HSBC HOLDINGS PLC
Form 6-K
May 11, 2009

**FORM 6-K**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Report of Foreign Private Issuer**

**Pursuant to Rule 13a - 16 or 15d - 16 of**

**the Securities Exchange Act of 1934**

For the month of May

**HSBC Holdings plc**

42nd Floor, 8 Canada Square, London E14 5HQ, England

(Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F).

Form 20-F X Form 40-F ......

(Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934).

Yes....... No X

(If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-..............).

**UNITED STATES SECURITIES**

**AND**
**EXCHANGE COMMISSION**
**Washington**
**,**
**D.C.**

**20549**

**FORM**
**10-Q**

**(**
**Mark**
**One)**
**X** QUARTERLY REPORT PURSUANT TO SECTION 13

OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

**For the quarterly period ended**
**March 31, 2009**

OR

TRANSITION REPORT PURSUANT TO SECTION 13

OR 15(d)

OF THE SECURITIES
AND
EXCHANGE ACT OF

1934

For the transition period

from
_____
to

_____

**Commission file number 1-7436**

**HSBC USA Inc.**
**(Exact name of registrant as specified in its charter)**

| **Maryland** (State of Incorporation) | **13-2764867** (I.R.S. Employer Identification No.) |
| --- | --- |
| **452 Fifth Avenue, New York, New York** (Address of principal executive offices) | **10018** (Zip Code) |

**(212) 525-5000**
**(Registrant's telephone number, including area code)**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes **X**
No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes

No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer **X** Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes

No **X**

At April 30, 2009, there were 711 shares of the registrant's Common Stock outstanding, all of which are owned by HSBC North America Inc.

**HSBC USA Inc.**

**Form 10-Q**
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**PART I.**
**FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**CONSOLIDATED STATEMENT OF (LOSS) INCOME (UNAUDITED)**

| Three Months Ended March 31, | 2009 | 2008 |
|---|---|---|
| | (in millions) | |
| **Interest income:** | | |
| Loans | **$1,546** | $1,488 |
| Securities | **277** | 302 |
| Trading assets | **59** | 158 |
| Short-term investments | **24** | 131 |
| Other | **11** | 83 |
| ***Total interest income*** | **1,917** | 2,162 |
| Interest expense: | | |
| Deposits | **313** | 799 |
| Short-term borrowings | **19** | 99 |
| Long-term debt | **237** | 303 |
| ***Total interest expense*** | **569** | 1,201 |
| Net interest income | **1,348** | 961 |
| Provision for credit losses | **1,174** | 498 |
| ***Net interest income after provision for credit*** | **174** | 463 |

| | | |
|---|---|---|
| ***losses*** | | |
| Other revenues (losses): | | |
| Credit card fees | **357** | 229 |
| Other fees and commissions | **229** | 162 |
| Trust income | **32** | 33 |
| Trading (loss) revenue | **(154)** | (709) |
| Net other-than-temporary impairment losses (includes $116 million of total losses less $78 million of losses on securities available for sale, recognized in other comprehensive income at March 31, 2009) | **(38)** | - |
| Other securities gains, net | **47** | 84 |
| Servicing and other fees from HSBC affiliates | **34** | 54 |
| Residential mortgage banking revenue | **65** | 38 |
| Gain on instruments designated at fair value and related derivatives | **112** | 57 |
| Other income (loss) | **66** | (33) |
| ***Total other revenues (losses)*** | **750** | (85) |
| Operating expenses: | | |
| Salaries and employee benefits | **291** | 310 |
| Support services from HSBC affiliates | **423** | 290 |
| Occupancy expense, net | **63** | 64 |
| Other expenses | **195** | 156 |
| ***Total operating expenses*** | **972** | 820 |
| (Loss) before income tax expense (benefit) | **(48)** | (442) |
| Income tax expense (benefit) | **41** | (164) |
| ***Net loss*** | **$(89)** | $(278) |

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED BALANCE SHEET (UNAUDITED)**

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| ***Assets*** | | |
| Cash and due from banks | **$** | $ 2,972 |

| | | |
|---|---|---|
| | **2,478** | |
| Interest bearing deposits with banks | **6,337** | 15,940 |
| Federal funds sold and securities purchased under agreements to resell | **15,660** | 10,813 |
| Trading assets | **28,872** | 31,292 |
| Securities available for sale | **22,981** | 24,908 |
| Securities held to maturity (fair value of $2,999 million and $2,935 million at March 31, 2009 and December 31, 2008, respectively) | **2,868** | 2,875 |
| Loans | **88,542** | 81,113 |
| Less - allowance for credit losses | **3,465** | 2,397 |
| Loans, net | **85,077** | 78,716 |
| Loans held for sale (includes $925 million and $874 million designated under fair value option at March 31, 2009 and December 31, 2008, respectively) | **4,710** | 4,431 |
| Properties and equipment, net | **558** | 559 |
| Intangible assets, net | **352** | 374 |
| Goodwill | **2,647** | 2,647 |
| Other assets | **9,229** | 10,042 |
| ***Total assets*** | **$ 181,769** | $ 185,569 |
| ***Liabilities*** | | |
| Debt: | | |
| Deposits in domestic offices: | | |
| Noninterest bearing | **$ 18,118** | $ 17,663 |
| Interest bearing (includes $2,549 million and $2,293 million designated under fair value option at March 31, 2009 and December 31, 2008, respectively) | **66,115** | 67,903 |
| Deposits in foreign offices: | | |
| Noninterest bearing | **1,170** | 922 |
| Interest bearing | **29,927** | 32,550 |
| Total deposits | **115,330** | 119,038 |
| Short-term borrowings | **9,806** | 10,495 |
| Long-term debt (includes $2,526 million and $2,627 million designated under fair value option at March 31, 2009 and December 31, 2008, respectively) | **25,197** | 22,089 |
| Total debt | **150,333** | 151,622 |
| Trading liabilities | **12,764** | 16,323 |
| Interest, taxes and other liabilities | **4,885** | 4,907 |
| ***Total liabilities*** | **167,982** | 172,852 |
| ***Shareholders' equity*** | | |
| Preferred stock | **1,565** | 1,565 |
| Common shareholder's equity: | | |
| Common stock ($5 par; 150,000,000 shares authorized; 711 and 709 shares issued and outstanding at March 31, 2009 and December 31, 2008, respectively) | **-** | - |
| Additional paid-in capital | **12,761** | 11,694 |
| Retained earnings | **152** | 245 |

| | | |
|---|---|---|
| Accumulated other comprehensive loss | **(691)** | (787) |
| Total common shareholder's equity | **12,222** | 11,152 |
| ***Total shareholders' equity*** | **13,787** | 12,717 |
| ***Total liabilities and shareholders' equity*** | **$ 181,769** | $ 185,569 |

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)**

| Three Months Ended March 31, | 2009 | 2008 |
|---|---|---|
| | (in millions) | |
| ***Preferred stock*** | | |
| Balance at beginning and end of period | **$ 1,565** | $ 1,565 |
| ***Common stock*** | | |
| Balance at | **-** | - |

| | | |
|---|---|---|
| beginning and end of period | | |
| ***Additional paid-in capital*** | | |
| Balance at beginning of period | **11,694** | 8,123 |
| Capital contributions from parent | **1,067** | 1,010 |
| Employee benefit plans and other | **-** | - |
| Balance at end of period | **12,761** | 9,133 |
| ***Retained*** | | |

| | | |
|---|---|---|
| ***earnings*** | | |
| Balance at beginning of period | **245** | 1,901 |
| Adjustment to initially apply fair value measurement and fair value option accounting, under SFAS 157 and 159, net of tax | **-** | 113 |
| Adjustment to | **<u>15</u>** | <u>-</u> |

| | | |
|---|---|---|
| initially apply FSP SFAS 115-2 and 124-2, net of tax | | |
| Balance at beginning of period, as adjusted | **260** | 2,014 |
| Net (loss) | **(89)** | (278) |
| Cash dividends declared on preferred stock | **(19 )** | (23 ) |
| Balance at end | **152** | 1,713 |

| | | |
|---|---|---|
| of period | | |
| ***Accumulated other comprehensive (loss)*** | | |
| Balance at beginning of period | **(787)** | (352) |
| Adjustment to initially apply FSP SFAS 115-2 and 124-2, net of tax | **(15)** | - |
| Balance at beginning of | **(802)** | (352) |

| | | |
|---|---|---|
| period, as adjusted | | |
| Net change in unrealized gains (losses), net of tax on: | | |
| Securities available for sale not other-than-temporarily impaired | **79** | (21) |
| Other-than-temporarily impaired securities available for sale (includes $116 million of total losses less $38 million of losses recognized in other revenues (losses)) | **(50)** | - |
| Derivatives classified as cash flow hedges | **76** | (39) |
| Unrecognized | **6** | 8 |

| | | |
|---|---|---|
| actuarial gains, transition obligation and prior service costs relating to pension and postretirement benefits, net of tax | | |
| Foreign currency translation adjustments, net of tax | **-** | 2 |
| Other comprehensive | **111** | (50) |

| | | |
|---|---|---|
| income (loss), net of tax | | |
| Balance at end of period | **(691)** | (402) |
| ***Total shareholders' equity*** | **$ 13,787** | $ 12,009 |
| ***Comprehensive income (loss)*** | | |
| Net loss | **$ (89)** | $ (278) |
| Other comprehensive income (loss), net of tax | **111** | (50) |
| ***Comprehensive income (loss)*** | **$ 22** | $ (328) |

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)**

| Three Months Ended March 31 | 2009 | 2008 |
|---|---|---|
| | (in millions) | |
| ***Cash flows from operating activities*** | | |
| Net loss | **$(89)** | $(278) |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation, amortization and deferred | **227** | (92) |

| | | |
|---|---|---|
| taxes | | |
| Provision for credit losses | **1,174** | 498 |
| Other-than-temporarily impaired available for sale securities | **38** | - |
| Net change in other assets and liabilities | **892** | (2,033) |
| Net change in loans held for sale | **(233)** | 522 |
| Loans attributable to | | |

| | | |
|---|---|---|
| tax refund anticipation loans program: | | |
| Originations of loans | **(9,000)** | (12,552) |
| Sales of loans to HSBC Finance, including premium | **8,989** | 12,530 |
| Net change in trading assets and liabilities | **(1,508)** | - |
| Mark-to-market on financial instruments | **(121)** | 2,405 |

| | | |
|---|---|---|
| designated at fair value and related derivatives | | |
| Net change in fair value of derivatives and hedged items | **(763)** | 6 |
| Net cash (used in) provided by operating activities | **(394)** | 1,006 |

***Cash flows***

| | | |
|---|---|---|
| ***from investing activities*** | | |
| Net change in interest bearing deposits with banks | **9,603** | 297 |
| Net change in federal funds sold and securities purchased under agreements to resell | **(4,847)** | (71) |
| Securities available for | | |

| | | |
|---|---|---|
| sale: | | |
| Purchases of securities available for sale | **(4,444)** | (5,492) |
| Proceeds from sales of securities available for sale | **3,064** | 11 |
| Proceeds from maturities of securities available for sale | **3,454** | 2,200 |
| Securities held to maturity: | | |
| Purchases | **(59)** | (125) |

| | | |
|---|---|---|
| of securities held to maturity | | |
| Proceeds from maturities of securities held to maturity | **66** | 153 |
| Change in loans: | | |
| Originations, net of collections | **9,902** | 7,408 |
| Loans purchased from HSBC Finance | **(4,599)** | (5,161) |
| Bulk purchase of | **(8,821)** | - |

| | | |
|---|---|---|
| loans from HSBC Finance | | |
| Loans sold to third parties | **1,824** | - |
| Net cash used for acquisitions of properties and equipment | **(17)** | (24) |
| Other, net | **345** | 75 |
| Net cash (used in) investing activities | **5,471** | (729) |

***Cash flows***

| ***from financing activities*** | | |
|---|---|---|
| Net change in deposits | **(3,747)** | 3,972 |
| Net change in short-term borrowings | **(689)** | (1,555) |
| Change in long-term debt: | | |
| Issuance of long-term debt | **303** | 365 |
| Repayment of long-term debt | **(2,486)** | (4,086) |
| Capital contribution from parent | **1,067** | 1,010 |
| Dividends | **(19 )** | (23 ) |

| | | |
|---|---|---|
| paid | | |
| Net cash provided by (used in) financing activities | **(5,571)** | (317) |
| Net change in cash and due from banks | **(494)** | (40) |
| Cash and due from banks at beginning of period | **2,972** | 3,567 |
| ***Cash and*** | **$2,478** | $3,527 |

| | | |
|---|---|---|
| ***due from banks at end of period*** | | |
| ***Supplemental disclosure of non-cash flow investing activities*** | | |
| Trading securities pending settlement | **$(368 )** | $1,634 |
| Assumption of indebtedness from HSBC Finance related to the | **$6,077** | $- |

bulk

loan

purchase

The accompanying notes are an integral part of the consolidated financial statements.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

***1. Organization and Basis of Presentation***

HSBC USA Inc. is an indirect wholly owned subsidiary of HSBC North America Holdings Inc. ("HSBC North America"), which is an indirect wholly owned subsidiary of HSBC Holdings plc ("HSBC"). The accompanying unaudited interim consolidated financial statements of HSBC USA Inc. and its subsidiaries (collectively "HUSI"), including its principal subsidiary HSBC Bank USA, National Association ("HSBC Bank USA"), have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X, as well as in accordance with predominate practices within the banking industry. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of financial position, results of operations and cash flows for the interim periods have been made. HSBC USA Inc. may also be referred to in this Form 10-Q as "we," "us" or "our." These unaudited interim consolidated financial statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2008 (the "2008 Form 10-K"). Certain reclassifications have been made to prior period amounts to conform to the current period presentation.

The preparation of financial statements in conformity with U.S. GAAP requires the use of estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates. Interim results should not be considered indicative of results in future periods.

During the first quarter of 2009, we adopted Statement of Financial Accounting Standards No. 161, "Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133" and FASB Staff Position (FSP) SFAS 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments." In addition, we early adopted FSP SFAS 115-2 and 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments" as well as FSP SFAS 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That are Not Orderly" effective January 1, 2009. See Note 20, "New Accounting Pronouncements" for further details and related impact.

***2. Restructuring Activities***

We continue to review our expense base in an effort to create a more streamlined organization, reduce expense growth and provide for future business initiatives. This review includes improving workforce management, consolidating certain functions where appropriate and increasing the use of global resourcing initiatives. The following summarizes the changes in the severance accrual relating to these activities during the three months ended March 31, 2009 and 2008:

| | 2009 | 2008 |
|---|---|---|
| | (in millions) | |
| Balance at January 1, | **$19** | $12 |
| Costs recorded during the period | **1** | 3 |
| Costs paid during the period | **(6)** | (7) |
| Balance at March 31, | **$14** | $8 |

Also in November 2008, we announced that we would exit the wholesale/correspondent channel of our Residential Mortgage business and focus our attention on our retail sales channel. In connection with this decision, we recorded expense of $3 million relating to one-time termination benefits of which approximately $2 million were paid during the first quarter of 2009. No additional charges relating to this decision are anticipated in future periods.

***3. Trading Assets and Liabilities***

Trading assets and liabilities are summarized in the following table.

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Trading assets: | | |
| U.S. Treasury | **$271** | $27 |
| U.S. Government agency | **246** | 271 |
| U.S. Government sponsored enterprises(1) | **197** | 521 |
| Asset backed securities | **1,555** | 1,698 |
| Corporate | **2,034** | 1,614 |
| and | | |

| | | |
|---|---|---|
| foreign bonds | | |
| Other securities | **766** | 982 |
| Precious metals | **5,552** | 4,905 |
| Fair value of derivatives | **18,251** | 21,274 |
| | **$28,872** | $31,292 |
| Trading liabilities: | | |
| Securities sold, not yet purchased | **$361** | $406 |
| Payables for precious metals | **2,137** | 1,599 |
| Fair value of derivatives | **10,266** | 14,318 |
| | **$12,764** | $16,323 |

(1) Includes mortgage backed securities of $133 million and $328 million issued or guaranteed by the Federal National Mortgage Association (FNMA) and $64 million and $193 million issued or guaranteed by the Federal Home Loan Mortgage Corporation (FHLMC) at March 31, 2009 and December 31, 2008, respectively.

At March 31, 2009 and December 31, 2008, the fair value of derivatives included in trading assets have been reduced by $5.5 billion and $6.1 billion, respectively, relating to amounts recognized for the obligation to return cash collateral received under master netting agreements with derivative counterparties, consistent with the reporting requirements of FASB Staff Position No. FIN 39-1, Amendment of FASB Interpretation No. 39 ("FSP FIN 39-1").

At March 31, 2009 and December 31, 2008, the fair value of derivatives included in trading liabilities have been reduced by $13.0 billion and $11.8 billion, respectively, relating to amounts recognized for the right to reclaim cash collateral paid under master netting agreements with derivative counterparties, consistent with the reporting requirements of FSP FIN 39-1.

