and in ensuring that no undue reliance is placed on particular individuals.

**Principle 5: Board meetings**

The Board meets as often and as frequently required to discharge its duties effectively. During the period under review the Board held seven meetings and another two informal meetings.

The Chairman ensures that all relevant issues are on the agenda and supported by all the available information. The agenda strikes a balance between long-term strategic objectives and short term performance issues. Notice of the dates of Board meetings together with supporting materials are circulated to the Directors well in advance of the meetings.

During the meetings Board Members have ample opportunity to discuss issues set on the board agenda, convey their opinions and challenge management. The Chairman facilitates presentation of views pertinent to the relevant issues on the agenda by promoting a culture of openness and debate. Moreover, Directors are encouraged to discuss any issue which they deem appropriate.

Minutes are taken during Board meetings that record faithfully attendance, discussed matters and decisions. These minutes are subsequently circulated to all the Directors as soon as practicable after the meeting. Besides attending formal Board meetings and Committee meetings of which they form part, Directors attend on frequent and regular basis meetings where their presence is required for the proper discharge of their duties. All the Directors dedicate the necessary time and attention to their duties as Directors of the bank. The holding of other directorships in other companies is in line with regulatory provisions.

Directors' attendance at Board Meetings

	Attended
Saviour sive Sonny Portelli	7 out of 7
Andrew Beane	7 out of 7
John Bonello	7 out of 7
Gordon Cordina	7 out of 7
Christopher Davies	4 out of 7
Alison Hewitt (resigned on 21 February 2018)	1 out of 2
Yiannos Michaelides	6 out of 7
Andrew Muscat	6 out of 7
Maryanne sive Sue Vella	6 out of 7

**Principle 6: Information and professional development**

The Board appoints the Chief Executive Officer of the bank upon guidance and recommendation by the HSBC Group and by the REMNOM Committee. The Board, through the REMNOM Committee, is actively involved in the appointment of other members of senior management. In this regard the bank benefits from the vast wealth of competence, talent and experience found across the Group.

Full, formal and tailored induction programmes, with particular emphasis on the systems of risk management and internal controls are arranged for newly appointed Directors.

The programmes consist of a series of meetings with senior executives to enable new Directors to familiarise themselves with the bank's strategy, risk appetite, operations and internal controls. Directors also receive comprehensive guidance on Directors' duties and liabilities.

A structured Board training and development programme is organised for the Directors and facilitated by an External Accounting Firm. The key objective of the programme is to improve the Board's awareness in risk, regulation, and compliance developments in the financial services sector. Topics covered during these awareness sessions range from the new regulatory environment to managing risk. Directors also participate in the Group's mandatory training which covers Financial Crime Compliance topics, regulatory matters, data privacy and cyber security. Additional training is also held for individual Directors sitting on Board committees.

Directors are given opportunities to update and develop their skills and knowledge, through briefings by senior executives and externally-run seminars throughout their directorship. Moreover, Directors have access to independent professional advice, at the bank's expense.

Directors also have access to the advice and services of the Company Secretary who is responsible for adherence to Board procedures as well as for effective information flows within the Board, its Committees and with senior management.

The Chairmen of the Audit and Risk Committees attend on an annual basis the Group Audit / Risk Committee Chairmen Forum where they are updated on the latest topical issues from an Audit / Risk Committees' perspective.

As part of succession planning and talent management, the Board and the Chief Executive Officer ensure that the bank implements appropriate schemes to recruit, retain and motivate high quality executive officers. They also encourage members of management to move to the higher ranks within the organisation and seek to maintain high morale amongst the bank's personnel.

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### Principle 7: Evaluation of the Board performance

During the year the Board undertook an evaluation of its own performance, the Chairman's performance and that of its Committees through a Board Effectiveness Questionnaire modelled on a questionnaire adopted by Group. This process was conducted by the REMNOM Committee through the support of the Company Secretary. No material changes in the governance structures and organisation resulted from this Board evaluation exercise.

### Principle 8: Committees

The Remuneration and Nomination Committee is covered under Principle 4 and in the Remuneration Report, which also includes the Remuneration Statement in terms of Code provisions 8.A.4.

### Principles 9 and 10: Relations with the shareholders, with the market and with institutional shareholders

The bank maintains on-going communication with its shareholders and the market on its strategy and performance in order to enhance trust and confidence in the bank. During the period under review the bank issued various company announcements and media releases to explain ongoing corporate developments and material events and transactions which have taken place and their impact on the financial position of the bank.

