

**HSBC SECURITIES (USA) INC.**  
(An Indirect Wholly Owned Subsidiary of HSBC Holdings plc)

Statement of Financial Condition

December 31, 2015

This report is deemed PUBLIC in accordance  
with Rule 17a-5(e)(3) under the Securities Exchange  
Act of 1934 and Regulations 1.10(g), 145.5, and 145.9  
under the Commodity Exchange Act



**Report of Independent Registered Public Accounting Firm**

To the Board of Directors of HSBC Securities (USA) Inc.:

In our opinion, the accompanying statement of financial condition presents fairly, in all material respects, the financial position of HSBC Securities (USA) Inc. at December 31, 2015 in conformity with accounting principles generally accepted in the United States of America. The statement of financial condition is the responsibility of the Company's management. Our responsibility is to express an opinion on the statement of financial condition based on our audit. We conducted our audit of this statement in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statement of financial condition is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the statement of financial condition, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial condition presentation. We believe that our audit of the statement of financial condition provides a reasonable basis for our opinion.

*PricewaterhouseCoopers LLP*

February 29, 2016

**HSBC SECURITIES (USA) INC.**  
(An indirect wholly owned subsidiary of HSBC Holdings plc)

Statement of Financial Condition

December 31, 2015

(Dollars in thousands)

**Assets**

Assets:

|   |    |                          |
|---|----|--------------------------|
| Cash  | \$ | 86,759                   |
| Cash and securities segregated under federal and other regulations  |    | 619,451                  |
| Financial instruments owned, at fair value (includes \$4,843,303 pledged as collateral, which the counterparty has right to sell or repledge) |    | 6,517,540                |
| Securities purchased under agreements to resell (includes \$1,967,722 at fair value)  |    | 38,170,850               |
| Receivable under securities borrowing arrangements  |    | 23,514,846               |
| Receivable from customers   |    | 190,665                  |
| Receivable from brokers, dealers, clearing organizations and others   |    | 2,286,667                |
| Goodwill  |    | 10,865                   |
| Other assets  |    | 182,867                  |
| Total assets  | \$ | <u><u>71,580,510</u></u> |

**Liabilities and Stockholder's Equity**

Liabilities:

|  |    |                   |
|--|----|-------------------|
| Short-term borrowings  | \$ | 625,462           |
| Financial instruments sold, not yet purchased, at fair value   |    | 4,783,424         |
| Securities sold under agreements to repurchase                 |    | 61,921,522        |
| Payable to customers   |    | 794,707           |
| Payable to brokers, dealers, clearing organizations and others |    | 1,647,878         |
| Accounts payable and accrued liabilities                       |    | 324,722           |
| Total liabilities  |    | <u>70,097,715</u> |

Commitments and contingent liabilities:

|   |    |                          |
|---|----|--------------------------|
| Liabilities subordinated to claims of general creditors |    | <u>650,000</u>           |
| Total stockholder's equity                              |    | <u>832,795</u>           |
| Total liabilities and stockholder's equity              | \$ | <u><u>71,580,510</u></u> |

The accompanying notes to the statement of financial condition.

**HSBC SECURITIES (USA) INC.**  
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**(1) Organization**

HSBC Securities (USA) Inc. (the Company) is a wholly owned subsidiary of HSBC Markets (USA) Inc. (the Parent), whose ultimate parent is HSBC Holdings plc (HSBC). The Company is an indirect wholly owned subsidiary of HSBC North America Holdings Inc. (HNAH), which is an indirect wholly owned subsidiary of HSBC. For purposes of this report, an “affiliate” is defined as a direct or indirect subsidiary of HSBC.

The Company is a registered broker-dealer of securities under the Securities Exchange Act of 1934 and a registered Futures Commission Merchant (FCM) with the Commodity Futures Trading Commission (CFTC). In 1996, HSBC was granted the authority by the Federal Reserve Board to engage, through the Company, in limited underwriting and dealing activities under the Bank Holding Company Act of 1956, as amended. The Company is engaged in underwriting, dealing, and brokering a full range of debt and equity securities and futures contracts. The Company is also a primary dealer in U.S. Government and government agency securities.

The Company is a member of the Financial Industry Regulatory Authority (FINRA), New York Stock Exchange (NYSE), CME Group Inc. (CME), Intercontinental Exchange (ICE), LCH.Clearnet Ltd (LCH), Securities Investor Protection Corporation (SIPC), and The Options Clearing Corporation (OCC). The Company is eligible to clear over-the-counter derivatives at the CME, ICE and LCH.

The Company is self-clearing for its business other than its retail brokerage business. The Company utilizes Pershing LLC (Pershing), a nonaffiliated broker-dealer, as its clearing agent for its retail securities brokerage transactions. Pershing carries the cash and margin accounts for the Company’s retail brokerage customers (both domestic and international) on a fully disclosed basis.

**(2) Summary of Significant Accounting Policies**

**(a) Basis of Presentation and Use of Estimates**

The Company’s financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) require the use of estimates by management. These estimates and the underlying assumptions affect the amounts of assets and liabilities reported, disclosures about contingent assets and liabilities, and reported amounts of revenues and expenses. Such estimates, including the fair value measurements of certain financial assets and financial liabilities, by their nature, are based on judgment and available information. Actual results could differ from those estimates.

**(b) Cash**

Cash consists of amounts due from banks.

**(c) Financial Instruments Owned and Financial Instruments Sold, Not Yet Purchased**

Financial instruments owned and financial instruments sold, not yet purchased, including debt and equity securities, and derivative transactions, are reported in the statement of financial condition on a

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trade-date basis. Refer to Note 6(b), Financial Instruments Owned, at Fair Value and Financial Instruments Sold, Not Yet Purchased, at Fair Value- Fair Value Measurements and Hierarchy, for further discussion on fair value measurements.

Receivables and payables relating to transactions that have not reached their contractual settlement date are reflected net on the statement of financial condition.

**(d) Collateralized Financing Transactions**

Securities purchased under agreements to resell (reverse repurchase agreements) and securities sold under agreements to repurchase (repurchase agreements) are treated as collateralized financing transactions and are generally recorded at the amount of cash paid or received, plus accrued interest. The Company offsets reverse repurchase and repurchase agreements with the same counterparty and same maturity date, which are subject to master netting arrangements, as permitted by US GAAP. In connection with reverse repurchase agreements, it is the Company's policy to obtain possession of collateral with market value in excess of the principal amount loaned. Collateral is valued daily, and additional collateral is obtained when appropriate.

Receivables under securities borrowing arrangements (securities borrowed) are treated as collateralized financing agreements and are generally recorded at the amount of cash paid, plus accrued interest. Securities borrowed transactions require the Company to deposit cash or other collateral with the lender. The Company monitors the market value of securities borrowed on a daily basis and obtains additional securities as collateral when necessary.

**(e) Fair Value Option**

The fair value option allows the Company to irrevocably elect fair value, on an instrument by instrument basis, as the initial and subsequent measurement attribute for most financial assets, financial liabilities, and unrecognized firm commitments. The guidance permits the Company to elect to measure certain eligible items at their initial recognition or upon occurrence of an event that gives rise to a new basis of accounting for that eligible item. The Company has elected to apply the fair value option to certain reverse repurchase agreements which are trading in nature. For further information on the fair value option related to reverse repurchase agreements, refer to Note 16, *Disclosures Related to Collateralized Financing Activities*.