***4. Securities***

The amortized cost and fair value of the securities available for sale and securities held to maturity portfolios are summarized in the following tables.

| **March 31, 2009** | **Amortized Cost** | **Non-Credit Loss Component of OTTI Securities Recorded in AOCI** | **Unrealized Gains Recorded in AOCI** | **Unrealized Losses Recorded in AOCI** | **Fair Value** |
|---|---|---|---|---|---|
| | | | **(in millions)** | | |
| Securities available for sale: | | | | | |
| U.S. Treasury | **$2,251** | **$-** | **$107** | **$(6)** | **$2,352** |
| U.S. Government sponsored enterprises:(1) | | | | | |
| Mortgage-backed securities | **7,411** | **-** | **203** | **(28)** | **7,586** |
| Direct agency obligations | **323** | **-** | **5** | **(1)** | **327** |
| U.S. Government agency issued | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| or guaranteed: | | | | | |
| Mortgage-backed securities | **2,632** | **-** | **93** | **(1)** | **2,724** |
| Collateralized mortgage obligations | **3,447** | **-** | **66** | **(1)** | **3,512** |
| Direct agency obligations | **778** | **-** | **26** | **(1)** | **803** |
| Obligations of U.S. states and political subdivisions | **724** | **-** | **5** | **(18)** | **711** |
| Asset backed securities collateralized by: | | | | | |
| Residential mortgages | **1,350** | **(27)** | **1** | **(341)** | **983** |
| Commercial mortgages | **985** | **-** | **1** | **(189)** | **797** |
| Home equity | **794** | **(51)** | **-** | **(423)** | **320** |
| Auto | **127** | **-** | **-** | **(26)** | **101** |
| Student | **39** | **-** | **-** | **(9)** | **30** |

| | | | | | |
|---|---|---|---|---|---|
| loans | | | | | |
| Other | **27** | **-** | **1** | **-** | **28** |
| Other domestic debt securities | **993** | **-** | **6** | **(12)** | **987** |
| Foreign debt securities | **1,044** | **-** | **9** | **(5)** | **1,048** |
| Equity securities(2) | **672** | **-** | **-** | **-** | **672** |
| Total available-for-sale securities | **$23,597** | **$(78)** | **$523** | **$(1,061)** | **$22,981** |
| Securities held to maturity: | | | | | |
| U.S. Government sponsored enterprises:(3) | | | | | |
| Mortgage-backed securities | **$1,899** | **$-** | **$124** | **$-** | **$2,023** |
| U.S. Government agency issued or guaranteed: | | | | | |
| Mortgage-backed securities | **130** | **-** | **12** | **-** | **142** |
| Collateralized mortgage | **358** | **-** | **23** | | **381** |

| | | | | | |
|---|---|---|---|---|---|
| obligations | | | | | |
| Obligations of U.S. states and political subdivisions | **209** | **-** | **9** | **(2)** | **216** |
| Asset backed securities collateralized by: | | | | | |
| Residential mortgages | **188** | **-** | **-** | **(35)** | **153** |
| Foreign debt securities | **84** | **-** | **-** | **-** | **84** |
| Total held-to-maturity securities | **$2,868** | **$-** | **$168** | **$(37 )** | **$2,999** |

| **December 31, 2008** | **Amortized Cost** | **Gross Unrealized Gains** | **Gross Unrealized Losses** | **Fair Value** |
|---|---|---|---|---|
| | | **(in millions)** | | |
| Securities available for sale: | | | | |

| | | | | |
|---|---|---|---|---|
| U.S. Treasury | $3,544 | $154 | $(12) | $3,686 |
| U.S. Government sponsored enterprises(1) | 11,271 | 187 | (96) | 11,362 |
| U.S. Government agency issued or guaranteed | 5,746 | 135 | (6) | 5,875 |
| Obligations of U.S. states and political subdivisions | 699 | 2 | (31) | 670 |
| Asset-backed securities | 3,462 | - | (987) | 2,475 |
| Other domestic debt securities | 144 | 7 | (7) | 144 |
| Foreign debt securities | 641 | 13 | (9) | 645 |
| Equity | 52 | - | (1) | 51 |

| | | | | |
|---|---|---|---|---|
| securities(2) | | | | |
| Total | $25,559 | $498 | $(1,149) | $24,908 |
| Securities held to maturity: | | | | |
| U.S. Government sponsored enterprises(3) | $1,892 | $73 | $(7) | $1,958 |
| U.S. Government agency issued or guaranteed | 495 | 23 | (2) | 516 |
| Obligations of U.S. states and political subdivisions | 217 | 8 | (5) | 220 |
| Asset-backed securities | 185 | 1 | (31) | 155 |
| Foreign debt securities | 86 | - | - | 86 |
| Total | $2,875 | $105 | $(45) | $2,935 |

(1) Includes securities of $3.5 billion and $5.1 billion issued or guaranteed by the Federal National Mortgage Association (FNMA) at March 31, 2009 and December 31, 2008, respectively, and $3.9 billion and $5.9 billion issued or guaranteed by Federal Home Loan Mortgage Corporation (FHLMC) at March 31, 2009 and December 31, 2008, respectively.

(2) Includes securities issued by FNMA of $2 million at March 31, 2009 and December 31, 2008. Balances at March 31, 2009 and December 31, 2008 reflect other-than-temporary impairment charges of $203 million.

(3) Includes securities of $.7 billion issued or guaranteed by FNMA at March 31, 2009 and December 31, 2008, and $1.2 billion issued and guaranteed by FHLMC at March 31, 2009 and December 31, 2008.
A summary of gross unrealized losses and related fair values as of March 31, 2009 and December 31, 2008, classified as to the length of time the losses have existed follows:

| | **One Year or Less** | | | **Greater Than One Year** | | |
|---|---|---|---|---|---|---|
| **March 31, 2009** | **Number of Securities** | **Gross Unrealized Losses** | **Aggregate Fair Value of Investment** | **Number of Securities** | **Gross Unrealized Losses** | **Aggregate Fair Value of Investment** |
| | | | **(dollars are in millions)** | | | |
| Securities available for sale: | | | | | | |
| U.S. Treasury | **3** | **$(6)** | **$1,102** | **-** | **$-** | **$-** |
| U.S. Government sponsored enterprises | **61** | **(3)** | **323** | **74** | **(26)** | **955** |
| U.S. Government agency issued or guaranteed | **31** | **(2)** | **254** | **41** | **(1)** | **91** |

| | | | | | | |
|---|---|---|---|---|---|---|
| Obligations of U.S. states and political subdivisions | **11** | **(2)** | **59** | **64** | **(16)** | **445** |
| Asset backed securities | **15** | **(55)** | **175** | **140** | **(933)** | **1,979** |
| Other domestic debt securities | **3** | **(11)** | **66** | **2** | **(1)** | **9** |
| Foreign debt securities | **2** | **-** | **10** | **4** | **(5)** | **60** |
| Equity securities | **2** | **-** | **2** | **-** | **-** | **-** |
| Securities available for sale | **128** | **$(79 )** | **$1,991** | **325** | **$(982 )** | **$3,539** |
| Securities held to maturity: | | | | | | |
| U.S. Government | **10** | **$-** | **$23** | **-** | **$-** | **$-** |

| | | | | | | |
|---|---|---|---|---|---|---|
| sponsored enterprises | | | | | | |
| U.S. Government agency issued or guaranteed | **99** | **-** | **3** | **-** | **-** | **-** |
| Obligations of U.S. states and political subdivisions | **45** | **(1)** | **27** | **6** | **(1)** | **8** |
| Asset backed securities | **-** | **-** | **-** | **12** | **(35)** | **146** |
| Securities held to maturity | **154** | **$(1)** | **$53** | **18** | **$(36)** | **$154** |

| | **One Year or Less** | | | **Greater Than One Year** | | |
|---|---|---|---|---|---|---|
| **December 31, 2008** | **Number of Securities** | **Gross Unrealized Losses** | **Aggregate Fair Value of Investment** | **Number of Securities** | **Gross Unrealized Losses** | **Aggregate Fair Value of Investment** |
| | | | **(dollars are in millions)** | | | |
| Securities available | | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| for sale: | | | | | | |
| U.S. Treasury | 5 | $(12) | $1,251 | - | $- | $- |
| U.S. Government sponsored enterprises | 136 | (42) | 1,361 | 101 | (54) | 2,295 |
| U.S. Government agency issued or guaranteed | 97 | (1) | 576 | 41 | (5) | 237 |
| Obligations of U.S. states and political subdivisions | 36 | (7) | 226 | 53 | (24) | 333 |
| Asset backed securities | 51 | (419) | 1,099 | 110 | (568) | 1,330 |
| Other domestic debt securities | 3 | (6) | 71 | 1 | (1) | 4 |
| Foreign | 1 | - | 5 | 5 | (9) | 97 |

| | | | | | | |
|---|---|---|---|---|---|---|
| debt securities | | | | | | |
| Equity securities | 2 | (1) | - | - | - | - |
| Securities available for sale | 331 | $(488) | $4,589 | 311 | $(661) | $4,296 |
| Securities held to maturity: | | | | | | |
| U.S. Government sponsored enterprises | 18 | $(2) | $113 | 7 | $(5) | $132 |
| U.S. Government agency issued or guaranteed | 176 | (2) | 105 | - | - | - |
| Obligations of U.S. states and political | 54 | (5) | 48 | 5 | - | 3 |

| | | | | | | |
|---|---|---|---|---|---|---|
| subdivisions | | | | | | |
| Asset backed securities | 2 | (10) | 52 | 10 | (21) | 96 |
| Securities held to maturity | 250 | $(19) | $318 | 22 | $(26) | $231 |

***Assessment for Other-Than-Temporary Impairment***

On a quarterly basis, we perform an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment pursuant to FASB Staff Position No. SFAS 115-1 and SFAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" ("
FSP

SFAS
115-1 and 124-1"). A debt security is considered impaired if the fair value is less than its amortized cost basis at the reporting date. The accounting literature requires us to assess whether the unrealized loss is other-than-temporary. Prior to the adoption of FASB Staff Position No. SFAS 115-2 and SFAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments" ("FSP SFAS 115-2 and 124-2"), unrealized losses that were determined to be temporary were recorded, net of tax, in other comprehensive income for available for sale securities, whereas unrealized losses related to held to maturity securities determined to be temporary were not recognized. Regardless of whether the security was classified as available for sale or held to maturity, unrealized losses that were determined to be other-than-temporary were recorded to earnings in their entirety. An unrealized loss was considered other than temporary if (i) it was not probable that the holder will collect all amounts due according to the contractual terms of the debt security, or (ii) the fair value was below the amortized cost of the debt security for a prolonged period of time and we did not have the positive intent and ability to hold the security until recovery or maturity.

We adopted
FSP

SFAS
115-2 and 124-2 effective January 1, 2009.
FSP

SFAS
115-2 and 124-2, which amended
FSP

SFAS
115-1 and 124-1, changed the recognition criteria and presentation of unrealized losses for available for sale and held to maturity debt securities that have suffered other-than-temporary impairment. Under

FSP

SFAS
 115-2 and 124-2, an unrealized loss is generally deemed to be other-than-temporary and a credit loss is deemed to exist if the present value of the expected future cash flows is less than the amortized cost basis of the debt security. As a result of our adoption of FSP SFAS 115-2 and 124-2, the credit loss component of an other-than-temporary impairment write-down is recorded as a component of
*Net other-than-temporary impairment losses*
 in the accompanying consolidated statement of (loss) income, while the remaining portion of the impairment loss is recognized in other comprehensive income (loss), provided we do not intend to sell the underlying debt security and it is "more likely than not" that we will not have to sell the debt security prior to recovery.

For all securities held in the available for sale or held to maturity portfolio for which unrealized losses have existed for a period of time, we do not have the intention to sell, and believe we will not be required to sell the securities for contractual, regulatory or liquidity reasons as of the reporting date. Therefore, the non-credit portion of unrealized losses related to debt securities in these portfolios were recorded in other comprehensive income (loss). Debt securities issued by U.S. Treasury, U.S. Government agencies and government sponsored entities accounted for 75% of total available for sale and held to maturity securities as of March 31, 2009. Therefore, our assessment for credit loss was concentrated on private label asset backed securities for which we evaluate for credit losses on a quarterly basis. We considered the following factors in determining whether a credit loss exists and the period over which the debt security is expected to recover:

•

The length of time and the extent to which the fair value has been less than the amortized cost basis. In general, a cash flow based recovery analysis is performed when the fair value of the debt security is below its amortized cost by more than 20% on a cumulative basis;

•

The level of credit enhancement provided by the structure, which includes but is not limited to credit subordination positions, excess spread, overcollateralization, protective triggers and financial guarantees provided by monoline wraps;

•

Changes in the near term prospects of the issuer or underlying collateral of a security such as changes in default rates, loss severities given default and significant changes in prepayment assumptions;

•

The level of excessive cash flows generated from the underlying collateral supporting the principal and interest payments of the debt securities; and

•

Any adverse change to the credit conditions of the issuer, the monoline insurer or the security such as credit downgrades by the rating agencies.

•

The expected length of time and the extent of continuing financial guarantee to be provided by the monoline insurers after announcement of downgrade or restructure.

We use a standard, market-based valuation model to measure the credit loss for available for sale and held to maturity securities. The valuation model captures the composition of the underlying collateral and the cash flow structure of the security. Management develops inputs to the model based on external analyst reports and forecasts and internal credit assessments. Significant inputs to the model include delinquencies, credit spreads, collateral types and related contractual features, estimated rates of default, loss given default and prepayment assumptions. Using the inputs, the model estimates cash flows generated from the underlying collateral and distributes those cash flows to respective tranches of securities considering credit subordination and other credit enhancement features. The projected future cash flows attributable to the debt security held are discounted using the effective interest rates determined at the original acquisition date if the security bears a fixed rate of return. The discount rate is adjusted for the floating index rate for securities which bear a variable rate of return, such as LIBOR-based instruments.

The excess of amortized cost over the present value of expected future cash flows, which represents the credit loss of a debt security, was $38 million as of March 31, 2009. The excess of the present value of discounted cash flows over fair value, which represents the non-credit component of the unrealized loss, was $78 million as of March 31, 2009. Since we do not have the intention to sell the securities and have sufficient capital and liquidity to hold these securities until a recovery of the fair value occurs, only the credit loss component is reflected in earnings. The difference between the fair value estimate of the security and the present value of estimated future cash flows, which represents the non-credit component of the unrealized loss, is recorded, net of taxes, in other comprehensive income (loss).

The following table summarizes the roll-forward of credit losses on debt securities held by us for which a portion of an other-than-temporary impairment is recognized in other comprehensive income:

| | **March 31, 2009** (in millions) |
|---|---|
| Credit losses at the beginning of the period | $5 |
| Credit losses related | 38 |

to

securities

for

which

an

other-than-temporary

impairment

was

not

previously

recognized
Increase

in

credit

losses

for

which

an

other-than-temporary

impairment

was

previously

recognized -
Reductions -

of

credit

losses

recognized

prior

to

the

sale

of

securities
Reductions
 of credit losses related to other than temporarily impaired securities for which we have recognized the non-credit loss in earnings because we have changed our intent not to sell or have to sell the security prior to recovery of amortized
cost -
Reductions -

of

credit

losses

for

increases

in

cash

flows

expected

to

be

collected

that

are

recognized

| | |
|---|---|
| over the remaining life of the security | |
| Ending balance of credit losses on debt securities held for which a portion of an other-than-temporary impairment was recognized | $43 |

in

other

comprehensive

income

At March 31, 2009, we held 155 individual asset-backed securities in the available for sale portfolio, of which 37 were also wrapped by a monoline insurance company. The asset backed securities backed by a monoline wrap comprised $429 million of the total aggregate fair value of asset-backed securities of $2.2 billion at March 31, 2009. The gross unrealized losses on these securities was $432 million at March 31, 2009. During the quarter, two monoline insurers were downgraded and as a result, we did not take into consideration the financial guarantee from those monoline insurers associated with certain securities. As of March 31, 2009, some of the securities which were wrapped by the monoline insurance companies which were downgraded in the first quarter of 2009 were deemed to be other-than-temporarily impaired.

At December 31, 2008, we held 161 individual asset-backed securities in the available for sale portfolio of which 37 were also wrapped by a monoline insurance company. These asset backed securities backed by a monoline wrap comprised $629 million of the total aggregate fair value of asset-backed securities of $2.4 billion at December 31, 2008. The gross unrealized losses on these securities was $404 million at December 31, 2008. As of December 31, 2008, we deemed these securities to be temporarily impaired as our analysis of the structure and our credit analysis of the monoline insurer resulted in the conclusion that it was probable we would receive all contractual cash flows from our investment, including amounts to be paid by the investment grade monoline insurers.