The bank communicates with shareholders in the following ways:

- through the 'Annual Report and Accounts' which is mailed to every shareholder and is available on the bank's website;
- through the publication of company announcements and media releases; and
- at the Annual General Meeting and Extraordinary General Meetings (further detail is provided under the section 'General Meetings').

The bank also holds meetings for stockbrokers, financial intermediaries and the media to explain the salient features of the interim and annual financial results.

The bank maintains an open channel of communication with its shareholders through the Company Secretarial Office and through the Head of Communications. Meetings have also been held between the Chief Executive Officer and the Malta Association of Small Shareholders.

As the Board always endeavours to protect the interests of both the bank and its shareholders, present and future, the Board takes into account the fact that shareholders are constantly changing. This is reflected in the Board's decisions on long term sustainability objectives to safeguard the interests of future shareholders. The Chairman ensures that the views of shareholders are communicated to the Board. Moreover, the Chairmen of the Audit Committee, of the Risk Committee and of the REMNOM Committee are available to answer questions during the Annual General Meeting. The conduct of the meeting is conducive to valid discussion and appropriate decision making.

In terms of the bank's Articles of Association, the Directors shall, on the request of members of the company holding not less than one-tenth of the paid up share capital, proceed duly to convene an Extraordinary General Meeting of the bank.

### Principle 11: Conflicts of interests

Directors are aware that their primary responsibility is always to act in the interest of the bank and its shareholders as a whole, irrespective of who appointed them to the Board. This requires that they avoid conflicts of interest at all times and that their personal interests never take precedence over those of the bank and its shareholders.

In line with HSBC Group best practice, the Board operates a Conflicts Policy. In terms of this policy a Director is to avoid situations in which he or she has, or could have, a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the bank. Without prejudice to Articles 136A (3)(C) and 143 of the Companies Act, this policy stipulates that a director must obtain an authorisation from the Board before a situational conflict arises. Notably, in accordance with this policy, all directorships and other non-HSBC appointments should be authorised by the Board.

By virtue of the bank's Articles of Association, a Director is bound not to vote at a Board meeting on any contract or arrangement or any other proposal in which he has a material interest, either directly or indirectly. Moreover, in terms of the Board's Conflicts Policy, a Director having a continuing material interest that conflicts with the interests of the Bank, should take effective steps to eliminate the grounds for conflict. In the event that such steps do not eliminate the grounds for conflict then the Director should consider resigning.

On joining the Board and regularly thereafter, Directors are informed and reminded of their obligations on dealing in securities of the bank within the parameters of law and the Listing Rules. A proper procedure of reporting advance notices to the Chairman by a Director who intends to deal in the bank's shares has been endorsed by the Board in line with the Principles, the Listing Rules and the internal Code of Dealing.

### Principle 12: Corporate sustainability

HSBC's Corporate Sustainability (CS) activities take place within the context of the Group wide strategy. The Board continues to recognise that the bank has a role within, and responsibility towards, the community it serves. To discharge these roles and responsibilities, during 2018, the bank continued to utilise its resources in order to carry out a series of initiatives and projects designed to provide value to various sectors within the community.

In Malta, the bank fulfils the Group's CS strategy primarily through the HSBC Malta Foundation (the 'Foundation'). The pillars of the HSBC Malta Foundation, with a yearly budget of more than €390,000, aim to improve the quality of life and education for children, especially the disadvantaged, to promote and work towards a more sustainable environment, to preserve Malta's rich and unique historical heritage, and in the area of medical research. In addition during 2018, in line with the Group's strategy, the Foundation also supported projects which focus on Future Skills. The objective of Future Skills is on helping people develop their employability and financial skills in order to thrive in the modern world.

Voluntary work is highly encouraged and HSBC staff who contribute to the charities and causes that they feel passionate about are encouraged to take an active role in initiatives supported by the Foundation, with an extra day's leave granted for voluntary work. During 2018, 306 HSBC colleagues volunteered on a range of projects around the country.

The HSBC Malta Water Programme - Catch the Drop Campaign, a nationwide environmental and educational water conservation campaign, continued to reach every student in Malta and Gozo, as well as various Local Councils. The main emphasis of this programme is to raise awareness on water shortage, encourage water consumption reduction, and water harvesting. This campaign was supported by a €540,000 grant from the HSBC Group. Bank employees are at the heart of this campaign with over 500 staff members volunteering to deliver the information sessions in all 172 schools around the country. Additionally, the HSBC Malta Foundation is supporting the international 'Water Explorer' programme, delivered locally by Nature Trust - FEE Malta through its Eco-Schools (EkoSkola) programme. In 2018 the HSBC Malta's CSR Institute was also launched, with the aim of training up to 500 members of public and business organisations on the values and ideals of corporate social responsibility as well as sustainability.