**(f) Goodwill**

Goodwill, representing the excess of the purchase price over the fair value of identifiable net assets acquired, results from business combinations. The goodwill balance of \$10,865 is not amortized, but is reviewed for impairment on an annual basis at the reporting unit level using a discounted cash flow approach. Goodwill is assessed for impairment annually or when events indicate a possible impairment as required. No impairment was recorded during 2015.

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**(g) *Income Taxes***

The Company is included in HNAH's consolidated federal income tax return and in various combined state income tax returns. As such, the Company has entered into a tax allocation agreement with HNAH and its subsidiary entities (HNAH Group) included in the consolidated return which governs the current amount of taxes to be paid or received by the various entities included in the consolidated return filings. Generally, such agreements allocate taxes to members of the HNAH Group based on the calculation of tax on a separate return basis, adjusted for the utilization or limitation of credits of the consolidated group. To the extent all the tax attributes available cannot be currently utilized by the consolidated group, the proportionate share of the utilized attribute is allocated based on each affiliate's percentage of the available attribute computed in a manner that is consistent with the taxing jurisdiction's laws and regulations regarding the ordering of utilization. In addition, the Company files some separate company state tax returns.

The Company recognizes deferred tax assets and liabilities for the future tax consequences related to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and for state tax credits and state net operating losses. Any Federal tax credits that cannot be currently utilized by the subsidiaries in the HNAH consolidated group are effectively transferred to HNAH and reflected within HNAH's deferred tax assets. Deferred tax assets and liabilities are measured using the enacted tax rates and laws that will be in effect when the deferred tax items are expected to be realized. If applicable, valuation allowances are recorded to reduce deferred tax assets to the amounts the Company concludes are more likely than not to be realized. Since the Company is included in HNAH's consolidated federal tax return and various combined state tax returns, the related evaluation of the recoverability of the deferred tax assets is performed at the HNAH consolidated level. The Company considers the HNAH Group's consolidated deferred tax assets and various sources of taxable income in reaching conclusions on recoverability of deferred tax assets. The HNAH Group evaluates deferred tax assets for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including historical financial performance, projections of future taxable income, future reversals of existing taxable temporary differences, tax planning strategies and any available carryback capacity. In evaluating the need for a valuation allowance, the HNAH Group estimates future taxable income based on management approved business plans. This process involves significant management judgment about assumptions that are subject to change from period to period.

Where a valuation allowance is determined to be necessary at the HNAH consolidated level, such allowance is allocated to principal subsidiaries within the HNAH Group in a manner that is systematic, rational and consistent with the broad principles of accounting for income taxes. The methodology generally allocates the valuation allowance to the principal subsidiaries based primarily on the entity's relative contribution to the HNAH Group's consolidated deferred tax asset against which the valuation allowance is being recorded.

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Further evaluation is performed at the entity level to evaluate the need for a valuation allowance where the Company files separate company state income tax returns. Foreign taxes paid are applied as credits to reduce federal income taxes payable, to the extent that such credits can be utilized.

**(h) Transactions with Related Parties**

In the normal course of business, the Company conducts transactions with HSBC and its subsidiaries. HSBC policy requires that these transactions occur at prevailing market rates and terms and include funding arrangements, derivative transactions, servicing arrangements, information technology support, centralized support services, banking and other miscellaneous services.

**(3) New Accounting Pronouncements Adopted**

***Repurchase to Maturity Transactions, Repurchase Financings, and Disclosures*** In June 2014, the Financial Accounting Standards Board (FASB) issued an Accounting Standards Update (ASU) which changes the accounting for repurchase-to-maturity transactions to secured borrowing accounting and requires secured borrowing accounting for the repurchase agreement in a contemporaneous repurchase financing arrangement. The accounting changes in the ASU were effective beginning January 1, 2015. The ASU also required new disclosure about repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions that are accounted for as secured borrowings to be presented for annual periods beginning January 1, 2015, and for interim periods beginning April 1, 2015. The adoption of this guidance did not have a significant impact on the Company's financial position. See Note 16, Disclosures Related to Collateralized Financing Activities, for the new disclosure required by this standard.

**(4) New Accounting Pronouncements to be Adopted in Future Periods**

***Financial Instruments - Classification and Measurement*** In January 2016, the FASB issued an ASU which changes aspects of its guidance on classification and measurement of financial instruments. The ASU requires equity investments (except those accounted for under the equity method or those that result in consolidation) to be measured at fair value. Under a practicability exception, entities may measure equity investments that do not have readily determinable fair values at cost adjusted for changes in observable prices minus impairment. Under this exception, a qualitative assessment for impairment will be required and, if impairment exists, the carrying amount of the investments must be adjusted to their fair value. For financial liabilities measured under the fair value option, the ASU requires recognizing the change in fair value attributable to our own credit in other comprehensive income. Additionally, the ASU requires new disclosure related to equity investments and modifies certain disclosure requirements related to the fair value of financial instruments. The ASU is effective for all annual and interim periods beginning January 1, 2018 and the guidance should be applied by recording a cumulative effect adjustment to the balance sheet or, as it relates to equity investments without readily determinable fair values, prospectively. Early adoption of the amendment related to financial liabilities measured under the fair value option is permitted. The Company is currently evaluating the impact of adopting this ASU.

There have been no additional accounting pronouncements issued during 2015 or early 2016 that are expected to have or could have a significant impact on the Company's financial position.

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**(5) Cash and Securities Segregated Under Federal and Other Regulations**

As of December 31, 2015, cash of \$415,418 and qualified securities with a market value of \$204,033 have been segregated in special reserve bank accounts for the exclusive benefit of customers in accordance with Regulations 1.32 and 30.7 of the Commodity Exchange Act and Rule 15c3-3 of the Securities Exchange Act of 1934, respectively.

**(6) Financial Instruments Owned, at Fair Value and Financial Instruments Sold, Not Yet Purchased, at Fair Value**

Financial instruments owned, at fair value and financial instruments sold, not yet purchased, at fair value at December 31, 2015, consisted of the following:

|  | <b>Financial<br/>instruments<br/>owned</b> | <b>Financial<br/>instruments<br/>sold, not yet<br/>purchased</b> |
|--|--|--|
| U.S. government treasury notes, bonds, strips, and zeros | \$ 4,148,665                               | \$ 3,994,821   |
| U.S. government agency securities                        | 1,044,542                                  | 237,177  |
| U.S. government treasury bills                           | 101,157                                    | 327  |
| Total U.S. government and government agency securities   | 5,294,364                                  | 4,232,325  |
| Corporate debt   | 948,101                                    | 550,353  |
| Asset-backed securities                                  | 251,210                                    | —  |
| Equities   | 15,936                                     | 1  |
| Municipal securities                                     | 6,834                                      | —  |
| Derivative financial instruments                         | 1,095                                      | 745  |
| Total  | 6,517,540                                  | 4,783,424  |
| Less:  |  |  |
| Financial instruments pledged                            | (4,843,303)                                |  |
| Obligation to return collateral                          |  | (4,533,312)  |
|  | \$ 1,674,237                               | \$ 250,112   |

**(a) Derivative Financial Instruments**

In the normal course of its business, the Company enters into derivative transactions including financial futures contracts, exchange-traded options, securities purchased or sold on a delayed delivery or forward basis, FX forwards and interest rate swaps. These derivative instruments are held for trading purposes and as economic hedges to manage the Company's exposure to market, credit, and interest rate risks. Derivative instruments are recorded at fair value in the statement of financial condition.