Gross unrealized losses within the available-for-sale and held-to-maturity portfolios decreased overall primarily due to sales of securities, but increased for asset backed securities during the first quarter of 2009 as the impact of wider credit spreads and continued reduced liquidity in many markets was only partially offset by decreases in interest rates. We have reviewed our securities on which there is an unrealized loss in accordance with our accounting policies for other-than-temporary impairment described previously. During the first quarter of 2009, nine debt securities were determined to be other-than-temporarily impaired pursuant to
FSP

SFAS
 115-2 and 124-2. As a result, we recorded an other-than-temporary impairment charge of $116 million during the three months ended March 31, 2009 on these investments. Consistent with
FSP

SFAS
 115-2 and 124-2, the credit loss component of the applicable debt securities totaling $38 million was recorded as a component of
*Net*

*other-than-temporary impairment losses*
in the accompanying consolidated statement of (loss) income, while the remaining non-credit portion of the impairment loss was recognized in other comprehensive income (loss).

We do not consider any other securities to be other-than-temporarily impaired as we expect to recover the amortized cost basis of these securities, do not intend to sell and do not have to sell these securities prior to recovery. However,

additional other-than-temporary impairments may occur in future periods if the credit quality of the securities deteriorates.

The following table summarizes realized gains and losses on investment securities transactions attributable to available for sale and held to maturity securities.

| | Gross Realized Gains | Gross Realized (Losses) | Net Realized (Losses) Gains |
|---|---|---|---|
| | | (in millions) | |
| **Three months ended March 31, 2009:** | | | |
| Securities available for sale | **$61** | **$(52)** | **$9** |
| Securities held to maturity: | | | |
| Maturities, calls and mandatory redemptions | **-** | **-** | **-** |
| | **$61** | **$(52)** | **$9** |
| **Year ended December 31,** | | | |

| | | | |
|---|---|---|---|
| **2008:** | | | |
| Securities available for sale | $29 | $(263) | $(234) |
| Securities held to maturity: Maturities, calls and mandatory redemptions | - | - | - |
| | $29 | $(263) | $(234) |

The amortized cost and fair values of securities available for sale and securities held to maturity at March 31, 2009, by contractual maturity are summarized in the table below. Expected maturities differ from contractual maturities because borrowers have the right to prepay obligations without prepayment penalties in certain cases. Securities available for sale amounts exclude equity securities as they do not have stated maturities. The table below also reflects the distribution of maturities of debt securities held at March 31, 2009, together with the approximate taxable equivalent yield of the portfolio. The yields shown are calculated by dividing annual interest income, including the accretion of discounts and the amortization of premiums, by the amortized cost of se
curities outstanding at March 31, 2009
. Yields on tax-exempt obligations have been computed on a taxable equivalent basis using applicable statutory tax rates.

| | Within One Year | | After One But Within Five Years | | After Five But Within Ten Years | | After Ten Years | |
|---|---|---|---|---|---|---|---|---|
| **Taxable Equivalent Basis** | **Amount** | **Yield** | **Amount** | **Yield** | **Amount** | **Yield** | **Amount** | **Yield** |
| | | | | **($ in millions)** | | | | |
| Available for sale: | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| U.S. Treasury | $1,000 | -% | $118 | 2.04% | $104 | 2.00% | $1,029 | -% |
| U.S. Government sponsored enterprises | - | 7.42 | 338 | 4.41 | 828 | 4.42 | 6,568 | 4.61 |
| U.S. Government agency issued or guaranteed | - | - | 8 | 4.52 | 282 | 4.94 | 6,560 | 3.22 |
| Obligations of U.S. states and political subdivisions | - | - | - | - | 207 | 5.02 | 517 | 5.01 |
| Asset backed securities | - | - | 231 | 3.75 | 174 | 3.88 | 2,878 | 3.79 |
| Other domestic debt securities | 24 | 3.86 | 866 | 2.30 | - | - | 103 | 6.80 |
| Foreign debt securities | 15 | 4.07 | 978 | 2.87 | 10 | 5.13 | 41 | 6.78 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Total amortized cost | $1,039 | 0.15% | $2,539 | 2.93% | $1,605 | 4.38% | $17,696 | 3.73 |
| Total fair value | $1,039 | | $2,524 | | $1,649 | | $17,097 | |
| Held to maturity: | | | | | | | | |
| U.S. Government sponsored enterprises | $- | 7.44% | $21 | 6.06% | $28 | 6.17% | $1,850 | 5.87% |
| U.S. Government agency issued or guaranteed | - | 7.19 | 1 | 7.41 | 6 | 8.85 | 481 | 6.34 |
| Obligations of U.S. states and political subdivisions | 13 | 5.76 | 37 | 5.11 | 33 | 4.73 | 126 | 5.11 |
| Asset backed securities | - | - | - | - | - | - | 188 | 5.80 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Foreign debt securities | 84 | 2.64 | - | - | - | - | - | - |
| Total amortized cost | $97 | 3.08% | $59 | 5.49% | $67 | 5.71% | $2,645 | 5.91% |
| Total fair value | $97 | | $63 | | $73 | | $2,766 | |

Investments in FHLB stock, FRB stock, and MasterCard Class B shares of $164 million, $382 million and $28 million, respectively, were included in other assets at March 31, 2009. Investments in FHLB stock, FRB stock and MasterCard Class B shares of $209 million, $349 million and $29 million, respectively, were included in other assets at December 31, 2008.

***5. Loans***

Loans consisted of the following:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Commercial loans: | | |
| Construction and other real estate | **$8,811** | $8,885 |
| Other commercial | **25,471** | 28,544 |
| Total commercial | **34,282** | 37,429 |
| Consumer loans: | | |
| HELOC and home equity mortgages | **4,540** | 4,549 |
| Other residential mortgages | **15,437** | 17,948 |
| Private label cards | **15,623** | 17,074 |
| Credit cards | **14,024** | 2,137 |
| Auto finance | **3,037** | 154 |
| Other consumer | **1,599** | 1,822 |
| Total consumer | **54,260** | 43,684 |
| Total loans | **$88,542** | $81,113 |

Secured financings of $1.2 billion and $5.1 billion at March 31, 2009 are secured by $1.5 billion and $6.1 billion of private label cards and credit cards, respectively. Secured financings of $1.2 billion at December 31, 2008 were secured by $1.6 billion of private label cards.

***Purchased Loan Portfolios:***

In January 2009, we purchased the
General
Motors

MasterCard
 receivable portfolio ("GM Portfolio") and the
AFL
-CIO Union Plus MasterCard/Visa receivable portfolio ("UP Portfolio") with an aggregate outstanding principal balance of $6.3 billion and $6.1 billion, respectively from HSBC Finance. The aggregate purchase price for the GM and UP Portfolios was $12.2 billion, which included the transfer of approximately $6.1 billion of indebtedness, resulting in a cash consideration of $6.1 billion. The purchase price was determined based on independent valuation opinions. HSBC Finance retained the customer relationships and by agreement we will purchase additional loan originations generated under existing and future accounts from HSBC Finance on a daily basis at fair market value. HSBC Finance will continue to service the GM and UP Portfolios for us for a fee. The loans purchased were subject to the requirements of AICPA Statement of Position 03-3, "Accounting for Certain Loans on Debt Securities Acquired in a Transfer," ("SOP 03-3") to the extent there was evidence of deterioration of credit quality since origination and for which it was probable, at acquisition, that all contractually required payments would not be collected and that the associated line of credit had been closed. The following table summarizes the outstanding loan balances, the cash flows expected to be collected and the fair value of the loans to which SOP 03-3 has been applied:

| | **GM Portfolio** | **UP Portfolio** |
|---|---|---|
| | **(in millions)** | |
| Outstanding contractual receivable balance at acquisition | $355 | $399 |
| Cash flows expected to be collected at | 164 | 167 |

| | | |
|---|---|---|
| acquisition | | |
| Basis in acquired receivables at acquisition | 122 | 114 |

The carrying amount of the loans to which SOP 03-3 has been applied at March 31, 2009 totaled $107 million and $96 million for the GM and UP Portfolios, respectively, and is included in credit card loans in the table above. The outstanding contractual balance at March 31, 2009 for these receivables is $198 million and $222 million for the GM and UP Portfolios, respectively. At March 31, 2009, no credit loss reserves for these credit card loans have been established as there has been no adverse change in anticipated future cash flows since these loans were purchased. There were no reclassifications to accretable yield from non-accretable yield during the three months ended March 31, 2009 as there was no change in the estimated cash flows to be collected on the underlying portfolios. The following summarizes the change in accretable yield associated with the portion of the GM and UP Portfolios to which SOP 03-3 has been applied in 2009:

| | **Three Months Ended March 31, 2009 (in millions)** |
|---|---|
| Accretable yield at beginning of period | **$(95)** |
| Accretable yield amortized to interest income | **15** |

| | |
|---|---|
| during the period Reclassification from non-accretable difference | - |
| Accretable yield at end of period | $(80) |

In January 2009, we also purchased $3 billion of auto finance loans ("Acquired Auto Finance Loans") from HSBC Finance with an aggregate outstanding principal balance of $3.0 billion for a purchase price of $2.8 billion. HSBC Finance will continue to service the Acquired Auto Finance Loans for us for a fee. None of the Acquired Auto Finance Loans purchased were subject to the requirements of SOP 03-3 as all of the loans were current at the time of purchase.

***Troubled Debt Restructurings:***

Provision for credit losses on loans for which we have modified the terms of the loan as part of a troubled debt restructuring ("TDR Loans"), are determined in accordance with FASB Statement No. 114, "Accounting by Creditors for Impairment of a Loan" which requires a discounted cash flow analysis to assess impairment. Interest income on TDR Loans is recognized in the same manner as loans which are not TDRs. The following table presents information about our TDR Loans:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| TDR | | |

| | | |
|---|---|---|
| Loans: | | |
| Commercial loans: | | |
| Construction and other real estate | **$-** | $- |
| Other commercial | **-** | 5 |
| Total commercial | **-** | 5 |
| Consumer loans: | | |
| Residential mortgages | **65** | 38 |
| Private label cards | **173** | 156 |
| Credit cards | **141** | 13 |
| Auto finance | **-** | - |
| Other consumer | **-** | - |
| Total consumer | **379** | 207 |
| Total TDR Loans | **$379** | $212 |

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Allowance for credit losses for TDR Loans(1): | | |
| Commercial loans: | | |
| Construction and other real estate | **$-** | $- |
| Other commercial | **-** | - |
| Total commercial | **-** | - |
| Consumer loans: | | |
| Residential mortgages | **9** | 6 |
| Private label cards | **32** | 29 |
| Credit cards | **21** | 3 |
| Other consumer | **-** | - |

| | | |
|---|---|---|
| Total consumer | **62** | 38 |
| Total Allowance for credit losses for TDR Loans | **$62** | $38 |

| | Three Months Ended March 31, | |
|---|---|---|
| | **2009** | **2008** |
| | (in millions) | |
| Average balance of TDR Loans | **$341** | $179 |
| Interest income recognized on TDR Loans | **6** | 3 |

(1) Included in the allowance for credit losses.

***Concentrations of Credit Risk:***

Certain residential mortgage loans have high loan-to-value ("LTV") ratios (loans on primary residences with LTV ratios equal to or exceeding 90 percent at the time of origination) and no mortgage insurance, which could result in the potential inability to recover the entire investment in loans involving foreclosed or damaged properties. We also offer interest-only residential mortgage loans. These interest-only loans allow customers to pay only the accruing interest for a period of time, which results in lower payments during the initial loan period. Depending on a customer's financial situation, the subsequent increase in the required payment attributable to loan principal could affect a customer's ability to repay the loan at some future date when the interest rate resets and/or principal payments are required. Outstanding balances of high LTV and interest-only loans, including loans held for sale, are summarized in the following table.

| | **March 31, 2009** | **December 31, 2008** |
|---|---|---|
| | **(in millions)** | |
| Residential mortgage loans with high LTV and no mortgage insurance | **$1,805** | $1,889 |
| Interest-only residential mortgage loans | **3,793** | 4,247 |
| Total | **$5,598** | $6,136 |

Concentrations of first and second liens within the residential mortgage loan portfolio are summarized in the following table. Amounts in the table exclude loans held for sale.

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Closed end: | | |
| First lien | **$15,437** | $17,948 |
| Second lien | **716** | 756 |
| Revolving: | | |
| Second lien | **3,824** | 3,793 |
| Total | **$19,977** | $22,497 |

Adjustable rate residential mortgage loans include mortgage loans which allow us to adjust pricing on the loan in line with market movements. At March 31, 2009 and December 31, 2008, we had approximately $9.5 billion and $10.2 billion, respectively, in adjustable rate residential mortgage loans. For the remainder of 2009, approximately $3.2 billion of adjustable rate residential mortgage loans will experience their first interest rate reset. In 2010, approximately $1.3 billion of adjustable rate residential mortgage loans will experience their first interest rate reset. A customer's financial situation and the general interest rate environment at the time of the interest rate reset could affect the customer's ability to repay or refinance the loan after the adjustment.

***6. Allowance for Credit Losses***

An analysis of the allowance for credit losses is presented in the following table:

| Three Months Ended March 31 | 2009 | 2008 |
|---|---|---|
| | (in millions) | |
| Balance at beginning of period | **$2,397** | $1,414 |

| | | |
|---|---|---|
| Provision charged to income | **1,174** | 498 |
| Charge offs | **(614)** | (402) |
| Recoveries | **71** | 73 |
| Allowance related to bulk loan purchases from HSBC Finance | **437** | - |
| Balance at end of period | **$3,465** | $1,583 |

***7. Loans Held for Sale***

Loans held for sale consisted of the following:

| | **March 31, 2009** | **December 31, 2008** |
|---|---|---|
| | **(in millions)** | |
| Commercial loans: | | |
| Construction and other real estate | **$-** | $- |

| | | |
|---|---|---|
| Other commercial | **925** | 874 |
| Total commercial | **925** | 874 |
| Consumer loans: | | |
| Residential mortgages | **3,740** | 3,512 |
| Other consumer | **45** | 45 |
| Total consumer | **3,785** | 3,557 |
| Total loans held for sale | **$4,710** | $4,431 |

We originate commercial loans in connection with our participation in a number of leveraged acquisition finance syndicates. A substantial majority of these loans were originated with the intent of selling them to unaffiliated third parties and are classified as other commercial loans held for sale at March 31, 2009. The fair value of commercial loans held for sale under this program were $925 million and $874 million at March 31, 2009 and December 31, 2008, respectively, all of which are recorded at fair value. During the first quarter of 2009, the market value of these loans increased due to narrowing credit spreads. Refer to Note 11, "Fair Value Option" of the consolidated financial statements for additional information.

During the first quarter of 2009, we sold approximately $1.8 billion of prime adjustable and fixed rate residential mortgage loans which resulted in gains of $37 million. The gains and losses from the sale of residential mortgage loans is reflected as a component of residential mortgage banking revenue in the accompanying consolidated statement of (loss) income. We retained the servicing rights in relation to the mortgages upon sale.

Residential mortgage loans held for sale include sub-prime residential mortgage loans with a fair value of $1.0 billion and $1.2 billion at March 31, 2009 and December 31, 2008, respectively, and were acquired from unaffiliated third parties and from HSBC Finance, with the intent of securitizing or selling the loans to third parties. Also included in residential mortgage loans held for sale are first mortgage loans originated and held for sale primarily to various governmental agencies.

Other consumer loans held for sale consist of student loans.

Excluding the commercial loans discussed above, loans held for sale are recorded at the lower of cost or fair value. The book value of loans held for sale exceeded fair value at March 31, 2009, resulting in an increase to the related valuation allowance. This was primarily a result of adverse conditions in the
U.S.
residential mortgage markets. The valuation allowance related to loans held for sale is presented in the following table.

| **Three Months Ended March 31** | **2009** | **2008** |
|---|---|---|
| | **(in millions)** | |
| Balance at beginning of period | **$(869)** | $(475) |
| Increase | **(76)** | (266) |

| | | |
|---|---|---|
| in allowance for net reductions in market value | | |
| Releases of valuation allowance for loans sold | **45** | 15 |
| Balance at end of period | **$(900)** | $(726) |

Loans held for sale are subject to market risk and interest rate risk, in that their value will fluctuate as a result of changes in market conditions, as well as the interest rate and credit environment. Interest rate risk for residential mortgage loans held for sale is partially mitigated through an economic hedging program to offset changes in the fair value of the mortgage loans held for sale. Trading related revenues associated with this economic hedging program, which are included in net interest income and trading (loss) revenues in the consolidated statement of (loss) income, were gains of $28 million for the three months ended March 31, 2009, compared with losses of $25 million for the three months ended March 31, 2008.