With the support of the HSBC Malta Foundation, Malta became the first country outside of the UK to introduce one of The Prince's Trust's long-standing educational programmes in its secondary schools. To date, 549 students were participating in the Achieve Programme which is helping these young people in Malta to develop the skills and confidence they need to reach a positive future through relevant, engaging and informal learning.

To raise the bank's commitment to support a sustainable environment for Malta and Gozo, the bank took several possible measures to ban single-use plastics within the organisation. Further, action was taken to introduce new recycling standards across the business.

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## Non-compliance with the Code

### Principle 4 (Code Provision 4.2.7)

Code Provision 4.2.7 recommends 'the development of a succession policy for the future composition of the Board of Directors and particularly the executive component thereof, for which the Chairman should hold key responsibility'. The bank discloses that it has not formalised a Board succession policy. However, in practice the REMNOM Committee is actively involved in the board succession, specifically in recommending the appointment of new members and also by evaluating any newly proposed appointees.

### Principle 9 (Code Provision 9.3)

This Code Provision recommends the bank to have in place a mechanism to resolve conflicts between minority shareholders and controlling shareholders. Although the bank does not have such mechanism in place there is ongoing open dialogue between the bank's senior management and the non-executive Directors to ensure that no such conflicts arise.

In terms of Code Provision 9.4 minority shareholders should be allowed to formally present an issue to the Board of Directors. The bank discloses that it does not have a policy in terms of this code provision.

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## Internal control

The Board is ultimately responsible for the bank's system of internal control and for reviewing its effectiveness. Such procedures are designed to manage and mitigate rather than to eliminate the risk of failure, to achieve business objectives and can only provide reasonable and not absolute assurance against material error, losses or fraud. The Group has reviewed the risk management and internal control structure referred to as the 'three lines of defence' to ensure we achieve our commercial aims while meeting regulatory, legal as well as Group requirements. It is a key part of our operational risk management framework.

- First line - The First Line of Defence consists of 'Risk Owners' and 'Control Owners'. The bank's Global Business employees are the 'Risk Owners'. They own the risk, set the risk appetite and are accountable for managing the risk associated with their commercial activities. In managing the risk they are responsible to both manage their own controls and work closely with other Control Owners who sit outside of their area. 'Control Owners' exist in Global Businesses, Global Functions and HOST (HSBC Operations, Services and Technology). They are accountable for the controls required to manage the risk associated with our commercial activities. They are required to monitor and provide an opinion on the effectiveness of the controls relied upon by the Risk Owners to manage their risk(s).
- Second line - The Second Line of Defence consists of 'Risk Stewards' and their teams. It is made up in part (but not exclusively) by leaders within Global Risk and other Global Functions. They set policy, give advice and provide independent challenge. In doing this, they oversee and assess the risk management activities carried out by the First Line. The Risk Stewards set the overall maximum risk appetite for their particular risk type (e.g. financial crime risk, regulatory compliance risk, legal risk, tax risk, accounting risk, people risk, fraud risk) and support the Risk Owners with setting their risk appetite within Group's overall risk appetite.
- Third line - The Third Line of Defence is Global Internal Audit, and it independently assures that the design and operating effectiveness of Group's framework of risk management, governance and internal control are adequate.

The local group's key risk management and internal control procedures include the following:

- Global standards. Functional, operating, financial reporting and certain management reporting standards are established by global function management committees, for application throughout HSBC globally. These are supplemented by operating standards set by functional and local management as required for the type of business and geographical location of each subsidiary.
- Delegation of authority within limits set by the Board. The Board has delegated specific, clear and unequivocal authority to the Chief Executive Officer to manage the day-to-day affairs of the business for which he is accountable within limits set by the Board. Delegation of authority from the Board requires the CEO to maintain appropriate apportionment of significant responsibilities and to oversee the establishment and maintenance of systems of control that are appropriate to the business.