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The Company's derivative instruments, executed through regulated exchanges and over the counter markets, at contract or notional amounts, together with their fair values at December 31, 2015, are presented in the following table. Although contract or notional amounts may reflect the extent of the Company's involvement in a particular class of financial instruments, they are not indicative of the potential loss. Securities purchased or sold on a delayed delivery or forward basis had a notional value of \$145,336 at December 31, 2015.

|                            | Contractual/<br>Notional<br>amount | Derivative Assets                          |               | Derivative Liabilities                                       |               |
|----------------------------|------------------------------------|--|---------------|--|---------------|
|                            |                                    | Balance Sheet<br>Location                  | Fair<br>Value | Balance Sheet<br>Location                                    | Fair<br>Value |
| Interest rate derivatives: |                                    |  |               |  |               |
| Futures                    | \$ 3,801,400                       | Financial instruments owned, at fair value | \$ —          | Financial instruments sold, not yet purchased, at fair value | \$ —          |
| Options                    | 4,450,000                          | Financial instruments owned, at fair value | 57            | Financial instruments sold, not yet purchased, at fair value | 10            |
| FX Forwards                | 19,154                             | Financial instruments owned, at fair value | 1,038         | Financial instruments sold, not yet purchased, at fair value | —             |
| Total                      | \$ 8,270,554                       |  | \$ 1,095      |  | \$ 10         |

**(b) Fair Value Measurements and Hierarchy**

Accounting principles related to fair value measurements provide a framework for measuring fair value and focuses on an exit price in the principal (or alternatively, the most advantageous) market accessible in an orderly transaction between willing market participants (the Fair Value Framework). The Fair Value Framework establishes a three-tiered fair value hierarchy with Level 1 representing quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 1 measurements include most Treasury bills, U.S. government and government agency securities (non-callable), active exchange-traded equity securities, and exchange-traded derivatives.

Fair values determined by Level 2 inputs are inputs that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 2 measurements include government agency securities (callable), corporate and municipal bonds,

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reverse repurchase and repurchase agreements, certain equity securities and over-the-counter derivatives.

Level 3 inputs are unobservable inputs for the asset or liability and include situations where there is little, if any, market activity for the asset or liability. Level 3 measurements is mainly comprised of certain equity securities.

In determining the appropriate measurement levels, the Company performs analyses on the assets and liabilities at the end of each reporting period taking into consideration the valuation technique applied in determining fair value. Changes in the observability of significant valuation inputs during the reporting period may result in a reclassification of certain assets and liabilities within the fair value hierarchy upon review. The following table presents information about the Company's fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis at December 31, 2015.

**Fair Value Measurement on Recurring Basis as of December 31, 2015**

|  | <u>Level 1</u>      | <u>Level 2</u>      | <u>Level 3</u>  | <u>Total</u>        |
|--|---------------------|---------------------|-----------------|---------------------|
| Assets:  |                     |                     |                 |                     |
| Securities purchased under agreements to resell          | \$ —                | \$ 1,967,722        | \$ —            | \$ 1,967,722        |
| Financial instruments owned:                             |                     |                     |                 |                     |
| U.S. government treasury notes, bonds, strips, and zeros | 4,148,665           | —                   | —               | 4,148,665           |
| U.S. government agency securities                        | 747,256             | 297,286             | —               | 1,044,542           |
| U.S. government treasury bills                           | 101,157             | —                   | —               | 101,157             |
| Corporate debt   | —                   | 948,101             | —               | 948,101             |
| Asset-backed securities                                  | —                   | 251,193             | 17              | 251,210             |
| Equities   | 8,387               | 122                 | 7,427           | 15,936              |
| Municipal securities                                     | —                   | 6,834               | —               | 6,834               |
| Financial instruments owned, excluding derivative assets | 5,005,465           | 1,503,536           | 7,444           | 6,516,445           |
| Derivative assets  | 57                  | 1,038               | —               | 1,095               |
| Total  | <u>\$ 5,005,522</u> | <u>\$ 3,472,296</u> | <u>\$ 7,444</u> | <u>\$ 8,485,262</u> |

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**Fair Value Measurement on Recurring Basis as of December 31, 2015**

|   | <u>Level 1</u>      | <u>Level 2</u>    | <u>Level 3</u> | <u>Total</u>        |
|---|---------------------|-------------------|----------------|---------------------|
| Liabilities:  |                     |                   |                |                     |
| Financial instruments sold, not yet purchased:                                  |                     |                   |                |                     |
| U.S. government treasury notes, bonds, strips and zeros                         | \$ 3,994,821        | \$ —              | \$ —           | \$ 3,994,821        |
| U.S. government agency securities   | 123,453             | 113,724           | —              | 237,177             |
| U.S. government treasury bills  | 327                 | —                 | —              | 327                 |
| Corporate debt  | —                   | 550,353           | —              | 550,353             |
| Equities  | —                   | 1                 | —              | 1                   |
| Financial instruments sold, not yet purchased, excluding derivative liabilities | 4,118,601           | 664,078           | —              | 4,782,679           |
| Derivative liabilities  | 10                  | 735               | —              | 745                 |
| Total   | <u>\$ 4,118,611</u> | <u>\$ 664,813</u> | <u>\$ —</u>    | <u>\$ 4,783,424</u> |

The Company had no transfers between Level 1 and 2 measurements within the fair value hierarchy.

**(c) Valuation Techniques for Major Assets and Liabilities**

**Debt and Equity Securities**

Where available, equity, debt, preferred securities and exchange-traded derivatives are valued based on quoted market prices. If a quoted market price for the identical security is not available, the security is valued based on quotes from similar securities where possible.

The fair value measurements for Level 2 financial instruments are primarily determined or validated by inputs obtained from independent pricing sources taking into account differences in the characteristics and the performance of the underlying collateral. The Company determines whether adjustments to the observable inputs are necessary as a result of investigations and inquiries about the reasonableness of the inputs used and the methodologies employed by the independent pricing sources.

The valuation of Level 3 debt is less transparent due to ongoing market dislocation and uncertainty. For these securities, the Company applies valuation techniques that may include significant inputs that are unobservable from objective sources (which may include probability of default and loss severity based on the collateral types and the performance assumptions of the collateral). To ensure

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that the valuation presented is appropriate, the Company also compares the valuation output to the hypothetical estimates using the relevant market indices as inputs.

*(d) Additional disclosures for financial assets and liabilities not carried at fair value*

Certain financial assets and liabilities that are not carried at fair value on the statement of financial condition are carried at amounts that approximate fair value due to their short-term nature or repricing terms and generally negligible credit risk. The following table presents information on these financial instruments as of December 31, 2015.

|   | Carrying<br>Value | Estimated<br>fair value | Level 1   | Level 2    | Level 3 |
|---|-------------------|-------------------------|-----------|------------|---------|
| Financial assets:   |                   |                         |           |            |         |
| Cash  | \$ 86,759         | \$ 86,759               | \$ 86,759 | \$ —       | \$ —    |
| Cash segregated pursuant to federal and other regulations           | 415,418           | 415,418                 | 415,418   | —          | —       |
| Securities segregated pursuant to federal and other regulations     | 204,033           | 204,033                 | —         | 204,033    | —       |
| Securities purchased under agreements to resell                     | 36,203,128        | 36,203,128              | —         | 36,203,128 | —       |
| Receivable under securities borrowing arrangements                  | 23,514,846        | 23,514,846              | —         | 23,514,846 | —       |
| Receivable from customers   | 190,665           | 190,665                 | —         | 190,665    | —       |
| Receivable from brokers, dealers, clearing organizations and others | 2,286,667         | 2,286,667               | —         | 2,286,667  | —       |
| Financial Liabilities:  |                   |                         |           |            |         |
| Short-term borrowings   | 625,462           | 625,462                 | —         | 625,462    | —       |
| Securities sold under agreement to repurchase                       | 61,921,522        | 61,921,522              | —         | 61,921,522 | —       |
| Payable to customers  | 794,707           | 794,707                 | —         | 794,707    | —       |
| Payable to brokers, dealers, clearing organizations and others      | 1,647,878         | 1,647,878               | —         | 1,647,878  | —       |
| Liabilities subordinated to claims of general creditors             | 650,000           | 650,000                 | —         | 650,000    | —       |