***8. Intangible Assets***

Intangible assets consisted of the following:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Mortgage servicing rights | **$320** | $341 |
| Other | **32** | 33 |
| Intangible assets | **$352** | $374 |

***Mortgage Servicing Rights (***
***"***
***MSRs***
***"***
***)***

A servicing asset is a contract under which estimated future revenues from contractually specified cash flows, such as servicing fees and other ancillary revenues, are expected to exceed the obligation to service the financial assets. We recognize the right to service mortgage loans as a separate and distinct asset at the time they are acquired or when originated loans are sold.

MSRs are subject to credit, prepayment and interest rate risk, in that their value will fluctuate as a result of changes in these economic variables. Interest rate risk is mitigated through an economic hedging program that uses securities and derivatives to offset changes in the fair value of MSRs. Since the hedging program involves trading activity, risk is quantified and managed using a number of risk assessment techniques, which are addressed in more detail in the 2008 Form 10-K.

***Residential Mortgage Servicing Rights***

Residential MSRs are initially measured at fair value at the time that the related loans are sold and are remeasured at fair value at each reporting date (the fair value measurement method). Changes in fair value of the asset are reflected in residential mortgage banking revenue in the period in which the changes occur. Fair value is determined based upon the application of valuation models and other inputs. The valuation models incorporate assumptions market participants would use in estimating future cash flows. The reasonableness of these valuation models is periodically validated by reference to external independent broker valuations and industry surveys.

Fair value of residential MSRs is calculated using the following critical assumptions:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| Annualized constant prepayment rate | **40.60%** | 39.40% |

| | | |
|---|---|---|
| (CPR) | | |
| Constant discount rate | **11.16%** | 10.26% |
| Weighted average life | **2.8 years** | 3.1 years |

Residential MSRs activity is summarized in the following table:

| **Three Months Ended March 31** | **2009** | **2008** |
|---|---|---|
| | **(in millions)** | |
| Fair value of MSRs: | | |
| Beginning balance | **$333** | $489 |
| Additions related to loan sales | **28** | 30 |
| Changes in fair value due to: | | |
| Change | **(25)** | (21) |

| | | |
|---|---|---|
| in valuation inputs or assumptions used in the valuation models | | |
| Realization of cash flows | **(23)** | (30) |
| Ending balance | **$313** | $468 |

Information regarding residential mortgage loans serviced for others, which are not included in the consolidated balance sheet, is summarized in the following table:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|
| | (in millions) | |
| Outstanding principal balances at period end | **$47,200** | $46,215 |

| Custodial balances maintained and included in noninterest bearing deposits at period end | **$1,016** | $695 |
|---|---|---|

Servicing fees collected are included in residential mortgage banking revenue and totaled $33 million and $31 million during the three months ended March 31, 2009 and 2008, respectively.

***Commercial Mortgage Servicing Rights***

Commercial MSRs, which are accounted for using the lower of cost or fair value method, totaled $7 million and $8 million at March 31, 2009 and December 31, 2008, respectively.

***Other Intangible Assets***

Other intangible assets, which result from purchase business combinations, are comprised of favorable lease arrangements of $23 million and $24 million at March 31, 2009 and December 31, 2008, respectively, and customer lists in the amount of $9 million at March 31, 2009 and December 31, 2008.

***9. Goodwill***

Goodwill was $2,647 million at March 31, 2009 and December 31, 2008. As a result of the continued deterioration in economic and credit conditions in the
U.S.
, we performed an interim impairment test of the goodwill of our Global Banking and Markets reporting unit as of March 31, 2009. As a result of this test, the fair value of our Global Banking and Markets reporting unit continues to exceed its carrying value including goodwill. Our goodwill impairment testing performed for our Global Banking and Markets reporting unit, however, is highly sensitive to certain assumptions and estimates used. In the event of further significant deterioration in the economic and credit conditions beyond the levels already reflected in our cash flow forecasts occur, or changes in the strategy or performance of our business or product offerings occur, an additional

interim impairment test will again be required.

### *10. Derivative Financial Instruments*

In our normal course of business, we enter into derivative contracts for market making and risk management purposes. For financial reporting purposes, a derivative instrument is designated in one of following categories: (a) financial instruments held for trading, (b) hedging instruments designated in a qualifying FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities ("SFAS 133") hedge or (c) a non-qualifying economic hedge. The derivative instruments held are predominantly swaps, futures, options and forward contracts. All freestanding derivatives including bifurcated embedded derivatives are stated at fair value in accordance with SFAS 133. Where we enter into enforceable master netting arrangements with counterparties, the master netting arrangements permit us to net those derivative asset and liability positions and to offset cash collateral held and posted with the same counterparty.

#### *Derivatives Held for Risk Management Purposes*

Our risk management policy requires us to identify, analyze and manage risks arising from the activities conducted during our normal course of business. We use derivative instruments as an asset and liability management tool to manage our exposures in interest rate, foreign currency and credit risks in existing assets and liabilities, commitments and forecasted transactions. The accounting for changes in fair value of a derivative instrument will depend on whether the derivative has been designated and qualifies for SFAS 133 hedge accounting.

SFAS 133 hedge accounting requires detailed documentation that describes the relationship between the hedging instrument and the hedged item, including, but not limited to, the risk management objectives and hedging strategy, and the methods to assess the effectiveness of the hedging relationship. We designate derivative instruments to offset the fair value risk and cash flow risk arising from fixed-rate and floating-rate assets and liabilities as well as forecasted transactions. We assess the hedging relationships, both at the inception of the hedge and on an ongoing basis, using a regression approach, to determine whether the designated hedging instrument is highly effective in offsetting changes in the fair value or cash flows of the hedged item. We discontinue hedge accounting when we determine that a derivative is not expected to be effective going forward or has ceased to be highly effective as a hedge, the hedging instrument is terminated, or when the designation is removed by us.

#### *Fair Value Hedges*

In the normal course of business, we hold fixed-rate loans and securities and issue fixed-rate senior and subordinated debt obligations. The fair value of fixed-rate (USD and non-USD denominated) assets and liabilities fluctuates in response to changes in interest rates or foreign currency exchange rates. We utilize interest rate swaps, interest rate forward and futures contracts and foreign currency swaps to minimize the effect on earnings caused by interest rate and foreign currency volatility.

For SFAS 133 reporting purposes, changes in fair value of a derivative designated in a qualifying fair value hedge, along with the changes in the fair value of the hedged asset or liability that is attributable to the hedged risk, are recorded in current period earnings. We recognized net gains (losses) of approximately $4 million and $(0.3) million for the period ending March 31, 2009 and 2008, respectively, reported as other income (loss) in the consolidated statements of (loss) income, which represented the ineffective portion of all fair value hedges.

The changes in fair value of the hedged item designated in a SFAS 133 hedge are captured as an adjustment to the carrying value of the hedged item (basis adjustment). If the hedging relationship is terminated and the hedged item continues to exist, the basis adjustment is amortized over the remaining term of the original hedge. We recorded basis adjustments for unexpired fair value hedges which (decreased) increased the carrying value of our debt by $(75) million and $38 million at March 31, 2009 and 2008, respectively. We amortized $1 million of basis adjustments related to terminated and/or re-designated fair value hedge relationships for the periods ending March 31,

2009 and 2008.

The following table presents the fair value of derivative instruments that are designated and qualifying as fair value hedges and their location on the balance sheet.

| | **Derivative Assets(a)** | | | **Derivative Liabilities(a)** | | |
|---|---|---|---|---|---|---|
| | | **Fair Value as of** | | | **Fair Value as of** | |
| | **Balance Sheet Location** | **March 31, 2009** | **December 31, 2008** | **Balance Sheet Location** | **March 31, 2009** | **December 31, 2008** |
| | | **(in millions)** | | | **(in millions)** | |
| **Derivatives in Statement 133 Fair Value Hedging Relationships** | | | | | | |
| Interest rate contracts | Other assets | **$294** | $372 | Interest, taxes & other liabilities | **$127** | $207 |
| Total | | **$294** | $372 | | **$127** | $207 |

(a) The derivative assets and derivative liabilities presented above may be eligible for netting under FIN 39 and consequently may be shown net against a different line item on the consolidated balance sheet. The balance sheet categories in the above table represent the location of the assets and liabilities absent the netting of the balances.

The following table presents the gains and losses on derivative instruments designated and qualifying as hedging instruments in fair value hedges and their locations on the consolidated statement of (loss) income.

| For the Period Ending March 31 | Location of Gain or (Loss) Recognized in Income on Derivatives | Amount of Gain or (Loss) Recognized in Income on Derivatives(a) 2009 | 2008 |
|---|---|---|---|
| | | (in millions) | |
| **Derivatives in Statement 133 Fair Value Hedging Relationships** | | | |
| Interest rate contracts | Other income (loss) | **$(12)** | $12 |
| Interest rate contracts | Interest income | **16** | 1 |
| Total | | **$4** | $13 |

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(a) The gains and losses associated with the contracts were presented in multiple line on the consolidated statement of (loss) income as shown above.

The following table presents information on gains and losses on the hedged items in fair value hedges and their location on the consolidated statement of (loss) income.

| | Gain/(Loss) on Derivative | | Gain (Loss) on Hedged Items | | Gain (Loss) on Derivative | | Gain (Loss) on Hedged Items | |
|---|---|---|---|---|---|---|---|---|
| | Interest Income | Other Income | Interest Income | Other Income | Interest Income | Other Income | Interest Income | Other Income |

| For the Period Ending March 31, | (Expense) | (Expense) | (Expense) | (Expense) | (Expense) | (Expense) | (Expense | (Expense) |
|---|---|---|---|---|---|---|---|---|
| | | 2009 | | | | 2008 | | |
| | | | | (in millions) | | | | |
| Interest rate contracts/ AFS Securities | **$(7)** | **$64** | **$18** | **$(60)** | $- | $(26) | $7 | $26 |
| Interest rate contracts/commercial loans | **-** | **(2)** | **-** | **-** | - | - | 1 | - |
| Interest rate contracts/subordinated debt | **23** | **(74)** | **(82)** | **76** | 1 | 38 | (32) | (38) |
| Total | **$16** | **$(12)** | **$(64)** | **$16** | $1 | $12 | $(24) | $(12) |

***Cash Flow Hedges***

We own or issue floating rate financial instruments and enter into forecasted transactions that give rise to variability in cash flows. We also hedge the variability in interest cash flows arising from on-line savings deposits. As a part of our risk management strategy, we use interest rate swaps, currency swaps and futures contracts to mitigate risk associated with variability in the cash flows.

Changes in fair value associated with the effective portion of a derivative instrument designated as a cash flow hedge are recognized initially in other comprehensive income (loss). When the cash flows for which the derivative is hedging materialize and are recorded in income or expense, the associated gain or loss from the hedging derivative previously recorded in other comprehensive income (loss) is released into the corresponding income or expense account. If a cash flow hedge of a forecasted transaction is de-designated because it is no longer highly effective, or if the hedge relationship is terminated, the cumulative gain or loss on the hedging derivative will continue to be reported in other comprehensive income (loss) unless the hedged forecasted transaction is no longer expected to occur, at which time the cumulative gain or loss is released into profit or loss. For the three months ending March 31, 2009 and 2008, $17 million and $19 million of losses, respectively, related to terminated and/or re-designated cash flow hedge relationships were amortized to earnings from other comprehensive income (loss). During the next twelve months, we expect to amortize $38 million of remaining losses to earnings resulting from these terminated and/or re-designated cash flow hedges.

The following table presents the fair value of derivative instruments that are designated and qualifying as cash flow hedges and their location on the balance sheet.

| | Derivative Assets(a) | | | Derivative Liabilities(a) | | |
|---|---|---|---|---|---|---|
| | | Fair Value as of | | | Fair Value as of | |
| | Balance Sheet Location | March 31, 2009 | December 31, 2008 | Balance Sheet Location | March 31, 2009 | December 31, 2008 |
| | | | (in millions) | | | |
| **Derivatives in Statement** | | | | | | |

| **133 Cash Flow Hedging Relationships** | | | | | | |
|---|---|---|---|---|---|---|
| Interest rate contracts | Other assets | **$2** | $5 | Interest, taxes & other liabilities | **$176** | $212 |
| Total | | **$2** | $5 | | **$176** | $212 |

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(a) The derivative assets and derivative liabilities presented above may be eligible for netting under FIN 39 and consequently may be shown net against a different line item on the consolidated balance sheet. Balance sheet categories in the above table represent the location of the assets and liabilities absent the netting of the balances.

The following table presents information on gains and losses on derivative instruments designated and qualifying as hedging instruments in cash flow hedges and their locations on the income statement.

| **For the Period Ending March 31** | **Gain (Loss) Recognized in OCI on Derivative (Effective Portion)** | | **Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)** | **Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)** | | **Location of Gain or (Loss) Recognized in Income the Derivative (Ineffective Po rtion and Amount Excluded from Effectiveness Testing** | **Gain (Loss) Reclassed from Accumulated OCI into Income (Ineffective Portion)** | |
|---|---|---|---|---|---|---|---|---|
| | **2009** | **2008** | | **2009** | **2008** | | **2009** | **2008** |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| | (in millions) | | | | | | |
| Interest rate contracts | **$26** | $(58) | Other income (loss) | **$17** | $19 | Other income (loss) | **$7** | $(1) |
| Foreign exchange contracts | **-** | (8) | Other income (loss) | **-** | - | Other income (loss) | **-** | - |
| Total | **$26** | $(66) | | **$17** | $19 | | **$7** | $(1) |

**Trading and Other Derivatives**

We enter into derivative instruments for short-term profit taking purposes, to repackage risks and structure trades to facilitate clients' needs for various risk taking and risk modification purposes. We manage our risk exposure by entering into offsetting derivatives with other financial institutions to mitigate the market risks, in part or in full, arising from our trading activities with our clients. In addition, we also enter into buy protection credit derivatives with other market participants to manage our counterparty credit risk exposure. Where we enter into derivatives for trading purposes, realized and unrealized gains and losses are recognized as Trading (Loss) Revenue. Credit losses arising from counterparty risks on over-the-counter derivative instruments and offsetting buy protection credit derivative positions are recognized as an adjustment to the fair value of the derivatives and are recorded in trading revenue (loss).

Derivative instruments designated as economic hedges that do not qualify for SFAS 133 hedge accounting are recorded in a similar manner as derivative instruments held for trading. Realized and unrealized gains and losses are recognized in other income (loss) while the derivative asset or liability positions are reflected as other assets or other liabilities. As of March 31, 2009, we have entered into credit default swaps which are designated as economic hedges against the credit risks within our loan portfolio and certain own debt issuances. In the event of an impairment loss occurring in a loan that is economically hedged, the impairment loss is recognized as provision for credit losses while the gain on the credit default swap is recorded as other income (loss). In addition, we also designated certain forward purchase or sale of to-be-announced (TBA) securities to economically hedge mortgage servicing rights. Changes in the fair value of TBA positions, which are considered derivatives, are recorded in residential mortgage banking revenue.

The following table presents the fair value of derivative instruments held for trading purposes and their location on the balance sheet.

| | Derivative Assets(a) | | | Derivative Liabilities(a) | | |
|---|---|---|---|---|---|---|
| | | Fair Value as of | | | Fair Value as of | |
| | Balance Sheet Location | March 31, 2009 | December 31, 2008 | Balance Sheet Location | March 31, 2009 | December 31, 2008 |
| | (in millions) | | | | | |
| **Other Derivatives not Designated** | | | | | | |

**as Hedging Instruments under Statement 133**

| | | | | | | |
|---|---|---|---|---|---|---|
| Interest rate contracts | Trading assets | **$50,433** | $59,861 | Trading Liabilities | **$50,507** | $60,104 |
| Foreign exchange contracts | Trading assets | **17,909** | 24,437 | Trading Liabilities | **17,547** | 23,890 |
| Equity contracts | Trading assets | **3,282** | 2,981 | Trading Liabilities | **3,209** | 2,848 |
| Precious Metals contracts | Trading assets | **2,111** | 2,667 | Trading Liabilities | **1,946** | 2,255 |
| Credit contracts | Trading assets | **58,330** | 64,341 | Trading Liabilities | **58,459** | 64,032 |
| Other | Trading assets | **84** | 55 | Trading Liabilities | **21** | 7 |
| Total | | **$132,149** | $154,342 | | **$131,689** | $153,136 |

The following table presents the fair value of derivative instruments held for other purposes and their location on the balance sheet.

| | Derivative Assets(a) | | | Derivative Liabilities(a) | | |
|---|---|---|---|---|---|---|
| | | Fair Value as of | | | Fair Value as of | |
| | Balance Sheet Location | March 31, 2009 | December 31, 2008 | Balance Sheet Location | March 31, 2009 | December 31, 2008 |
| | | | (In millions) | | | |
| **Other** | | | | | | |

| **Derivatives not Designated as Hedging Instruments under Statement 133** | | | | | | |
|---|---|---|---|---|---|---|
| Interest rate contracts | Other assets | **$633** | $794 | Interest, taxes & other liabilities | **$6** | $6 |
| Foreign exchange contracts | Other assets | **1** | 1 | Interest, taxes & other liabilities | **33** | 42 |
| Equity contracts | Other assets | | 2 | Interest, taxes & other liabilities | **229** | 244 |
| Credit contracts | Other assets | **176** | 210 | Interest, taxes & other liabilities | **10** | 70 |
| Total | | **$810** | $1,007 | | **$278** | $362 |

(a) The derivative assets and derivative liabilities presented above may be eligible for netting under FIN 39 and consequently may be shown net against a different line item on the consolidated balance sheet. Balance sheet categories in the above table represent the location of the assets and liabilities absent the netting of the balances.