## Statement of Compliance with the Code of Principles of Good Corporate Governance

- Risk identification and monitoring. Systems and procedures are in place to identify, control and report on the major risks facing the bank including credit, market, liquidity, capital, financial management, model, reputational, strategic, sustainability and operational (including accounting, tax, legal, compliance, fiduciary, information, external fraud, internal fraud, political, physical, business continuity, systems operations, project and people risk). Exposure to these risks is monitored by the Risk Management Meeting, Asset and Liability Committee and Executive Committee.
- Changes in market conditions/practices. Processes are in place to identify new risks arising from changes in market conditions/ practices or customer behaviours, which could expose the bank to heightened risk of loss or reputational damage. Further improvements have been, and will continue to be, implemented to combat the inherent challenges posed by financial crime. In addition attention remained focused on regulatory developments and engagement, including the ongoing supervisory review and evaluation process under the ECB's Single Supervisory Mechanism; regulatory commitments and consent orders that culminated in meeting the obligations under the Deferred Prosecution Agreement; challenges to balance business growth and risk management imperatives; internet crime and fraud; level of change creating operational complexity and heightened execution risk; and information security risk.
- IT operations. Centralised functional control is exercised over all IT developments and operations. In order to ensure consistency and benefit from economies of scale Common Group systems are employed for similar business processes wherever practicable.
- Comprehensive annual financial plans are prepared, reviewed and approved by the Board. Results are monitored and progress reports are prepared on a monthly basis to enable comparisons with plan. Financial accounting and management reporting standards have been established.
- Responsibilities for financial performance against plans and for capital expenditure, credit exposures and market risk exposures are delegated with limits to executive management. In addition, functional management in the bank has been given the responsibility to implement HSBC policies, procedures and standards for business and product lines; finance; legal and regulatory compliance; internal audit; human resources; credit risk; market risk; operational risk; computer systems and operations and property management.
- The Chief Risk Officer is responsible for the management of specific risks within the bank including credit risk in the wholesale and retail portfolios, markets risk and operational risk. Risks are monitored via Risk Management Meeting which meets regularly and via reporting to the Executive Committee, the Risk Committee and to the Board.
- Internal Audit. The establishment and maintenance of appropriate systems of risk management and internal control is primarily the responsibility of business management. The Internal Audit function reports to the Board. It provides independent and objective assurance in respect of adequacy of the design and operating effectiveness of the bank's framework of risk management, control and governance processes focusing on the areas of greatest risk to the bank using a risk-based approach. The Head of Internal Audit also reports to the Head of Global Internal Audit in so far as independence and resourcing are concerned.
- Internal Audit issues. Executive management is responsible for ensuring that any issues raised by the Internal Audit function are remediated within an appropriate and agreed timetable. Confirmation to this effect must be provided to Internal Audit who subsequently validate the remediation.
- The bank's Regulatory Compliance Department ensures that the local group maintains the highest standards of corporate conduct including compliance with all the local and international regulatory obligations and HSBC Group ethical standards and regulations.
- The bank's Financial Crime Compliance Department is responsible for the oversight of Anti Money Laundering and Terrorist Financing, Sanctions, Anti-Bribery and corruption and Fraud risks. Particular attention is given to the proactive management of identified Financial Crime Compliance issues. Routine governance is managed via the entity wide Financial Crime Risk Management Committee, and material matters reported to the Executive Committee, the Risk Committee and to the Board.
- Through the Audit Committee and Risk Committee, the Board reviews the processes and procedures to ensure the effectiveness of the system of internal control of the bank and its subsidiaries, which are subject to third line of defence review by Internal Audit.

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### Listing Rule 5.97.5

- The information relating to the Shareholder register required by this Listing rule is found in the Directors' Report.

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### General meetings

The General Meeting is the highest decision making body of the bank. A General Meeting is called by twenty-one days' notice and it is conducted in accordance with the Articles of Association of the bank.

The Annual General Meeting deals with what is termed as 'ordinary business', namely the receiving or adoption of the annual financial statements, the declaration of a dividend, the appointment and remuneration of the Board (which may or may not involve an election), the appointment of the external auditors and the grant of the authority to the Board to fix the external auditors' emoluments. Other business which may be transacted at a General Meeting will be dealt with as Special Business.

All shareholders registered in the shareholders' Register on the record date as defined in the Listing Rules, have the right to attend, participate and vote in the General Meeting. A shareholder or shareholders holding not less than 5% in nominal value of all the shares entitled to vote at the General Meeting may request the bank to include items on the agenda of a General Meeting and/or table

draft resolutions for items included in the agenda of a general meeting. Such requests are to be received by the bank at least forty-six days before the date set for the relative General Meeting. A shareholder who is unable to participate in the General Meeting can appoint a proxy by written or electronic notification to the bank. Every shareholder represented in person or by proxy is entitled to ask questions which are pertinent and related to items on the agenda of the General Meeting and to have such questions answered by the Directors or such persons as the Directors may delegate for that purpose.