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**(7) Receivable from and Payable to Brokers, Dealers, Clearing Organizations and Others**

The balances shown as receivable from and payable to brokers, dealers, clearing organizations and others comprise the following:

|  |                     |
|--|---------------------|
| Receivable from:                             |                     |
| Fail to deliver                              | \$ 1,245,923        |
| Exchanges and clearing organizations         | 860,472             |
| Other receivables from brokers and dealers   | <u>180,272</u>      |
|  | <u>\$ 2,286,667</u> |
| Payable to:                                  |                     |
| Fail to receive                              | \$ 1,121,211        |
| Securities transactions not yet settled, net | 449,215             |
| Exchanges and clearing organizations         | 76,639              |
| Other payables to brokers and dealers        | <u>813</u>          |
|  | <u>\$ 1,647,878</u> |

**(8) Other Assets**

The composition of other assets at December 31, 2015 was as follows:

|  |                   |
|--|-------------------|
| Accrued interest receivable                          | \$ 63,959         |
| Receivables from affiliates                          | 59,034            |
| Internally generated software, net                   | 23,969            |
| Deferred tax assets, net                             | 18,206            |
| Prepaid expenses                                     | 4,346             |
| Exchange memberships, at cost (market value \$1,920) | 255               |
| Other  | <u>13,098</u>     |
|  | <u>\$ 182,867</u> |

**(9) Short-Term Borrowings**

Short-term borrowings represent unsecured loans used to finance operations, including the securities settlement process.

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At December 31, 2015, loans of \$125,000 and \$500,000 each were outstanding under uncommitted and committed unsecured credit lines with an affiliate. These credit facilities mature on November 13, 2017 and May 30, 2016, respectively.

Committed unsecured facilities represent contractual lines of credit with annual renewal dates. The committed unsecured bank lines have various maturity dates through November 29, 2016. Uncommitted unsecured and secured facilities represent lines of credit without a contractual obligation to fund that facility. These committed and uncommitted facilities are used to fund the day-to-day operations of the Company. At December 31, 2015, the Company had undrawn unsecured credit facilities totaling \$3,906,000, of which \$3,025,000 was from an affiliate and \$881,000 was from third party banks. Of the \$3,025,000 affiliate facilities, \$2,775,000 was uncommitted and \$250,000 was committed. Of the \$881,000 third party bank facilities, \$406,000 was uncommitted and \$475,000 was committed.

Interest rates on short-term borrowings are at market interest rates as of December 31, 2015.

In light of current market conditions, the Company has determined that an adverse change has not occurred for line of credit arrangements that could require acceleration of repayment or termination of lines of credit.

**(10) Related Parties**

In the normal course of business, the Company conducts transactions with HSBC and its subsidiaries. HSBC policy requires that these transactions occur at prevailing market rates and terms and include funding arrangements, derivative transactions, servicing arrangements, information technology support, centralized support services, banking and other miscellaneous services. The following tables and discussions below present the more significant related party balances.

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Balances and amounts resulting from transactions with related parties included in the statement of financial condition are presented below:

|   |    |            |
|---|----|------------|
| Assets:   |    |            |
| Cash  | \$ | 51,741     |
| Financial instruments owned, at fair value  |    | 98,349     |
| Securities purchased under agreements to resell   |    | 10,213,655 |
| Receivable from customers   |    | 26,707     |
| Receivable from brokers, dealers, clearing organizations and others                                       |    | 134,165    |
| Other assets  |    | 62,448     |
| Liabilities:  |    |            |
| Short-term borrowings   | \$ | 625,351    |
| Securities sold under agreements to repurchase  |    | 7,947,846  |
| Financial instruments sold not yet purchased, at fair value   |    | 735        |
| Payable to customers  |    | 535,808    |
| Payable to brokers, dealers, clearing organizations and others  |    | 365,760    |
| Accounts payable and accrued liabilities  |    | 38,209     |
| Liabilities subordinated to claims of general creditors:  |    |            |
| Floating rate revolving subordinated loan due June 15, 2019<br>at three-month LIBOR plus 150 basis points | \$ | 650,000    |

**Funding and Derivative Related Arrangements with HSBC Affiliates:**

The Company has entered into revolving subordinated loan agreements with two affiliates. The Company has a \$700,000 revolving subordinated loan facility due May 15, 2019 with HNAH at three-month LIBOR plus 150 basis points. As of December 31, 2015, the Company has drawn \$650,000 from the total facility of \$700,000. The Company also has a \$500,000 revolving subordinated loan facility due March 15, 2017 with HSBC USA Inc. at LIBOR plus 300 basis points. As of December 31, 2015, no amount has been drawn from the total facility of \$500,000.

The subordinated loans are covered by an agreement approved by FINRA and are, therefore, available in computing net capital under the Securities and Exchange Commission (SEC)'s Uniform Net Capital Rule. To the extent that such borrowings are required for the Company's continued compliance with minimum net capital requirements, they may not be repaid.

At December 31, 2015, the Company has entered into FX forwards, and interest rate forwards with affiliates for notional values of \$19,154 and \$145,336 respectively. The fair values were \$1,038 and \$(735), respectively. As part of its collateralized financing activities, the Company has entered into reverse repurchase agreements and repurchase agreements with affiliates for contract values of \$10,213,655 and \$7,947,846 respectively.

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**(11) Post Retirement Benefits**

The Company's employees participate, to the extent they meet minimum eligibility requirements, in various benefit plans sponsored by HNAH and HSBC. Employees of the Company are covered under HNAH's noncontributory defined benefit pension plan and defined contribution pension plan. In addition, certain employees of the Company are covered under HNAH's welfare benefit plan providing retiree medical benefits. These plans are subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA). HNAH reserves the right to amend, suspend, or terminate the plans and the benefits provided to the extent permitted by law, in whole or in part, at any time and for any reason. There are no separate plans solely for employees of the Company and therefore, pension expenses and other postretirement employee benefits expenses for the Company are determined based on employee participation in the plans and are recorded through an intercompany charge from HNAH, which is cash settled monthly. The following is a discussion of HNAH's significant benefit plans.

**(a) Pension Plan**

The HSBC – North America (U.S.) Pension Plan (Pension Plan) is a defined benefit pension plan sponsored by HNAH. The Pension Plan has both a final average pay formula, which uses base pay and years of credited service, and a cash balance formula. Participants become fully vested after three years of service.

The final average pay formula covered all employees of the Company hired prior to January 1, 1997 who attained the age of 21 and completed one year of eligibility service, defined generally as a minimum of 1,000 hours in a 12-month period.

Employees hired on or after January 1, 1997 qualify for the cash balance formula, which provides employees who have attained the age of 21 and have completed one year of eligibility service with the Company paid retirement account credits equal to 2% of eligible pay plus interest credits. The definition of eligible pay includes base pay, bonus pay, commissions, and overtime.