The following table presents information on gains and losses on derivative instruments held for trading purposes and their locations on the statement of (loss) income.

| For the Three Months Ended March 31, | Location of Gain (Loss) Recognized in Income on Derivatives | Amount of Gain (Loss) Recognized in Income on Derivatives 2009 | 2008 |
|---|---|---|---|
| | (in millions) | | |
| **Trading Derivatives not Designated as Hedging Instruments under Statement 133** | | | |
| Interest rate contracts | Trading (loss) revenue | **$96** | $(259) |
| Foreign exchange contracts | Trading (loss) revenue | **81** | 415 |
| Equity contracts | Trading (loss) revenue | **(10)** | 291 |
| Precious Metals contracts | Trading (loss) revenue | **20** | 93 |
| Credit contracts | Trading (loss) revenue | **(634)** | (603) |
| Other | Trading (loss) revenue | **42** | 0 |
| Total | | **$(405)** | $(63) |

The following table presents information on gains and losses on derivative instruments held for other purposes and their locations on the statement of (loss) income.

| For the Three Months Ended March 31, | Location of Gain (Loss) Recognized in Income on Derivatives | Amount of Gain (Loss) Recognized in Income on Derivatives 2009 | 2008 |
|---|---|---|---|
| | (in millions) | | |
| **Other Derivatives not Designated as** | | | |

| **Hedging Instruments under Statement 133** | | | |
|---|---|---|---|
| Interest rate contracts | Other income (loss) | **$(138)** | $127 |
| Foreign exchange contracts | Other income (loss) | **6** | 83 |
| Equity contracts | Other income (loss) | **(1)** | (106) |
| Credit contracts | Other income (loss) | **(9)** | (4) |
| Total | | **$(142)** | $100 |

***Credit-Risk-Related Contingent Features***

We enter into total return swap, interest rate swap, cross-currency swap and credit default swap contracts, amongst others which contain provisions that require us to maintain a specific credit rating from each of the major credit rating agencies. Sometimes the derivative instrument transactions are a part of broader structured products transaction. As of March 31, 2009, we were given credit ratings of AA and Aa3 by S&P and Moody's respectively. We were given a short-term debt rating at March 31, 2009 of A-1+ and P-1 by S&P and Moody's respectively. If our credit ratings were to fall below our current ratings, the counterparties to our derivative instruments could demand additional collateral to be posted with them. The amount of additional collateral required to be posted will depend on whether we are downgraded by one or more notches as well as whether the downgrade is in relation to our long-term or short-term ratings. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that are in a liability position as of March 31, 2009, is $18 billion for which we have posted collateral of $15 billion in the normal course of business.

In the event of a credit downgrade, we do not expect our long-term ratings to go below A2 and A+ and our short-term ratings to go below P-2 and A-1 by Moody's and S&P, respectively. The following tables summarize our obligation to post additional collateral (from the current collateral level) in certain hypothetical "commercially reasonable" downgrade scenarios. It is not appropriate to accumulate or extrapolate information presented in the table below to

determine our total obligation because the information presented to determine our obligation in hypothetical rating scenarios is not mutually exclusive.

**Moody's**

| | Long-Term Ratings | | |
|---|---|---|---|
| **Short-Term Ratings** | **Aa3** | **A1** | **A2** |
| | (in millions) | | |
| P-1 | $0 | 269 | 625 |
| P-2 | 692 | 926 | 1,039 |

**S&P**

| | Long-Term Ratings | | |
|---|---|---|---|
| **Short-Term Ratings** | **AA** | **AA-** | **A+** |
| | (in millions) | | |
| A-1+ | $0 | 3 | 258 |
| A-1 | 439 | 441 | 697 |

We would be required to post $488 million of additional collateral on a total return swaps if we are not rated by any two of the rating agencies at least A-1 (Moody's), A+ (Fitch), A+ (S&P), or not rated A (high) by DBRS.

***Notional Value of Derivative Contracts***

The following table summarizes the notional values of derivative contracts.

| | As of | |
|---|---|---|
| | **March 31, 2009** | **December 31, 2008** |
| | (in millions) | |
| Interest rate: | | |
| Futures and forwards | **$287,451** | $281,584 |
| Swaps | **1,426,040** | 1,593,440 |
| Options written | **92,206** | 99,858 |
| Options | **93,585** | 90,286 |

| | | |
|---|---|---|
| purchased | **1,899,282** | 2,065,168 |
| Foreign Exchange: | | |
| Swaps, futures and forwards | **505,296** | 560,167 |
| Options written | **35,642** | 31,154 |
| Options written | **35,752** | 31,394 |
| Spot | **38,323** | 36,229 |
| | **615,013** | 658,944 |
| Commodities, equities and precious metals: | | |
| Swaps, futures and forwards | **33,216** | 35,093 |
| Options written | **14,183** | 14,425 |
| Options purchased | **13,765** | 13,521 |
| | **61,164** | 63,039 |
| Credit derivatives | **914,475** | 968,260 |
| Total | **$3,489,934** | $3,755,411 |

***11. Fair Value***

HSBC complies with International Financial Reporting Standards for its financial reporting. We have elected to apply the fair value option to selected financial instruments under FASB Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities", ("SFAS No. 159") to align the measurement attributes of those instruments under U.S. GAAP and IFRSs and to simplify the accounting model applied to those financial instruments. We elected to apply the fair value option ("FVO") reporting to commercial leveraged acquisition finance loans and unfunded commitments which are classified as held for sale, certain fixed rate long-term debt issuances, and hybrid instruments which include all structured notes and structured deposits which contained embedded derivatives. Changes in fair value for these assets and liabilities which are accounted for under FVO are reported as a Gain on instruments at fair value and related derivatives in the consolidated statement of (loss) income.

***Loans***

We elected to apply FVO to all commercial leveraged acquisition finance loans and unfunded commitments. The election allows us to account for these loans and commitments at fair value which is consistent with the manner in which the instruments are managed. As of March 31, 2009, commercial leveraged acquisition finance loans and unfunded commitments of $925 million carried at fair value had an aggregate unpaid principal balance of $1,347 million. As of December 31, 2008, commercial leveraged acquisition finance loans and unfunded commitments of $874 million carried at fair value had an aggregate unpaid principal balance of $1,320 million. These loans are included in loans held for sale in the consolidated balance sheet. Interest from these loans is recorded as interest income in the consolidated statement of (loss) income. Changes in fair value of these loans resulted in a gain of $35 million and a loss of $141 million during the three months ended March 31, 2009 and 2008, respectively, which is included in gain on instruments designated at fair value and related derivatives in the consolidated statement of (loss) income. Because substantially all of the loans elected for the fair value option are floating rate assets, changes in their fair value are primarily attributable to changes in loan-specific credit risk.

As of March 31, 2009 and December 31, 2008, no loans for which the fair value option has been elected are 90 days or more past due or are on non-accrual status.

***Long-Term Debt (Own Debt Issuances)***

We elected to apply FVO for fixed rate long-term debt for which we had applied SFAS 133 fair value hedge accounting. The election allows us to achieve similar hedge accounting effect without meeting the vigorous SFAS 133 hedge accounting requirements. We measure the fair value of the debt issuances based on inputs observed in the secondary market. Changes in fair value of these instruments are attributable to changes of our own credit risk and the interest rate.

Fixed rate debt accounted for under FVO at March 31, 2009 totaled $1,466 billion and had an aggregate unpaid principal balance of $1,750 million. Fixed rate debt accounted for under FVO at December 31, 2008 totaled $1,668 billion and had an aggregate unpaid principal balance of $1,750 million.

During the three months ended March 31, 2009 and 2008, we recorded a gain of $202 million and $56 million, respectively, resulting from changes in the fair value of the fixed rate debt accounted for under FVO which is included in gain on instruments designated at fair value and related derivatives in the consolidated statement of (loss) income. Changes in our own credit risk accounted for $111 million gain in addition to a $91 million gain attributable to changes in the benchmark interest rate. Interest paid on the fixed rate debt elected for FVO is recorded as interest expense in the consolidated statement of (loss) income.

***Hybrid Instruments***

Upon adoption of SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments" ("SFAS No. 155"), we elected to measure all hybrid instruments issued after January 1, 2006 that contain embedded derivatives which should be bifurcated from the debt host at fair value. Such election has reduced the differences between IFRSs and U.S. GAAP. SFAS No. 159 has incorporated accounting requirements similar to SFAS No. 155 and because

SFAS No. 159 has a broader application than SFAS No. 155, we elected the fair value option available under SFAS No. 159 to all hybrid instruments, inclusive of structured notes and structured deposits, issued after January 1, 2006.

As of March 31, 2009, interest bearing deposits in domestic offices included $2,548 million of structured deposits accounted for under FVO which had an unpaid principal balance of $2,600 million. Long-term debt at March 31, 2009 included structured notes of $1,060 million accounted for under FVO which had an unpaid principal balance of $1,338 million. As of December 31, 2008, interest bearing deposits in domestic offices included $2,293 million of structured deposits accounted for under FVO which had an unpaid principal balance of $2,386 million. Long-term debt at December 31, 2008 included structured notes of $959 million accounted for under FVO which had an unpaid principal balance of $1,242 million. Interest incurred was recorded as interest expense in the consolidated statement of (loss) income. As a result of remeasuring structured deposits and structured notes at fair value, we recorded a gain of $16 million and $72 million during the three months ended March 31, 2009 and 2008, respectively, as a component of gain on instruments designated at fair value and related derivatives in the consolidated statement of (loss) income. Changes in our own credit risk accounted for $28 million and $37 million of the gain during the three months ended March 31, 2009 and 2008, respectively.

***Components of Gain on instruments at fair value and related derivatives***

Gain on instruments at fair value and related hedges includes the changes in fair value related to both interest and credit risk as well as the mark-to-market adjustment on derivatives related to the debt designated at fair value and net realized gains or losses on these derivatives. The components of gain on instruments at fair value and related derivatives related to the changes in fair value of fixed rate debt accounted for under FVO are as follows:

| Three Months Ended March 31, 2009 | Loans | Long -Term Debt | Hybrid Instruments | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| Interest rate component | $- | $91 | $(12) | $79 |
| Credit risk component | 35 | 111 | 28 | 174 |
| Total mark-to-market on financial instruments designated at fair | 35 | 202 | 16 | 253 |

| | | | | |
|---|---|---|---|---|
| value | | | | |
| Mark-to-market on the related derivatives | **-** | **(167)** | **77** | **(90)** |
| Net realized gain (losses) on the related derivatives | **-** | **14** | **(65)** | **(51)** |
| Gain (loss) on instruments designated at fair value and related derivatives | **$35** | **$49** | **$28** | **$112** |

| Three Months Ended March 31, 2008 | Loans | Long -Term Debt | Hybrid Instruments | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| Interest rate component | $- | $(81) | $80 | $(1) |
| Credit risk component | (141) | 137 | 37 | 33 |
| Total mark-to-market on financial instruments designated at fair value | (141) | 56 | 117 | 32 |
| Mark-to-market on the related derivatives | - | 100 | (156) | (56) |
| Net realized gain (losses) on the related | - | 5 | 76 | 81 |

| | | | | |
|---|---|---|---|---|
| derivatives | | | | |
| Gain (loss) on instruments designated at fair value and related derivatives | $(141) | $161 | $37 | $57 |

### *12. Income Taxes*

The following table presents our effective tax rates.

| **Three Months Ended March 31** | **2009** | | **2008** | |
|---|---|---|---|---|
| Statutory federal income tax rate | **(35.0)%** | **$(17)** | (35.0)% | $(155) |
| Increase (decrease) in rate resulting from: | | | | |
| State and local taxes, | **11.5** | **5** | 1.4 | 6 |

| | | | | |
|---|---|---|---|---|
| net of federal benefit | | | | |
| Sale of minority stock interest | **154.6** | **74** | - | - |
| Tax exempt income | **(8.0)** | **(4)** | (.9) | (4) |
| Validation of deferred tax balances | - | - | (.7) | (3) |
| Low income housing and other tax credits | **(32.2)** | **(15)** | (3.0) | (13) |
| Effects of foreign operations | **12.3** | **6** | 2.2 | 10 |

| | | | | |
|---|---|---|---|---|
| Uncertain tax provision | **(4.7)** | **(2)** | (.9) | (4) |
| IRS Audit Effective Settlement | **(17.1)** | **(8)** | - | - |
| State rate change effect on net deferred tax assets | **4.7** | **2** | - | - |
| Other | **(.7)** | **-** | (.2) | (1) |
| Effective tax rate | **85.4%** | **$41** | (37.1)% | $(164) |

In March, as part of a corporate restructuring within HSBC's Private Banking business, our 5.24% indirect interest in HSBC Private Bank (Suisse) S.A. to HSBC Private Bank Holdings (Suisse) S.A., the majority shareholder, for cash proceeds of $350 million. A gain of $33 million was reported on the books. For US tax purposes, the transaction is treated as a dividend in the amount of the sale proceeds to the extent of PBRS' earnings and profits.

The Internal Revenue Service's audit of our 2004 and 2005 federal income tax returns was effectively settled during the quarter, resulting in an $8 million decrease in tax expense. We are currently under audit by various state and local

tax jurisdictions, and although one or more of these audits may be concluded within the next 12 months, it is not possible to reasonably estimate the impact on our uncertain tax positions at this time. The Internal Revenue Service will begin its audit of our 2006 and 2007 returns in the second quarter.

We recognize 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 tax credits and net operating losses. Our net deferred tax assets, net of both deferred tax liabilities and valuation allowances, totaled $1.5 billion and $1.4 billion as of March 31, 2009 and December 31, 2008, respectively. We evaluate our deferred tax assets for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including our historical financial performance, projections of future taxable income, future reversals of existing taxable temporary differences, tax planning strategies and any carryback availability. In evaluating the need for a valuation allowance, we estimate future taxable income based on management approved business plans, future capital requirements and ongoing tax planning strategies, including capital support from HSBC necessary as part of such plans and strategies. This process involves significant management judgment about assumptions that are subject to change from period to period.

Based on our forecasts of future taxable income, which include assumptions about the depth and severity of further home price depreciation and the U.S. recession, including unemployment levels and their related impact on credit losses, we currently anticipate that our results of future operations will generate sufficient taxable income to allow us to realize substantially all of our deferred tax assets. Since the recent market conditions have created significant downward pressure and volatility on our near-term pre-tax book income, our analysis of the realizability of the deferred tax assets significantly discounts any future taxable income expected and relies to a greater extent on continued capital support from our parent, HSBC, including tax planning strategies implemented in relation to such support. HSBC has indicated they are fully committed and have the capacity to provide such support. In considering only the expected benefits of tax planning strategies, it is more likely than not that the deferred tax asset would be fully realized before the end of the applicable carryforward period. Absent the capital support from HSBC and implementation of the related tax planning strategies, we would be required to record a valuation allowance against our deferred tax assets.

We are included in HSBC North America's consolidated Federal income tax return and in various state income tax returns. We have entered into tax allocation agreements with HSBC North America and its subsidiary entities included in the consolidated return which govern the timing and the current amount of taxes to be paid or received by the various entities. The evaluation of the recoverability of the deferred tax assets is performed at the HSBC North America legal entity level and considers our activities and performance together with the tax planning strategies identified in reaching a conclusion on recoverability.

If future events differ from our current forecasts, a valuation allowance may need to be established which could have a material adverse effect on our results of operations, financial condition and capital position. We will continue to update our assumptions and forecasts of future taxable income and assess the need for a valuation allowance, including the consideration of the prudence and feasibility of the various tax planning strategies, some of which rely on the level of capital support from HSBC.

***13. Pensions and other Post Retirement Benefits***

The components of pension expense for the domestic defined benefit pension plan reflected in our consolidated statement of income (loss) are shown in the table below and reflect the portion of the pension expense of the combined HSBC North America pension plan which has been allocated to HSBC USA Inc.:

| Three Months Ended March 31, | 2009 | 2008 |
|---|---|---|

| | **(in millions)** | |
|---|---|---|
| Service cost - benefits earned during the period | **$7** | $8 |
| Interest cost on projected benefit obligation | **18** | 19 |
| Expected return on assets | **(13)** | (22) |
| Recognized losses | **9** | - |
| Pension expense | **$21** | $5 |

Pension expense increased during the first quarter of 2009 due to the amortization of a portion of the actuarial losses incurred by the plan as a result of the volatile capital markets that occurred in 2008.