In November 2009, the HNAH Board of Directors approved a plan to cease all future benefit accruals of final average pay formula participants effective January 1, 2011. Any service or pay earned by such participants after December 31, 2010 will not be used in benefit calculations under the final average pay formula. However, continued employment with a participating HSBC employer will maintain a participant's eligibility to reach age and service milestones for early retirement subsidies and features which may be available under the formula. Pension Plan accruals of all eligible participants beginning January 1, 2011, including participants who had accrued a benefit under the final average pay formula, will only be provided under the cash balance formula.

In July 2012, the HNAH Board of Directors approved a plan to cease all future benefit accruals of cash balance formula participants effective January 1, 2013. Any service or pay earned by such participants after December 31, 2012, will not be used for benefit calculations under the cash balance formula. Interest rate credits will continue to be credited to existing cash balance accounts until the account is distributed to the participant or beneficiary(ies) of the account.



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The costs of the Pension Plan have been actuarially determined. No separate determination has been made of the actuarial present value of accumulated benefits and the Pension Plan's net assets as they relate to the employees of the Company.

**(b) Defined Contribution Plan**

Employees of the Company participate in the HNAH 401(k) savings plan if they meet certain eligibility requirements. Under these plans, each participant's contribution is matched up to a maximum of 6 percent of the participant's compensation. Contributions are in the form of cash.

**(c) Retiree Medical**

The HSBC – North America (U.S.) Retiree Health Plan (Retiree Health Plan) is an employee welfare benefit plan sponsored by HNAH. Employees of the Company who were hired before January 1, 1993 (except certain former Republic National Bank employees) are generally eligible to participate in the retiree medical benefit component of the Retiree Health Plan provided that, at the time the employee retires, the employee is employed by the Company as a regular full-time employee, qualifies for an immediate pension benefit from the Pension Plan, and meets certain age and service requirements. Employees hired or rehired by the Company on or after January 1, 1993 are not eligible for retiree medical benefits.

The premium amount paid by retirees for retiree medical benefit coverage varies by type of coverage, retirement date and total years of credited service, although the Company generally pays the entire cost of coverage for individuals who retired before January 1, 1993, subject to a contribution limitation based on the cost of coverage in 1992. Prior to August 1, 2015, the coverage for retirees over age 65 was limited to a Medicare supplement plan with a lifetime maximum of \$20 per covered person.

In July 2015, the HNAH Board of Directors approved a change in the way health benefits are provided for retirees over age 65. Effective August 1, 2015, these retirees were transitioned to a Retiree Health Reimbursement Arrangement Plan (HRA Component), a new component of the Retiree Health Plan. The HRA Component provides retirees with a health reimbursement account (HRA) and catastrophic prescription drug benefits, and works in conjunction with a private insurance exchange on which retirees may purchase individual Medicare supplemental coverage. The HRA can be used to reimburse retirees for premiums incurred in connection with their individual Medicare supplemental coverage and other eligible medical expenses.

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**(12) Stock Option Plans and Restricted Share Plan**

Certain employees of the Company participate in HSBC's long-term stock-based incentive plans, which provide for grants of common stock-based awards, including stock options and restricted share units (RSUs) described below. There are no separate plans solely for employees of the Company.

**(a) *HSBC Holdings Savings-Related Share Option Plan***

Options have been granted to employees of the Company under the HSBC Holdings Savings-Related Share Option Plan. Under the plan, employees have the choice to buy shares in HSBC at a discounted price fixed at the beginning of a one, three, or five-year contribution period. Employee contributions to the plan cannot exceed \$400 per month. At the end of the one, three, or five-year periods, employees have a six month period to exercise their option to buy HSBC shares or receive the cash equivalent of selling all or a portion of the shares back to the Company at the market price at the date of exercise. The Plan has been discontinued.

Options outstanding at December 31, 2015 were 85,474. The weighted average price outstanding was \$7.11. The weighted average vesting period for options outstanding, at December 31, 2015, was 0.75 years. There were 39,422 options exercisable at December 31, 2015. The exercise price on options outstanding was between \$6.52 and \$8.09.

**(b) *Employee Stock Purchase Plans***

During 2014, HSBC introduced the HSBC International Employee Share Purchase Plan (the "HSBC ShareMatch Plan"). The HSBC ShareMatch Plan allows eligible employees to purchase HSBC shares with a maximum monthly purchase of \$400. For every three shares purchased under the HSBC ShareMatch Plan (the "Investment Share") the employee is awarded an additional share at no charge (the "Matching Share"). The Investment Share is fully vested at the time of purchase while the Matching Share vests at the end of three years contingent upon continuing employment with the HSBC Group.

**(c) *Restricted Share Plan***

Under the HSBC Group Share Plan, share-based awards have been granted to key employees typically in the form of restricted share units (RSUs). These RSUs are recorded as a liability over the relevant vesting period and the Company delivers cash to HSBC when the shares vest to the employees.

**(d) *Fixed Pay Allowance***

Beginning in 2014, a fixed pay allowance ("FPA") program was introduced which grants HSBC shares to certain key employees on a quarterly basis. The FPA shares are not linked to the achievement of any performance conditions and they vest immediately. However, these shares are subject to various retention periods of up to five years based on the role of the employee.

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**(13) Income Taxes**

Under the income tax allocation agreement with the Parent, the Company's U.S. federal, state and local income taxes are provided on a separate entity basis. The Company has \$15,494 current income tax payable, net to the Parent at December 31, 2015.

The effective tax rate of 160.9% for 2015 is mainly driven by the release of valuation allowance reserves on previously unrecognized state net operating loss carryforwards and temporary differences and the effects of revaluing our deferred tax assets for New York City tax reform that was enacted on April 13, 2015.

Pursuant to the agreement with the Parent, the tax effects of temporary differences are included in intercompany tax settlements with the Parent. The Company had \$18,206 deferred income tax receivable from the Parent at December 31, 2015. In absence of such an agreement, the Company would have reported net deferred income tax assets of \$312,840 at December 31, 2015, as follows:

|  |                         |
|--|-------------------------|
| Deferred Tax Assets:                               |                         |
| Net operating loss carryforward, Federal and State | \$ 51,939               |
| New York State subtraction pool                    | 180,942                 |
| Deferred compensation                              | 75,403                  |
| Capitalization Costs                               | 28,498                  |
| Other  | <u>14,653</u>           |
| Gross deferred tax asset                           | 351,435                 |
| Valuation allowance:                               | <u>(33,009)</u>         |
| Deferred tax assets, net of valuation allowance    | <u>318,426</u>          |
| Deferred Tax liabilities:                          |                         |
| Underwriting fees                                  | 1,223                   |
| Performance fees                                   | <u>4,363</u>            |
| Gross deferred tax liability                       | <u>5,586</u>            |
| Net Deferred Tax Assets                            | <u>312,840</u>          |
| Intercompany tax settlements                       | <u>294,634</u>          |
| Net deferred tax assets after settlements          | <u><u>\$ 18,206</u></u> |

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The Internal Revenue Service commenced its examination of the HNAH Group's 2012 and 2013 federal income tax returns in the first quarter of 2015 and is expected to conclude its examination in 2016.

The Company remains subject to state and local income tax examinations for years 2003 and forward. The Company is currently under audit by various state and local tax jurisdictions. Uncertain tax positions are reviewed on an ongoing basis and are adjusted in light of changing facts and circumstances, including progress of tax audits, developments in case law and the closing of statute of limitations. Such adjustments are reflected in the tax provision.