Components of the net periodic benefit cost for our postretirement benefits other than pensions are as follows:

| **Three Months Ended March 31,** | **2009** | **2008** |
|---|---|---|
| | **(in millions)** | |

| | | |
|---|---|---|
| Service cost - benefits earned during the period | **$-** | $- |
| Interest cost | **1** | 1 |
| Recognized losses | **1** | - |
| Transition amount amortization | **(1)** | 1 |
| Net periodic postretirement benefit cost | **$1** | $2 |

***14. Related Party Transactions***

In the normal course of business, we conduct transactions with HSBC and its subsidiaries. These transactions occur at prevailing market rates and terms. All extensions of credit by HSBC Bank USA to other HSBC affiliates (other than FDIC-insured banks) are legally required to be secured by eligible collateral. The following table presents related party balances and the income and expense generated by related party transactions:

| | **March 31, 2009** | **December 31, 2008** |
|---|---|---|
| | **(in millions)** | |
| Assets: | | |
| Cash | **$209** | $157 |

| | | |
|---|---|---|
| and due from banks | | |
| Interest bearing deposits with banks | **233** | 138 |
| Federal funds sold and securities purchased under resale agreements | **989** | 346 |
| Trading assets(1) | **24,720** | 32,445 |
| Loans | **2,044** | 2,586 |
| Other | **1,210** | 733 |
| Total assets | **$29,405** | $36,405 |
| Liabilities: | | |
| Deposits | **$9,427** | $10,285 |
| Trading liabilities(1) | **29,256** | 36,589 |
| Short-term borrowings | **1,986** | 1,831 |
| Other | **185** | 162 |
| Total | **$40,854** | $48,867 |

liabilities

____________

(1) Trading assets and liabilities exclude the impact of netting in accordance with FASB Interpretation No. 39 and FSP FIN 39-1.

| **Three Months Ended March 31** | **2009** | **2008** |
|---|---|---|
| | **(in millions)** | |
| Interest income | **$47** | $56 |
| Interest expense | **7** | 31 |
| Net interest income (loss) | **$40** | $25 |
| HSBC affiliate income: | | |
| Fees and commissions: | | |
| HSBC | **(3)** | 26 |
| HSBC Finance | **6** | 6 |
| HSBC Markets (USA) Inc. ("HMUS") | **2** | 3 |
| Other HSBC affiliates | **13** | 2 |
| Gains on sales of refund anticipation loans | **10** | 12 |

| | | |
|---|---|---|
| to HSBC Finance | | |
| Other HSBC affiliates income | **6** | 5 |
| Total affiliate income | **$34** | $54 |
| Support services from HSBC affiliates: | | |
| HSBC Finance | **189** | 121 |
| HMUS | **71** | 54 |
| HSBC Technology & Services ( USA ) Inc. ("HTSU") | **111** | 63 |
| Other HSBC affiliates | **52** | 52 |
| Total support | **$423** | $ 290 |

services

from

HSBC

affiliates

***Transactions Conducted with HSBC Finance Corporation***

•

In January 2009, we purchased the GM and UP Portfolios from HSBC Finance with an outstanding principal balance of $6.3 billion and $6.1 billion, respectively, at the time of sale, at a total net premium of $113 million. Premiums paid are amortized to interest income over the estimated life of the receivables purchased. HSBC Finance retained the customer account relationships associated with these credit card portfolios. On a daily basis we purchase all new credit card loan originations for the GM and UP Portfolios from HSBC Finance. During the three months ended March 31, 2009, we purchased $4.2 billion of GM and UP loan originations at fair market value as determined by an independent third party. HSBC Finance continues to service these credit card loans for a fee. Fees paid relating to the servicing of these loans totaled $55 million for the three months ended March 31, 2009. At March 31, 2009, HSBC Finance was servicing GM and UP loans for us with an outstanding principal balance of $5.9 billion and $6.0 billion, respectively.

•

In January 2009, we also purchased certain auto finance loans with an outstanding principal balance of $3.0 billion from HSBC Finance at the time of sale, with a total net discount of $226 million. Discounts are amortized to interest income over the estimated life of the receivables purchased. HSBC Finance continues to service the auto finance loans for us for a fee. Fees paid relating to the servicing of these loans totaled $14 million for the three months ended March 31, 2009. At March 31, 2009, HSBC Finance was servicing auto finance loans for us of $2.6 billion.

•

We purchased $1 billion and $1.1 billion of other credit card receivables originated by HSBC Finance during the three months ended March 31, 2009 and 2008, respectively, at fair market value, as determined by an independent third party. Premiums paid are amortized to interest income over the estimated life of the receivables purchased. HSBC Finance continues to service the customer receivables and charges us a servicing fee. Fees paid relating to the servicing of these credit card receivables during the three months ended March 31, 2009 and 2008 totaled $16 million and $11 million, respectively. At March 31, 2009 and December 31, 2008, HSBC Finance was servicing $1.9 billion and $2.0 billion, respectively, of credit card receivables.

•

We purchased $3.6 billion and $4.5 billion of private label credit card receivables originated by HSBC Finance during the three months ended March 31, 2009 and 2008, respectively, at fair market value, as determined by an independent third party. Premiums paid are amortized to interest income over the estimated life of the receivables purchased. HSBC Finance continues to service the customer receivables and charge us a servicing fee. Fees paid relating to the servicing of private label credit card receivables during the three months ended March 31, 2009 and 2008 totaled

$93 million and $96 million, respectively. At March 31, 2009 and December 31, 2008, HSBC Finance was servicing $15.5 billion and $17.1 billion, respectively, of private label credit card receivables.

•

Support services from HSBC affiliates include charges by HSBC Finance under various service level agreements for loan origination and servicing, including the servicing of the portfolios previously discussed, as well as other operational and administrative support. Fees paid for these services totaled $189 million and $121 million for the three months ended March 31, 2009 and 2008, respectively.

•

In the second quarter of 2008, HSBC Finance launched a new program with HSBC Bank
USA
 to sell loans originated in accordance with the Federal Home Loan Mortgage Corporation's ("
Freddie

Mac
") underwriting criteria to HSBC Bank
USA
 who then sells them to
Freddie

Mac
 under its existing
Freddie

Mac
 program. During the three months ended March 31, 2009, $51 million of real estate secured loans were purchased by
HSBC Bank
USA
 under this program, with a total premium of $1 million. This program was discontinued in February 2009 as a result of the decision to discontinue new receivable originations in HSBC Finance's Consumer Lending business.

•

At March 31, 2009 and December 31, 2008, HSBC Finance was servicing $785 million and $877 million, respectively, of private label commercial and closed end loans. HSBC Finance continues to service the customer receivables and charge us a servicing fee. Fees paid relating to the servicing of private label commercial and closed end loans receivables for the three months ended March 31, 2009 and 2008 totaled $3 million and $4 million, respectively.

•

Our wholly-owned subsidiaries, HSBC Bank
USA
 and HSBC Trust Company (
Delaware
),
N.A.

("HTCD"), are the originating lenders for a federal income tax refund anticipation loan program for clients of third party tax preparers, which are managed by HSBC Finance. By agreement, HSBC Bank
USA
and HTCD process applications, fund and subsequently sell these loans to HSBC Finance. HSBC Bank USA and HTCD originated approximately $9 billion and $13 billion during the three months ended
March 31 2009
and 2008, respectively, that were sold to HSBC Finance. This resulted in gains of $10 million and $12 million during the three months ended
March 31 2009
and 2008, respectively.

•

Certain of our consolidated subsidiaries have revolving lines of credit totaling $1.0 billion with HSBC Finance. There were no balances outstanding under any of these lines of credit at March 31, 2009 or December 31, 2008.

•

We extended a secured $1.5 billion uncommitted credit facility to HSBC Finance in December 2008. This is a 364 day credit facility and there were no balances outstanding at March 31, 2009 or December 31, 2008.

•

We extended a $1.0 billion committed credit facility to HSBC Bank
Nevada
, a subsidiary of HSBC Finance, in December 2008. This is a 364 day credit facility and there were no balances outstanding at March 31, 2009 or December 31, 2008.

•

We service a portfolio of residential mortgage loans owned by HSBC Finance with an outstanding principal balance of $1.8 billion and $2.0 billion at March 31, 2009 and
December 31 2008
, respectively. The related servicing fee income was $2 million and 3 million during the three months ended
March 31 2009
and 2008, respectively.

•

HSBC Finance services a portfolio of residential mortgage loans for us with an outstanding principal balance of $2.0 billion and $2.1 billion at March 31, 2009 and December 31, 2008, respectively. Fees paid relating to the servicing of this portfolio totaled $1 million and $2 million for the three months ended March 31, 2009 and 2008, respectively.

***Transactions Conducted with HMUS***

We utilize HSBC Securities (USA) Inc. ("
HSI
") for broker dealer, debt and preferred stock underwriting, customer referrals, loan syndication and other treasury and traded markets related services, pursuant to service level agreements. Fees charged by
HSI

for broker dealer, loan syndication services, treasury and traded markets related services are included in support services from HSBC affiliates. Debt underwriting fees charged by
HSI
are deferred as a reduction of long-term debt and amortized to interest expense over the life of the related debt. Preferred stock issuance costs charged by
HSI
are recorded as a reduction of capital surplus. Customer referral fees paid to
HSI
are netted against customer fee income, which is included in other fees and commissions.

We have extended loans and lines, some of them uncommitted, to HMUS and its subsidiaries in the amount of $2.9 billion, of which $1.3 billion and $1.5 billion was outstanding at March 31, 2009 and December 31, 2008, respectively. Interest income on these loans and lines for the three months ended March 31, 2009 and 2008 totaled $11 million and $8 million, respectively.

***Other Transactions with HSBC Affiliates***

In March 2009, we sold an equity investment in HSBC Private Bank (Suisse) SA ("PBRS") to another HSBC affiliate for cash, resulting in a gain of $33 million in the first quarter of 2009.

We have an unused line of credit with HSBC Bank plc of $2.5 billion at March 31, 2009 and December 31, 2008.

We have extended loans and lines of credit to various other HSBC affiliates totaling $1.7 billion, of which $615 million and $715 million was outstanding at March 31, 2009 and December 31, 2008, respectively. Interest income on these lines for the three months ended March 31, 2009 and 2008 totaled $3 million and $1 million, respectively.

Historically, we have provided support to several HSBC affiliate sponsored asset backed commercial paper (ABCP) conduits by purchasing A-1/P-1 rated commercial paper issued by them. We have continued to provide support to these conduits by purchasing ABCP. At March 31, 2009 and December 31, 2008, no ABCP was held.

We utilize other HSBC affiliates primarily for treasury and traded markets services and, to a lesser extent, for global resourcing initiatives. Fees billed to us for these services are included in support services from HSBC affiliates and totaled $72 million and $62 million during the three months ended March 31, 2009 and 2008, respectively.

We routinely enter into derivative transactions with HSBC Finance and other HSBC affiliates as part of a global HSBC strategy to offset interest rate or other market risks associated with debt issues and derivative contracts with unaffiliated third parties. The notional value of derivative receivables related to these contracts was approximately $760 billion and $904 billion at March 31, 2009 and December 31, 2008, respectively. The net credit exposure (defined as the recorded fair value of derivative receivables) related to the contracts was approximately $25 billion and $32 billion at March 31, 2009 and December 31, 2008, respectively. Our Global Banking and Markets business accounts for these transactions on a mark to market basis, with the change in value of contracts with HSBC affiliates substantially offset by the change in value of related contracts entered into with unaffiliated third parties.

In December 2008, HSBC Bank
USA
entered into derivative transactions with another HSBC affiliate to offset the risk associated with the contingent "loss trigger" options embedded in certain leveraged super senior (
LSS
) tranched credit default swaps. These transactions are expected to significantly reduce income volatility for HSBC Bank

USA
by transferring the volatility to the affiliate.

Technology and some centralized operational services and beginning in January 2009, human resources, corporate affairs and other shared services in
North America
are centralized within HSBC Technology and Services (USA) Inc. ("HTSU.") Technology related assets and software purchased subsequent to January 1, 2004 are generally purchased and owned by HTSU. HTSU also provides certain item processing and statement processing activities which are included in Support services from HSBC affiliates in the consolidated statement of (loss) income.

Our domestic employees participate in a defined benefit pension plan sponsored by HSBC North America. Additional information regarding pensions is provided in Note 13, "Pension and Other Postretirement Benefits" of the consolidated financial statements.

Employees participate in one or more stock compensation plans sponsored by HSBC. Our share of the expense of these plans on a pre-tax basis was approximately $18 million and $17 million for the three months ended March 31, 2009 and 2008, respectively. As of March 31, 2009, our share of compensation cost related to nonvested stock compensation plans was approximately $61 million, which is expected to be recognized over a weighted-average period of 1.4 years. A description of these stock compensation plans can be found in Note 24, "Share-based Plans," of the 2008 Form 10-K.

***15. Business Segments***

We have five distinct segments that we utilize for management reporting and analysis purposes, which are generally based upon customer groupings, as well as products and services offered.

Our segment results are presented under International Financial Reporting Standards ("IFRSs") (a non-U.S. GAAP financial measure) as operating results are monitored and reviewed, trends are evaluated and decisions about allocating resources, such as employees are made almost exclusively on an IFRSs basis since we report results to our parent, HSBC in accordance with its reporting basis, IFRSs.

Net interest income of each segment represents the difference between actual interest earned on assets and interest paid on liabilities of the segment, adjusted for a funding charge or credit. Segments are charged a cost to fund assets (e.g. customer loans) and receive a funding credit for funds provided (e.g. customer deposits) based on equivalent market rates. The objective of these charges/credits is to transfer interest rate risk from the segments to one centralized unit in Global Banking and Markets and more appropriately reflect the profitability of segments.

Certain other revenue and operating expense amounts are also apportioned among the business segments based upon the benefits derived from this activity or the relationship of this activity to other segment activity. For segment reporting purposes, these inter-segment transactions are accounted for as if they were with third parties and have not been eliminated.

Results for each segment on an IFRSs basis, as well as a reconciliation of total results under IFRSs to U.S. GAAP consolidated totals, are provided in the following tables. Descriptions of the significant differences between IFRSs and U.S. GAAP that impact our results follow the tables.

| **IFRSs Consolidated Amounts** | | | |
|---|---|---|---|
| **Global** | | **(4)** | **(5)** |
| | **Intersegmental** | **IFRSs** | **IFRSs** |

| | PFS | CF | CMB | Banking and Markets | PB | Other | Revenue | Total | Adjustments | Reclassifications | C |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | (in millions) | | | | |
| **Three months ended March 31, 2009** | | | | | | | | | | | |
| Net interest income(1) | **$187** | **$529** | **$176** | **$232** | **$42** | **$1** | **$(11)** | **$1,156** | **$102** | **$90** | |
| Other operating income | **40** | **81** | **81** | **221** | **33** | **156** | **11** | **623** | **99** | **28** | |
| Total operating income (loss) | **227** | **610** | **257** | **453** | **75** | **157** | **-** | **1,779** | **201** | **118** | |
| Loan impairment charges(3) | **200** | **554** | **81** | **229** | **(3)** | **-** | **-** | **1,061** | **214** | **(101)** | |
| | **27** | **56** | **176** | **224** | **78** | **157** | **-** | **718** | **(13)** | **219** | |
| Operating expenses(2) | **296** | **14** | **154** | **199** | **59** | **13** | **-** | **735** | **18** | **219** | |
| Profit (loss) before tax expense | **(269)** | **42** | **22** | **25** | **19** | **144** | **-** | **(17)** | **(31)** | **-** | |
| Tax expense (benefit) | **(95)** | **15** | **8** | **9** | **7** | **149** | **-** | **93** | **(52)** | **-** | |
| Net income (loss) | **$(174)** | **$27** | **$14** | **$16** | **$12** | **$(5)** | **$-** | **$(110)** | **$21** | **$-** | |
| **Balances at end of period:** | | | | | | | | | | | |
| Total assets | **$25,747** | **$32,897** | **$18,830** | **$230,214** | **$4,890** | **$111** | **$-** | **$312,689** | **$(129,683)** | **$(1,237)** | |
| Total loans | **20,674** | **31,240** | **17,331** | **39,171** | **4,080** | **-** | **-** | **112,496** | **(5,523)** | **(13,721)** | |
| Goodwill | **876** | **-** | **368** | **497** | **326** | **-** | **-** | **2,067** | **580** | **-** | |
| Total deposits | **47,525** | **36** | **21,018** | **35,247** | **11,486** | **2** | **-** | **115,314** | **(5,343)** | **5,359** | |
| **Three months ended March 31, 2008** | | | | | | | | | | | |
| Net interest income(1) | $247 | $294 | $184 | $122 | $49 | $2 | $(106) | $792 | $(5) | $174 | |
| Other operating income | 226 | 93 | 71 | (717) | 43 | 164 | 106 | (14) | - | (71) | |
| Total operating | 473 | 387 | 255 | (595) | 92 | 166 | - | 778 | (5) | 103 | |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| income (loss) | | | | | | | | | | |
| Loan impairment charges(3) | 59 | 368 | 47 | 42 | (3) | - | - | 513 | (3) | (12) |
| | 414 | 19 | 208 | (637) | 95 | 166 | - | 265 | (2) | 115 |
| Operating expenses(2) | 280 | 17 | 144 | 203 | 61 | - | - | 705 | - | 115 |
| Profit (loss) before tax expense | 134 | 2 | 64 | (840) | 34 | 166 | - | (440) | (2) | - |
| Tax expense (benefit) | 51 | 1 | 25 | (318) | 13 | 64 | - | (164) | - | - |
| Net income (loss) | $83 | $1 | $39 | $(522) | $21 | $102 | $- | $(276) | $(2) | $- |
| **Balances at end of period:** | | | | | | | | | | |
| Total assets | $35,931 | $20,722 | $20,923 | $217,692 | $5,626 | $379 | $- | $301,273 | $(106,146) | $(3,406) |
| Total loans | 28,893 | 20,266 | 18,924 | 28,868 | 4,834 | - | - | 101,785 | (858) | (8,262) |
| Goodwill | 924 | - | 368 | 497 | 326 | - | - | 2,115 | 586 | - |
| Total deposits | 44,138 | 39 | 19,124 | 44,192 | 12,759 | 2 | - | 120,254 | (3,653) | 3,541 |

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(1) Net interest income of each segment represents the difference between actual interest earned on assets and interest paid on liabilities of the segment adjusted for a funding charge or credit. Segments are charged a cost to fund assets (e.g. customer loans) and receive a funding credit for funds provided (e.g. customer deposits) based on equivalent market rates.