As of December 31, 2015, for federal tax purposes, the Company has separate return net operating loss carry forwards of \$87,766 of which \$7,569 expire in 2018, \$76,755 expire in 2022, and \$3,442 expire in 2023 and separate return alternative minimum tax credits of \$2,291 which have no expiry.

At December 31, 2015, for state and local tax purposes, the Company had apportioned and pre-tax effected net operating loss carryforwards of \$32,647 which expire in 2034.

For 2015, the Company had no unrecognized tax benefits. It is reasonably possible that there could be a change in the amount of our unrecognized tax benefits within the next 12 months due to settlements in various state and local tax jurisdictions.

It is the Company's policy to recognize accrued interest related to unrecognized tax positions. The Company had no unrecognized tax benefits at December 31, 2015.

**(14) Commitments and Contingent Liabilities**

**(a) Guarantees**

In the normal course of business, the Company provides guarantees to securities clearing organizations, exchanges and central clearing counterparties. These guarantees are generally required under the standard membership agreements, such that members are required to guarantee the performance of other members. To mitigate these performance risks, the clearing organizations, exchanges and central clearing counterparties often require members to post collateral. The Company's obligation under such guarantees could exceed the collateral amounts posted; however, the potential for the Company to be required to make payments under such agreements is deemed remote.

**(b) Commitments**

At December 31, 2015, the Company had entered into forward starting reverse repurchase agreements and repurchase agreements of \$170,966 and \$803,051, respectively. All contracts expire either before or on February 16, 2016.

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**(c) Leases**

At December 31, 2015, the Company was obligated under various lease agreements with an affiliated entity relating to property used for office space and business purposes. These lease agreements will expire on December 31, 2016.

**(d) Litigation and Regulatory Matters**

In addition to the matters described below, in the ordinary course of business, the Company is routinely named as a defendant in, or as party to, various legal actions and proceedings relating to activities of our current and/or former operations. These legal actions and proceedings may include claims for substantial or indeterminate compensatory or punitive damages, or for injunctive relief. In the ordinary course of business, the Company also is subject to governmental and regulatory examinations, information-gathering requests, investigations and proceedings (both formal and informal), certain of which may result in adverse judgments, settlements, fines, penalties, injunctions or other relief. In connection with formal and informal inquiries by these regulators, the Company receives numerous requests, subpoenas and orders seeking documents, testimony and other information in connection with various aspects of its regulated activities.

In view of the inherent unpredictability of legal matters, including litigation, governmental and regulatory matters, particularly where the damages sought are substantial or indeterminate or when the proceedings or investigations are in the early stages, the Company cannot determine with any degree of certainty the timing or ultimate resolution of such matters or the eventual loss, fines, penalties or business impact, if any, that may result. The Company establishes reserves for litigation, governmental and regulatory matters when those matters present loss contingencies that are both probable and can be reasonably estimated. Once established, reserves are adjusted from time to time, as appropriate, in light of additional information. The actual costs of resolving litigation, governmental and regulatory matters, however, may be substantially higher than the amounts reserved for those matters.

Based on the facts currently known, in respect of each of the below investigations, it is not practicable at this time for us to determine the terms on which these ongoing investigations will be resolved or the timing of such resolution or for us to estimate reliably the amounts, or range of possible amounts, of any fines and/or penalties. As matters progress, it is possible that any fines and/or penalties could be significant.

Given the substantial or indeterminate amounts sought in certain of these matters, and the inherent unpredictability of such matters, an adverse outcome in certain of these matters could have a material adverse effect on our financial statements in any particular period.

Participants in the U.S. mortgage securitization market that purchased and repackaged whole loans have been the subject of lawsuits and governmental and regulatory investigations and inquiries, which have been directed at groups within the U.S. mortgage market, such as servicers, originators, underwriters, trustees or sponsors of securitizations, and at particular participants within these groups. The Company previously participated in residential loan securitization activities as an

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underwriter. From 2005 to 2007, the Company acted as underwriter for approximately \$34 billion of securities issued by affiliates, and the Company also acted as underwriter for \$42 billion of securities issued by third-parties. As an underwriter, the Company's risks primarily relate to misrepresentations or omissions in the offering documents and other client communications.

The Company currently has been named as a defendant in a number of actions in its role as underwriter of residential mortgage-backed securities ("RMBS"), which generally allege that the offering documents for securities issued by securitization trusts contained material misstatements and omissions, including statements regarding the underwriting standards governing the underlying mortgage loans. As an underwriter of securities issued by affiliates, the Company may be entitled to indemnification by its affiliates. Those affiliates may, in turn, be entitled to indemnification as well. Additionally, as an underwriter of securities issued by third-parties, the Company may be entitled to indemnification by the issuer of the security. While these indemnities were intended to protect the Company from exposure to liability, it is possible that the enforceability of these indemnities may be challenged, or that collection of indemnity payments may be impaired due to the financial condition of the indemnifying party. In cases where the Company is named as a defendant along with its affiliates, the Company expects to allocate any potential judgment or other potential payment in connection with these matters among the various HSBC entities with potential exposure.

In May 2012, the Federal Deposit Insurance Corporation, acting in its capacity as receiver for Citizens National Bank, filed an action against the Company and 16 other institutions seeking damages or rescission of mortgage-backed securities that were underwritten and sold by the defendants, including the Company. The action is captioned, Federal Deposit Insurance Corporation as receiver for Citizens National Bank, v. Bear Stearns Asset Backed Securities I, LLC, et al., (12-CV-4000). In March 2015 the court granted the defendants' consolidated motion to dismiss. FDIC has appealed that ruling. We await the outcome of the appeal. In August 2012, the Federal Deposit Insurance Corporation, acting in its capacity as receiver for Colonial Bank, filed two nearly identical actions, one in the US District Court for the Southern District of New York and the other in the Circuit Court of Montgomery County, Alabama, against the Company and several other institutions. The complaints seek damages or rescission of mortgage-backed securities that were underwritten and sold by the defendants, including the Company. The actions are captioned Federal Deposit Insurance Corporation, as receiver for Colonial Bank, case nos. 12 CIV 6166 and 03-CV-2012-901035.00, respectively. The Company is sued as an underwriter only, and has confirmed its right to indemnification by the issuers of the securities at issue in those actions as they concern the Company. These actions are in early stages. At this time the Company is unable to reasonably estimate the liability, if any, that might arise as a result of these actions.

Since 2010, various HSBC entities including the Company have received certain subpoenas and requests for information from U.S. authorities seeking production of documents and information relating to HSBC's involvement, and the involvement of its affiliates, in specified private-label RMBS transactions as an issuer, sponsor, underwriter, depositor, trustee, custodian or servicer. HSBC continues to cooperate with these authorities.

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In November 2014, HNAH, on behalf of itself and subsidiaries, including, but not limited to, HSBC Bank USA N.A. (HBUS), HSI Assets Securitization Corporation (HASCO), the Company, HSI Asset Loan Obligation, HSBC Mortgage Corporation (USA), HSBC Finance Corporation (HBIO) and Decision One Mortgage Company LLC, received a subpoena issued by the US Attorney's Office, District of Colorado, pursuant to the Financial Industry Reform, Recovery and Enforcement Act of 1989, 12 U.S.C. § 1833a ("FIRREA"), concerning the origination, financing, purchase, securitization and servicing of subprime and non-subprime residential mortgages. We are cooperating fully with US authorities and are continuing to produce documents and information responsive to their requests.

The Company expects these types of claims to continue. As a result, the Company may be subject to additional claims, litigation and governmental and regulatory scrutiny related to its participation in the U.S. mortgage securitization market, either individually or as a member of a group.

The Company continues to cooperate in a review of its AML/BSA compliance program by the Financial Industry Regulatory Authority ("FINRA"), which was initiated in the third quarter of 2012.

In July 2013, HSBC Bank plc and certain of its affiliates, including the Company, and 13 other investment banks received a Statement of Objections from the European Commission relating to its ongoing investigation of alleged anti-competitive activity by a number of market participants in the credit derivatives market between 2006 and 2009. The Statement of Objections sets out the European Commission's preliminary views and does not prejudice the final outcome of its investigation. The HSBC entities responded to the Statement of Objections and attended an oral hearing in May 2014. Following the oral hearing, the European Commission decided to conduct a further investigation phase before deciding whether or how to proceed with the case. In December 2015, the European Commission announced that based on a thorough analysis of all the information received from the parties in their responses to the Statement of Objections and during the oral hearing, as well as the results of additional fact finding conducted by the European Commission after the oral hearing, it had decided to close the case against all 13 investment banks, including all of the HSBC entities.

Since March 2014, numerous putative class actions have been filed in the US District Courts for the Southern District of New York, the District of New Jersey and the Northern District of California naming HBUS, HSBC Bank plc, the Company and other members of The London Gold Market Fixing Limited as defendants. The complaints allege that, from January 2004 to the present, defendants conspired to manipulate the price of gold and gold derivatives during the afternoon London gold fix in order to reap profits on proprietary trades. These actions have been assigned to and consolidated in the New York District Court. An amended consolidated class action complaint was filed in December 2014, and defendants filed a consolidated response in February 2015. Plaintiffs filed a second consolidated amended complaint in March 2015. Defendants filed a motion to dismiss in April 2015. The motion is fully briefed. A hearing has been scheduled for March 2016.

Since July 2014, putative class actions were filed in the US District Court for the Southern District of New York and the Eastern District of New York naming HSBC, HNAH, HBUS, HSBC USA Inc. and other members of The London Silver Market Fixing Ltd as defendants. The complaints allege

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that, from January 2007 to the present, defendants conspired to manipulate the price of physical silver and silver derivatives for their collective benefit in violation of US antitrust laws and the CEA. These actions have been assigned to and consolidated in the New York District Court. Plaintiffs filed a consolidated amended complaint in January 2015, which defendants moved to dismiss in March 2015. In response thereto, plaintiffs filed a second amended consolidated complaint in April 2015. Defendants' motion to dismiss the second amended consolidated complaint was filed in May 2015. The motion is fully briefed. A hearing has been scheduled for March 2016.

In December 2015 a putative class action "Notice of Action" was filed in the Superior Court of Justice, Ontario Province, Canada, against, among others, HSBC, HSBC Bank plc, HSBC USA, the Company, HSBC Bank Canada and HSBC Securities Canada. The Notice of Action alleges, among other things, that defendants conspired to manipulate the price of gold and gold derivatives during the London Gold Fix. The action is at an early stage.

Since July 2015, putative class actions were filed in various US District Courts around the country naming the Company and twenty-one other institutions that serve as primary dealers for US Treasury securities. The complaints generally allege that the defendants conspired to manipulate the US Treasury auction market by inflating prices in the "when issued" market and deflating prices during the auctions. The class is defined to include anyone who transacted in US treasuries between January 1, 2007 and December 31, 2012. These cases have been consolidated and transferred to the US District Court for the Southern District of New York. These matters are at a very early stage.

**(15) Risk Management**

***Financial Instruments with Off-Balance-Sheet Risk***

In the normal course of business, the Company's customer and trading activities involve the execution, settlement, and financing of various securities and financial instrument transactions. These activities may expose the Company to off-balance-sheet risk in the event the customer or other broker is unable to fulfill its contracted obligations and the Company has to purchase or sell the financial instrument underlying the contract at a loss.

As part of the Company's financing and securities settlement activities, the Company uses securities as collateral to support various secured financing sources. In the event the counterparty is unable to meet its contractual obligation to return securities pledged as collateral, the Company may be exposed to the risk of acquiring the securities at prevailing market prices in order to satisfy its obligations. The Company controls this risk by monitoring the market value of financial instruments pledged on a daily basis and by requiring adjustments of collateral levels in the event of excess market exposure.

***Concentrations of Market Risk***

In the normal course of its operations, the Company enters into various contractual commitments involving forward settlement. These include financial futures contracts, options contracts, and commitments to buy and sell securities. The potential for changes in the market value of our trading positions is referred to as



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market risk. Such positions result from market-making, proprietary trading, and investing activities. All of the Company's inventory positions are marked-to-market.

The Company monitors and manages its market risk exposure by setting market risk limits and by reviewing the effectiveness of economic hedging strategies. The Company's policy is to take possession of securities purchased under agreements to resell and securities borrowed and maintain these securities with its custodian. The Company monitors the market value of the assets acquired to ensure their adequacy as compared to the amount at which the securities will be subsequently resold, as specified in the respective agreements. The agreements provide that, where appropriate, the Company may require the delivery of additional collateral.

The Company records all contractual commitments involving future settlement at fair value. Futures contracts are exchange traded and cash settlement is made on a daily basis for market movements. Margin on futures contracts is included in receivable from and payable to brokers, dealers, and clearing organizations.

***Concentrations of Credit Risk***

Credit risk is measured by the loss that the Company would record if its counterparties failed to perform pursuant to the terms of contractual commitments. Management of credit risk involves a number of considerations, such as the financial profile of the counterparty, specific terms, and duration of the contractual agreement, market fluctuations, and the value of collateral held, if any. The Company has established various procedures to manage credit exposure, including initial credit approval, credit limits, collateral requirements, rights of offset, and continuous oversight.

The Company regularly transacts business with, and owns securities issued by, a range of corporations, governments and agencies, and other financial institutions. The Company also enters into collateralized financing agreements in which it extends short-term credit, primarily to major financial institutions, including major U.S. and non-U.S. commercial banks, investment banks, and affiliates.

The Company generally controls access to the collateral pledged by the counterparties, which consists largely of securities issued by the U.S. Government and government agencies. The value and adequacy of the collateral are continually monitored. Consequently, management believes the risk of credit loss from counterparties' failure to perform in connection with collateralized lending activities is minimal.

Remaining concentrations arise principally from financial or contractual commitments involving future settlements, fixed income securities, and equity securities. Concentrations are diverse with respect to geographic locations and industries of counterparties.

Substantially all of the Company's cash and securities positions are either held as collateral by its clearing brokers and banks against various margin obligations of the Company or deposited with such clearing brokers and banks for safekeeping purposes.

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***Liquidity Risk***

Liquidity risk is the risk that an institution will be unable to meet its obligations as they become due or fund its activities because of an inability to liquidate assets or obtain adequate funding. The Company continuously monitors the impact of market events on liquidity positions. Liquidity is managed to provide the ability to generate cash to meet securities settlements and other commitments at a reasonable cost in a reasonable amount of time while maintaining routine operations and market confidence. Liquidity is managed at the major entity level within HNAH. Each entity is required to maintain sufficient reliable liquidity to support itself through a 90 day stress event in which both the markets are stressed and HSBC is under pressure globally. In addition, liquidity is managed on a standalone legal entity basis with no reliance on any HSBC Group entity unless pre-committed. As discussed in Note 10, *Related Parties*, the Company does obtain some liquidity support through borrowing arrangements with its affiliates.