(2) Expenses for the segments include fully apportioned corporate overhead expenses.

(3) The provision assigned to the segments is based on the segments' net charge offs and the change in allowance for credit losses.

(4) IFRS Adjustments consist of the accounting differences between U.S. GAAP and IFRSs which have been described more fully below.

(5) Represents differences in balance sheet and income statement presentation between IFRSs and U.S. GAAP.

Further discussion of the differences between IFRSs and U.S. GAAP are presented in Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Form 10-Q under the caption "Basis of Reporting." A summary of the significant differences between U.S. GAAP and IFRSs as they impact our

results are presented below:

***Net interest income***

*Deferred loan origination costs and fees*
 - Certain loan fees and incremental direct loan costs, which would not have been incurred but for the origination of loans, are deferred and amortized to earnings over the life of the loan under IFRSs. Certain loan fees and direct incremental loan origination costs, including internal costs directly attributable to the origination of loans in addition to direct salaries, are deferred and amortized to earnings under U.S. GAAP.

Loan origination deferrals under IFRSs are more stringent and result in lower costs being deferred than permitted under U.S. GAAP. In addition, all deferred loan origination fees, costs and loan premiums must be recognized based on the expected life of the receivables under IFRSs as part of the effective interest calculation while under U.S. GAAP they may be recognized on either a contractual or expected life basis.

Under IFRSs, net interest income includes the interest element for derivatives which corresponds to debt designated at fair value. For U.S. GAAP, this is included in gain on financial instruments designated at fair value and related derivatives which is a component of other revenues.

***Other operating income (Total other revenues)***

*Derivatives*
 - Effective January 1, 2008, U.S. GAAP removed the observability requirement of valuation inputs to recognize the difference between transaction price and fair value as Day 1 profit and loss and permits recognition up front in the consolidated statement of (loss) income. Under IFRSs, recognition is permissible only if the inputs used in calculating fair value are based on observable inputs. If the inputs are not observable, profit and loss is deferred and is recognized: (1) over the period of contract, (2) when the data becomes observable, or (3) when the contract is settled. This causes the net income under U.S. GAAP to be different than under IFRSs.

*Unquoted equity securities*
 - Under IFRSs, equity securities which are not quoted on a recognized exchange (MasterCard Class B shares and Visa Class B shares), but for which fair value can be reliably measured, are required to be measured at fair value. Securities measured at fair value under IFRSs are classified as either available for sale securities, with changes in fair value recognized in shareholders' equity, or as trading securities, with changes in fair value recognized in income. Under U.S. GAAP, equity securities that are not quoted on a recognized exchange are not considered to have a readily determinable fair value and are required to be measured at cost, less any provisions for known impairment, in other assets.

*Loans held for sale*
 - IFRSs requires loans designated as held for sale at the time of origination to be treated as trading assets and recorded at their fair market value. Under U.S. GAAP, loans designated as held for sale are reflected as loans and recorded at the lower of amortized cost or fair value. Under IFRSs, the income and expenses related to receivables held for sale are reported in net interest income on trading. Under U.S. GAAP, the income and expenses related to receivables held for sale are reported similarly to loans held for investment.

For loans transferred to held for sale subsequent to origination, IFRSs requires these receivables to be reported separately on the balance sheet but does not change the measurement criteria. Accordingly, for IFRSs purposes such loans continue to be accounted for in accordance with IAS 39 with any gain or loss recorded at the time of sale. U.S. GAAP requires loans that management intends to sell to be transferred to a held for sale category at the lower of cost or fair value. Under U.S. GAAP, the component of the lower of cost or fair value adjustment related to credit risk is recorded in the consolidated statement of (loss) income as provision for credit losses while the component related to

interest rates and liquidity factors is reported in the consolidated statement of (loss) income in other revenues.

*Fair value option -*
*LAF*
*loan reclass*
- Certain Leverage Acquisition Finance (
LAF
) Loans were classified as "Trading Assets" for IFRSs and to be consistent, an irrevocable fair value option was elected on these loans under U.S. GAAP on January 1, 2008. These loans were classified to "loans and advances" as of July 1, 2008 under IFRSs pursuant to an amendment to IAS 39. Under U.S. GAAP, these loans are classified "held for sale" and carried at fair value due to the irrevocable nature of the fair value option.

*Servicing assets*
- Under IAS 38, servicing assets are initially recorded on the balance sheet at cost and amortized over the projected life of the assets. Servicing assets are periodically tested for impairment with impairment adjustments charged against current earnings. Under U.S. GAAP, servicing assets are initially recorded on the balance sheet at fair value. All subsequent adjustments to fair value are reflected in current period earnings.

*Other-than-temporary impairment*
- Effective January 1, 2009 under U.S. GAAP, the credit loss component of an other-than-temporary impairment of a debt security is recognized in earnings while the remaining portion of the impairment loss is recognized in other comprehensive income provided a company concludes it does not intend to sell the security and it is not more-likely-than-not that it will need to sell the security prior to recovery. Under IFRSs, there is no bifurcation and the entire impairment is recognized in earnings.

There are also other less significant differences in measuring other-than-temporary impairment under IFRSs versus U.S. GAAP.

***Loan impairment charges (Provision for credit losses)***

IFRSs requires a discounted cash flow methodology for estimating impairment on pools of homogeneous customer loans which requires the incorporation of the time value of money relating to recovery estimates. Also under IFRSs, future recoveries on charged-off loans are accrued for on a discounted basis and a recovery asset is recorded. Subsequent recoveries are recorded to earnings under U.S. GAAP, but are adjusted against the recovery asset under IFRSs. Interest is recorded based on collectability under IFRSs.

As discussed above, under U.S. GAAP, the credit risk component of the lower of cost or fair value adjustment related to the transfer of receivables to held for sale is recorded in the consolidated statement of (loss) income as provision for credit losses. There is no similar requirement under IFRSs.

***Operating expenses (Total operating expenses)***

*Pension costs*
- Costs under U.S. GAAP are higher than under IFRSs as a result of the amortization of the amount by which actuarial losses exceed gains beyond the 10 percent "corridor."

***Assets***

*Derivatives*
- Under U.S. GAAP, derivative receivables and payables with the same counterparty may be reported on a net basis in the balance sheet when there is an executed International Swaps and Derivatives Association, Inc. (ISDA) Master

Netting Arrangement. In addition, under U.S. GAAP, fair value amounts recognized for the obligation to return cash collateral received or the right to reclaim cash collateral paid are offset against the fair value of derivative instruments. Under IFRSs, these agreements do not necessarily meet the requirements for offset, and therefore such derivative receivables and payables are presented gross on the balance sheet.

*Goodwill*
- IFRSs and U.S. GAAP require goodwill to be tested for impairment at least annually, or more frequently if circumstances indicate that goodwill may be impaired. For IFRSs, goodwill was amortized until 2005, however goodwill was amortized under U.S. GAAP until 2002, which resulted in a lower carrying amount of goodwill under IFRSs.

*Property*
- Under IFRSs, the value of property held for own use reflects revaluation surpluses recorded prior to January 1, 2004. Consequently, the values of tangible fixed assets and shareholders' equity are lower under U.S. GAAP than under IFRSs. There is a correspondingly lower depreciation charge and higher net income as well as higher gains (or smaller losses) on the disposal of fixed assets under U.S. GAAP. For investment properties, net income under U.S. GAAP does not reflect the unrealized gain or loss recorded under IFRSs for the period.

*Securities -*
Under IFRSs, securities include HSBC shares held for stock plans which are recorded at fair value through other comprehensive income. If it is determined these shares have become impaired, the fair value loss is recognized in profit and loss and any fair value loss recorded in other comprehensive income is reversed.

Some securities were reclassified from "trading assets" to "loans and receivables" as of July 1, 2008 under IFRSs, pursuant to an amendment to IAS 39. In November 2008, additional securities were similarly transferred to loans and receivables. These securities continue to be classified as "trading assets" under U.S. GAAP.

***16. Regulatory Capital***

Capital amounts and ratios of HSBC USA Inc and HSBC Bank USA, calculated in accordance with current banking regulations, are summarized in the following table.

| | March 31, 2009 | | | December 31, 2008 | | |
|---|---|---|---|---|---|---|
| | Capital Amount | Well-Capitalized Minimum Ratio(1) | Actual Ratio | Capital Amount | Well-Capitalized Minimum Ratio(1) | Actual Ratio |
| | (dollars are in millions) | | | | | |
| Total capital ratio: | | | | | | |
| HSBC USA Inc. | **$18,665** | **10.00%** | **12.17%** | $17,691 | 10.00% | 12.04% |
| HSBC Bank USA | **18,966** | **10.00** | **12.56** | 17,395 | 10.00 | 12.04 |
| Tier 1 capital ratio: | | | | | | |
| HSBC USA Inc. | **12,057** | **6.00** | **7.86** | 11,156 | 6.00 | 7.60 |
| HSBC Bank USA | **12,319** | **6.00** | **8.16** | 10,822 | 6.00 | 7.49 |
| Tier 1 leverage ratio: | | | | | | |
| HSBC USA Inc. | **12,057** | **3.00(2)** | **6.57** | 11,156 | 3.00(2) | 5.96 |
| HSBC Bank USA | **12,319** | **5.00** | **6.86** | 10,822 | 5.00 | 5.90 |

| Risk weighted assets: | | |
|---|---|---|
| HSBC USA Inc. | **153,316** | 146,878 |
| HSBC Bank USA | **151,044** | 144,507 |

___________

(1) HSBC USA Inc and HSBC Bank USA are categorized as "well-capitalized", as defined by their principal regulators. To be categorized as well-capitalized under regulatory guidelines, a banking institution must have the minimum ratios reflected in the above table, and must not be subject to a directive, order, or written agreement to meet and maintain specific capital levels.

(2) There is no Tier 1 leverage ratio component in the definition of a well-capitalized bank holding company. The ratio shown is the minimum required ratio.

In the first quarter of 2009, we received capital contributions from HSBC North America Inc. (HNAI) in an aggregate amount of approximately $1.1 billion in exchange for two shares of common stock. This amount, along with an additional $0.6 billion received by us from HNAI in December 2008, was subsequently contributed to our subsidiary, HSBC Bank USA, to provide capital support for receivables purchased from our affiliate, HSBC Finance Corporation. Refer to Note 4 "Loans" for additional information.

As part of the regulatory approvals with respect to the aforementioned receivable purchases completed in January 2009, HSBC Bank USA and its ultimate parent HSBC committed that HSBC Bank USA will maintain a Tier 1 risk-based capital ratio of at least 7.62 percent, a total capital ratio of at least 11.55 percent and a Tier 1 leverage ratio of at least 6.45 percent for one year following the date of transfer. In addition, HSBC Bank USA and HSBC made certain additional capital commitments to ensure that HSBC Bank USA holds sufficient capital with respect to the purchased receivables that are or become "low-quality assets," as defined by the Federal Reserve Act.

In February 2009, the U.S. Treasury Department announced that U.S regulators would conduct a stress test of all U.S. bank holding companies with assets in excess of $100 billion. The results of these tests may cause additional regulatory capital requirements for the companies that are subjected to the test. As a result of foreign ownership, we are not included in the group of bank holding companies subject to the regulatory stress test.

Regulatory guidelines impose certain restrictions that may limit the inclusion of deferred tax assets in the computation of regulatory capital. Continued losses coupled with bad debt provisions that exceed charge-offs which are creating additional deferred tax assets, could lead to such an exclusion in future periods. We closely monitor the deferred tax assets for potential limitations or exclusions in future periods for capital planning purposes.

***17. Special Purpose Entities***

In the ordinary course of business, we organize special purpose entities ("SPEs") primarily to structure financial products to meet our clients' investment needs and to securitize financial assets held to meet our own funding needs. For disclosure purposes, we aggregate SPEs based on the purpose of organizing the entities, the risk characteristics

and the business activities of the SPEs. Special purpose entities can be a variable interest entity ("VIE"), a qualifying special purpose entity ("QSPE") or neither. A VIE is an entity that lacks sufficient equity at risk or whose equity investors do not have a controlling interest. A QSPE is an unconsolidated off-balance sheet entity whose activities are restricted and limited to holding and servicing financial assets and provided it meets the requirements of FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities" ("SFAS 140").

***Variable Interest Entities***

We consolidate VIEs in which we hold variable interests that absorb a majority of the risks and/or receive a majority of the benefits and therefore are deemed to be the primary beneficiary. We take into account all of our involvements in a VIE in identifying variable interests (explicit or implicit) that individually or in the aggregate could be significant enough to warrant our designation as the primary beneficiary and hence require us to consolidate the VIE or otherwise require us to make appropriate disclosures under FIN 46(R). We consider our involvement to be significant where we, among other things, (i) provide liquidity put options or other liquidity facilities to support the VIE's debt issuances, (ii) enter into derivative contracts to absorb the risks and benefits from the VIE or from the assets held by the VIE, (iii) provide a financial guarantee that covers assets held or liabilities issued and (iv) help structure the transaction and retain a financial or servicing interest in the VIE.

In most cases, a qualitative analysis of our involvement in the entity provides sufficient evidence to determine whether we are the primary beneficiary. In rare cases, a more detailed analysis to quantify the extent of variability to be absorbed by each variable interest holder is required to determine the primary beneficiary. The quantitative analysis provides probability-weighted estimates of a range of potential outcomes and management judgment is required in determining the primary beneficiary.

***Consolidated VIEs***

The following table summarizes the assets and liabilities of our consolidated VIEs as of March 31, 2009 and December 31, 2008:

| | **March 31, 2009** | | **December 31, 2008** | |
|---|---|---|---|---|
| | **Consolidated Assets** | **Consolidated Liabilities** | **Consolidated Assets** | **Consolidated Liabilities** |
| | | **(in millions)** | | |
| Securitization vehicles | **$7,551** | **$6,278** | $1,588 | $1,200 |
| Structured note vehicles | **121** | **120** | 147 | 124 |
| Total | **$7,672** | **$6,398** | $1,735 | $1,324 |

***Securitization Vehicles***

We utilize entities that are structured as trusts to securitize certain private label and other credit card receivables where securitization provides an attractive source of low cost funding. We transfer the credit card receivables to the trusts which in turn issue debt instruments collateralized by the transferred receivables. These trusts are considered VIEs and are consolidated as we are the primary beneficiary at March 31, 2009 and December 31, 2008.

We held debt securities issued by these securitization vehicles at such a level that we were deemed to be the primary beneficiary and, as such, we consolidated these entities. At March 31, 2009 and December 31, 2008, the consolidated assets of these trusts were $7,551 million and $1,588 million, respectively and were reported in loans. Debt securities issued by these VIEs are reported as secured financings in long-term debt.

***Structured Note Vehicles***

In the normal course of business, we enter into derivative transactions with special purpose entities organized by HSBC affiliates and by third parties for the purpose of issuing structured debt instruments to facilitate clients' investment demand. These entities, which are deemed to be VIEs, are organized as trusts and issue fixed or floating rate debt instruments backed by the financial assets they hold. They were established to create investments with specific risk profiles for investors.