***Operational Risk Management***

Operational risk results from inadequate or failed internal processes, people and systems or from external events, including legal risk. Operational risk is relevant to every aspect of the Company's business and covers a wide spectrum of risks. The Company's strategy is to manage operational risks in a cost effective manner, within targeted levels consistent with the risk appetite. The operational risk management framework ensures minimum standards of governance and organization over operational risk and internal control throughout the Company and covers all businesses and operations (including all entities, activities, processes, systems and products).

***Compliance Risk Management***

Compliance risk is the risk that the Company fails to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice. It is a composite risk that can result in regulatory sanctions, financial penalties, litigation exposure and loss of reputation. Compliance risk is inherent throughout the organization. All Company employees are required to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice.

The enterprise-wide program in HNAH is designed in accordance with its policy and the principles established by the Federal Reserve Board in Supervision and Regulation Letter 08-8 (SR 08-8) dated October 16, 2008. By leveraging industry-leading practices and taking an enterprise-wide, integrated approach to managing compliance risks, the Company can better identify and understand its compliance requirements, monitor its compliance risk profile, and assess and report its compliance performance across the organization. The Company's enterprise-wide compliance risk management program is designed to promote a consistent understanding of roles and responsibilities, as well as consistency in compliance program activities. The program is structured to pro-actively identify as well as quickly react to emerging issues and to, assess, control, measure, monitor and report compliance risks across the company, both within and across business lines, support units, jurisdictions and legal entities.

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**(16) Disclosures Related to Collateralized Financing Activities**

*(a) Offsetting*

The Company accounts for transactions subject to reverse repurchase and repurchase agreements, and securities borrowing arrangements as collateralized financings, and those with a single counterparty are presented net on the balance sheet, provided certain criteria are met that permit balance sheet offsetting under US GAAP. Most transactions subject to these agreements do not meet those criteria and thus are not eligible for balance sheet offsetting. Collateral pledged and received consists of securities, and is not offset on the balance sheet against the related collateralized assets and liabilities.

The following table presents the gross reverse repurchase agreements, securities borrowing arrangements and repurchase agreements, and the related offsetting amount permitted under US GAAP at December 31, 2015. The table also includes amounts related to financial instruments that are not permitted to be offset but would be eligible for offsetting to the extent that an event of default occurred and a legal opinion supporting enforceability of the offsetting rights has been obtained. Remaining exposures continue to be secured by financial collateral, but the Company may not have sought or been able to obtain a legal opinion evidencing enforceability of the offsetting right. In some jurisdictions and for some counterparty types, the insolvency law for a particular counterparty type may be ambiguous. For example, this may be the case for certain government entities and U.S. pension plans.

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December 31, 2015

(Dollars in thousands)

|  | <u>Gross Amounts Not Offset</u>     |  |   |                                      |   |                           |
|--|-------------------------------------|--|---|--------------------------------------|---|---------------------------|
|  | <u>Gross Amounts<br/>Recognized</u> | <u>Gross Amounts<br/>Offset in the<br/>Balance Sheet (1)</u> | <u>Net Amounts<br/>Presented in the<br/>Balance Sheet</u> | <u>Financial<br/>Instruments (2)</u> | <u>Cash<br/>Collateral<br/>Received</u> | <u>Net Amount<br/>(3)</u> |
| Securities purchased under agreements to resell (enforceable)(4)     | \$ 61,206,899                       | \$ (32,177,380)  | \$ 29,029,519   | \$ 29,028,510                        | \$ —                                    | \$ 1,009                  |
| Securities purchased under agreements to resell (nonenforceable)     | 9,141,331                           |  | 9,141,331   | 9,125,392                            | —                                       | 15,939                    |
| Receivables under securities borrowing arrangements (enforceable)    | 13,220,400                          |  | 13,220,400  | 13,084,094                           | —                                       | 136,306                   |
| Receivables under securities borrowing arrangements (nonenforceable) | 10,294,445                          |  | 10,294,445  | 10,071,709                           | —                                       | 222,736                   |
| Securities sold under agreements to repurchase (enforceable)         | 60,947,485                          | (32,177,380)   | 28,770,104  | 28,754,605                           | —                                       | 15,499                    |
| Securities sold under agreements to repurchase (nonenforceable)      | 33,151,418                          |  | 33,151,418  | 33,150,962                           | —                                       | 456                       |

(1) Represents recognized amount of reverse repurchase and repurchase agreements with counterparties subject to legally enforceable netting that meet the applicable netting criteria as permitted by generally accepted accounting principles.

(2) Represents securities received or pledged to cover financing transaction exposures.

(3) Represents the amount of our exposure that is not collateralized / covered by pledged collateral.

(4) The Company has elected the fair value option for reverse repurchase agreements totalling \$1,967,722.

**HSBC SECURITIES (USA) INC.**  
(An Indirect Wholly Owned Subsidiary of HSBC Holdings plc)

Notes to Financial Statements

December 31, 2015

(Dollars in thousands)

**(b) Collateral Pledged In and Pledged Out Associated with Collateralized Financing Activities**

The following table provides the class of collateral pledged and remaining contractual maturity of repurchase agreements accounted for as secured borrowings as of December 31, 2015:

|  | <u>Overnight<br/>and<br/>Continuous</u> | <u>Up to 30 days</u> | <u>30 to 90 days</u> | <u>Greater than 90<br/>days</u> | <u>Total</u>         |
|--|---|----------------------|----------------------|---------------------------------|----------------------|
| U.S. Government and government agency securities | \$ 66,029,503                           | \$ 17,777,659        | \$ 4,678,263         | \$ 806,777                      | \$ 89,292,202        |
| Corporate debt                                   | 3,615,170                               | 22,829               | —                    | 900,723                         | 4,538,722            |
| Asset-backed securities                          | 265,150                                 |                      |                      |                                 | 265,150              |
| Municipal securities                             | 2,829                                   |                      |                      |                                 | 2,829                |
|  | <u>\$ 69,912,652</u>                    | <u>\$ 17,800,488</u> | <u>\$ 4,678,263</u>  | <u>\$ 1,707,500</u>             | <u>\$ 94,098,903</u> |

As part of its financing activities, the Company has also accepted collateral that it is permitted to sell or repledge, the fair value of which was \$94,065,984 as of December 31, 2015. Collateral in the amount of \$93,727,222 has been sold or repledged. This is in excess of amounts recorded in the statement of financial condition due to various netting arrangements.

**(17) Net Capital Requirements**

The Company is subject to the Uniform Net Capital Rule (15c3-1) of the SEC, Regulation 1.17 of the CFTC, and the capital rules of the FINRA. The Company has elected to use the alternative method, permitted by Rule 15c3-1, which requires that it maintains a minimum net capital, as defined, equal to the greater of \$5,000 or 2% of aggregate debit balances arising from customer transactions, as defined. In addition, under the CFTC regulations, the Company is required to maintain a minimum net capital in an amount equal to the greater of \$1,000 or 8% of total risk margin in noncustomer accounts plus 8% of total risk margin in customer accounts, pursuant to the Commodity Exchange Act, exclusive of the market value of commodity options purchased by option customers. At December 31, 2015, the Company's net capital was \$1,090,696 which was 58.08% of aggregate debit balances, and \$867,329 in excess of its required net capital of \$223,366.

**(18) Subsequent Events**

The Company has evaluated whether any events or transactions occurred subsequent to the date of the statement of financial condition and through February 29, 2016, and determined that there were no material events or transactions that would require recognition or disclosure in the statement of financial condition.