At March 31, 2009 and December 31, 2008, we held all or substantially all of the debt securities issued by several VIE trusts that were organized by an affiliate and by third parties to issue structured notes. The consolidated assets of these VIEs were $121 million and $147 million at March 31, 2009 and December 31, 2008, respectively, and are reported in trading assets. Debt instruments issued by these VIEs and held by us were eliminated in consolidation. Debt instruments issued by these VIEs and held by third parties were not material.

The assets of consolidated VIEs serve as collateral for the obligations of the VIEs. The holders of debt instruments issued by consolidated VIEs have no recourse to our general credit. There are no communications or contractual arrangements that constitute an obligation by us to provide financial support to the VIEs or the holders of debt securities issued by the VIEs.

***Unconsolidated VIEs***

We also had significant involvement with other VIEs that were not consolidated at March 31, 2009 or December 31, 2008 because we were not the primary beneficiary. The following table provides additional information on those unconsolidated VIEs, the variable interests held by us and our maximum exposure to loss arising from our involvements in those VIEs as of March 31, 2009 and December 31, 2008:

| | **March 31, 2009** | | | | **December 31, 2008** | |
|---|---|---|---|---|---|---|
| | **Variable Interests Held Classified as Assets** | **Variable Interests Held Classified as Liabilities** | **Total Assets in Unconsolidated VIEs** | **Maximum Exposure to Loss** | **Total Assets in Unconsolidated VIEs** | **Maximum Exposure to Loss** |
| | | | **(in millions)** | | | |
| Asset-backed commercial paper conduits | **$527** | **$-** | **$24,448** | **$7,830** | $28,112 | $7,782 |
| Structured investment vehicles | **29** | **-** | **5,829** | **32** | 4,768 | 34 |
| Structured note vehicles | **1,009** | **529** | **8,044** | **2,408** | 8,221 | 1,842 |
| Low income | **16** | **-** | **211** | **40** | 211 | 40 |

| | | | | | | |
|---|---|---|---|---|---|---|
| housing<br><br>partnerships | | | | | | |
| Total | **$1,581** | **$529** | **$38,532** | **$10,310** | $41,312 | $9,698 |

Information on the types of variable interest entities with which we are involved, the nature of our involvement and the variable interests held in those entities is presented below.

***Asset-Backed Commercial Paper Conduits***

We provide liquidity facilities to a number of multi-seller and single-seller asset-backed commercial paper conduits ("ABCP conduits") sponsored by HSBC affiliates and by third parties. These conduits support the financing needs of customers by facilitating the customers' access to commercial paper markets.

Customers sell financial assets, such as trade receivables, to ABCP conduits, which fund the purchases by issuing short-term highly-rated commercial paper collateralized by the assets acquired. In a multi-seller conduit, any number of companies may be originating and selling assets to the conduit whereas a single-seller conduit acquires assets from a single company. We, along with other financial institutions, provide liquidity facilities to ABCP conduits in the form of lines of credit or asset purchase commitments. Liquidity facilities provided to multi-seller conduits support transactions associated with a specific seller of assets to the conduit and we would only be required to provide support in the event of certain triggers associated with those transactions and assets. Liquidity facilities provided to single-seller conduits are not identified with specific transactions or assets and we would be required to provide support upon occurrence of certain triggers that generally affect the conduit as a whole. Our obligations are generally pari passu with that of other institutions that also provide liquidity support to the same conduit or for the same transactions. We do not provide any program-wide credit enhancements to ABCP conduits.

Each seller of assets to an ABCP conduit typically provides collateral in the form of excess assets and therefore bears the risk of first loss related to the specific assets transferred. We do not transfer our own assets to the conduits. We have no ownership interests in, perform no administrative duties for, and do not service any of the assets held by the conduits. We are not the primary beneficiary and do not consolidate any of the ABCP conduits to which we provide liquidity facilities. Credit risk related to the liquidity facilities provided is managed by subjecting them to our normal underwriting and risk management processes. The $7,830 million maximum exposure to loss presented in the table above represents the maximum amount of loans and asset purchases we could be required to fund under the liquidity facilities. The maximum loss exposure is estimated assuming the facilities are fully drawn and the underlying collateralized assets are in default with zero recovery value.

***Structured Investment Vehicles***

We provide a liquidity facility to a single structured investment vehicle ("SIV") sponsored by a third party. This entity, which is deemed to be a VIE, seeks to earn a profit by investing in mostly highly rated longer-dated fixed income instruments and funding those investments by issuing cheaper short-term, highly rated commercial paper and medium term notes. We do not transfer our own assets to the SIV. We have no ownership interests in, perform no administrative duties for, and do not service any of the assets the SIV holds. We are not the primary beneficiary of the SIV and therefore do not consolidate the SIV. Credit risk related to the liquidity facility provided is managed through our normal underwriting and risk management processes. The maximum exposure to loss presented in the preceding table represents a $32 million liquidity facility which was fully funded, and is recorded as a loan, as of March 31, 2009. This loan was considered in the determination of our allowance for loan losses and an $3 million specific reserve has been established against this facility in accordance with our credit policies.

***Structured Note Vehicles***

Our involvements in structured note vehicles include entering into derivative transactions such as interest rate and currency swaps, and investing in their debt instruments. With respect to several of these VIEs, we hold variable interests in the form of total return swaps entered into in connection with the transfer of certain assets to the VIEs. In these transactions, we transferred financial assets from our trading portfolio to the VIEs and entered into total return swaps under which we receive the total return on the transferred assets and pay a market rate of return. The transfers of assets in these transactions do not qualify as sales under the applicable accounting literature and are accounted for as secured borrowings. Accordingly, the transferred assets continue to be recognized as trading assets on our balance sheet and the funds received are recorded as liabilities in long-term debt. As of March 31, 2009, we recorded approximately $290 million of trading assets and $479 million of long-term liabilities on our balance sheet as a result of "failed sale" accounting treatment for certain transfers of financial assets. As of December 31, 2008, we recorded approximately $539 million of trading assets and $829 million of long-term liabilities on our balance sheet as a result of "failed sale" accounting treatment. The financial assets and financial liabilities were not legally ours and we have no control over the financial assets which are restricted solely to satisfy the liability.

In addition to its variable interests, we also hold credit default swaps with these structured note VIEs under which we receive credit protection on specified reference assets in exchange for the payment of a premium. Through these derivatives, the VIEs assume the credit risk associated with the reference assets which is then passed on to the holders of the debt instruments they issue. Because they create rather than absorb variability, the credit default swaps we hold are not considered variable interests.

We record all investments in, and derivative contracts with, unconsolidated structured note vehicles at fair value on our consolidated balance sheet. Our maximum exposure to loss is limited to the recorded amounts of these instruments.

***Low Income Housing Partnerships***

We invest as a limited partner in a number of low-income housing partnerships that operate qualified affordable housing projects and generate tax benefits, including federal low-income housing tax credits, for investors. Some of the partnerships are deemed to be VIEs because they do not have sufficient equity investment at risk or are structured with non-substantive voting rights. We are not the primary beneficiary of these VIEs and do not consolidate them.

Our investments in low-income housing partnerships are recorded using the equity method of accounting and are included in other assets on the consolidated balance sheet. The maximum exposure to loss shown in the table represents the recorded investment net of estimated expected reductions in future tax liabilities and potential recapture of tax credits allowed in prior years.

***Unconsolidated QSPEs***

We organize special purpose entities to securitize residential mortgage loans. In these cases, we purchase and transfer residential mortgage loans into a trust which is designed and structured as a QSPE. The QSPE issues debt securities to investors to finance the purchase of the residential mortgage loans. The securitizations are non-recourse in that the risk of future loss in the transferred residential mortgages has been transferred to the investors and the investors' recourse is limited to the transferred assets. The transfers are accounted for as sales in accordance with SFAS 140.

Neither the transferor nor its consolidated affiliates have any continuing involvement with the transferred assets. We do not provide any liquidity arrangement or financial support (through written or unwritten communications) to, enter into any derivative transactions with, or have any obligation to repurchase financial assets from the QSPE or the investors. Neither the transferor nor its consolidated affiliates retains any residual interests in the transferred financial assets. On limited occasions, we transfer residential mortgage loans we originated to the QSPE and retain the right to service the transferred assets. In those cases, the transferred residential mortgages for which we retain the servicing rights represent an insignificant portion of the entire transferred asset portfolio.

***18. Guarantee Arrangements and Pledged Assets***

As part of our normal operations, we enter into various off-balance sheet guarantee arrangements with affiliates and third parties. These arrangements arise principally in connection with our lending and client intermediation activities and include standby letters of credit and certain credit derivative transactions. The contractual amounts of these arrangements represent our maximum possible credit exposure in the event that we are required to fulfill the maximum obligation under the contractual terms of the guarantee.

The following table presents total carrying value and contractual amounts of our major off-balance sheet guarantee arrangements as of March 31, 2009 and December 31, 2008. Following the table is a description of the various arrangements.

| | March 31, 2009 | | December 31, 2008 | |
|---|---|---|---|---|
| | Carrying Value | Notional/Maximum Exposure to Loss | Carrying Value | Notional/Maximum Exposure to Loss |
| | (in millions) | | | |
| Credit derivatives(1),(3) | **$(55,648)** | **$460,331(1)** | $(59,640) | $493,583(1) |
| Financial standby letters of credit, net of participations(2),(4) | **-** | **4,464(2)** | - | 4,444(2) |
| Performance (non-financial) guarantees | **-** | **3,736** | - | 3,800 |
| Liquidity asset purchase agreements(3) | **-** | **7,830** | - | 7,782 |
| Total | **$(55,648)** | **$476,361** | $(59,640) | $509,609 |

(1) Includes $74,264 million and $103,409 million issued for the benefit of HSBC affiliates at March 31, 2009 and December 31, 2008, respectively.

(2) Includes $736 million and $732 million issued for the benefit of HSBC affiliates at March 31, 2009 and December 31, 2008, respectively.

(3) For standby letters of credit and liquidity asset purchase agreements, maximum loss represents losses to be recognized assuming the letter of credit and liquidity facilities have been fully drawn and the obligors have defaulted with zero recovery.

(4) For credit derivatives, the maximum loss is represented by the notional amounts without consideration of mitigating effects from collateral or recourse arrangements.

***Credit-Risk Related Guarantees:***

***Credit Derivatives***

Credit derivatives are financial instruments that transfer the credit risk of a reference obligation from the credit protection buyer to the credit protection seller who is exposed to the credit risk without buying the reference obligation. We sell credit protection on underlying reference obligations (such as loans or securities) by entering into credit derivatives, primarily in the form of credit default swaps, with various institutions. We account for all credit derivatives at fair value. Where we sell credit protection to a counterparty that holds the reference obligation, the arrangement is effectively a financial guarantee on the reference obligation. Although we do not specifically identify whether the derivative counterparty retains the reference obligation, we have disclosed information about all credit derivatives that could meet the accounting definition of a financial guarantee. Under a credit derivative contract, the credit protection seller will reimburse the credit protection buyer upon occurrence of a credit event (such as bankruptcy, insolvency, restructuring or failure to meet payment obligations when due) as defined in the derivative contract, in return for a periodic premium. Upon occurrence of a credit event, we will pay the counterparty the stated notional amount of the derivative contract and receive the underlying reference obligation. The recovery value of the reference obligation received could be significantly lower than its notional principal amount when a credit event occurs.

Certain derivative contracts are subject to master netting arrangements and related collateral agreements. A party to a derivative contract may demand that the counterparty post additional collateral in the event its net exposure exceeds certain predetermined limits and when the credit rating falls below a certain grade. We set the collateral requirements by counterparty such that the collateral covers various transactions and products, and is not allocated to specific individual contracts. The collateral amount presented in the table above only includes those derivative contracts or transactions where specific collateral can be identified.

We manage our exposure to credit derivatives using a variety of risk mitigation strategies where we enter into offsetting hedge positions or transfer the economic risks, in part or in entirety, to investors through the issuance of structured credit products. We actively manage the credit and market risk exposure in the credit derivative portfolios on a net basis and, as such, retain no or a limited net sell protection position at any time. The following table summarizes our net credit derivative positions as of March 31, 2009 and December 31, 2008:

| | March 31, 2009 | December 31, 2008 |
|---|---|---|

| | **Carrying (Fair) Value** | **Notional** | Carrying (Fair) Value | Notional |
|---|---|---|---|---|
| | | **(in millions)** | | |
| Sell-protection credit derivative positions | **$(55,648)** | **$460,331** | $(59,640) | $493,583 |
| Buy-protection credit derivative positions | **56,992** | **454,144** | 59,737 | 474,677 |
| Net position | **$1,344** | **$6,187** | $97 | $18,906 |

***Standby Letters of Credit***

A standby letter of credit is issued to a third party for the benefit of a customer and is a guarantee that the customer will perform or satisfy certain obligations under a contract. It irrevocably obligates us to pay a specified amount to the third party beneficiary if the customer fails to perform the contractual obligation. We issue two types of standby letters of credit: performance and financial. A performance standby letter of credit is issued where the customer is required to perform some nonfinancial contractual obligation, such as the performance of a specific act, whereas a financial standby letter of credit is issued where the customer's contractual obligation is of a financial nature, such as the repayment of a loan or debt instrument. As of March 31, 2009, the total amount of outstanding financial standby letters of credit (net of participations) and performance guarantees were $4,464 million and $3,736 million, respectively. As of December 31, 2008, the total amount of outstanding financial standby letters of credit (net of participations) and performance guarantees were $4,444 million and $3,800 million, respectively.

The issuance of a standby letter of credit is subject to our credit approval process and collateral requirements. We charge fees for issuing letters of credit commensurate with the customer's credit evaluation and the nature of any collateral. Included in other liabilities are deferred fees on standby letters of credit, which represent the fair value of the stand-ready obligation to perform under these guarantees, amounting to $34 million and $33 million at March 31, 2009 and December 31, 2008, respectively. Also included in other liabilities is an allowance for credit losses on unfunded standby letters of credit of $32 million and $30 million at March 31, 2009 and December 31, 2008, respectively.

Pursuant to FSP SFAS 133-1 and FIN 45-4, below is a summary of the credit ratings of credit risk related guarantees including the credit ratings of counterparties against which we sold credit protection and financial standby letters of credit as of March 31, 2009 as an indicative proxy of payment risk:

| | **Average Life** | **Credit Ratings of the Obligors or the Transactions** | |
|---|---|---|---|
| | | **Investment** | **Non-Investment** |

| Notional/Contractual Amounts | (in years) | Grade | Grade | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| Self-protection Credit Derivatives(a) | | | | |
| Single name CDS | **3.7** | **$183,450** | **$61,885** | **$245,335** |
| Structured CDS | **3.8** | **9,052** | **46,267** | **55,319** |
| Index credit derivatives | **4.3** | **87,930** | **57,289** | **145,219** |
| Total return swaps | **8.6** | **4,818** | **9,640** | **14,458** |
| Subtotal | | **285,250** | **175,081** | **460,331** |
| Financial Standby Letters of Credit(b) | **1.5** | **7,943** | **257** | **8,200** |
| Total | | **$293,193** | **$175,338** | **$468,531** |

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(a) The credit ratings in the table represent external credit ratings for classification as investment grade and non-investment grade.

(b) External ratings for most of the obligors are not available. Presented above are the internal credit ratings which are developed using similar methodologies and rating scale equivalent to external credit ratings for purposes of classification as investment grade and non-investment grade.

Our internal groupings are determined based on our risk rating systems and processes which assign a credit grade based on a scale which ranks the risk of loss from a customer as either low risk, satisfactory risk, fair risk, watch, substandard, doubtful or loss. The groupings are determined and used for managing risk and determining level of credit exposure appetite based on the customer's operating performance, liquidity, capital structure and debt service ability. In addition, we also incorporate subjective judgments into the risk rating process concerning such things as industry trends, comparison of performance to industry peers and perceived quality of management. We compare our internal risk ratings to outside external rating agencies benchmarks, where possible, at the time of formal review and regularly monitor whether our risk ratings are comparable to the external ratings benchmark data.

***Written Put Options, Non Credit-Risk Related Guarantees and Indemnity Arrangements:***

***Liquidity Asset Purchase Agreements***

We provide liquidity facilities to a number of multi-seller and single-seller asset-backed commercial paper conduits sponsored by affiliates and third parties. The conduits finance the purchase of individual assets by issuing commercial paper to third party investors. Each liquidity facility is transaction specific and has a maximum limit. Pursuant to the liquidity agreements, we are obligated, subject to certain limitations, to purchase the eligible assets from the conduit at an amount not to exceed the face value of the commercial paper in the event the conduit is unable to refinance its commercial paper. A liquidity asset purchase agreement is essentially a conditional written put option issued to the conduit where the exercise price is the face value of the commercial paper. As of March 31, 2009 and December 31, 2008, we have issued $7,830 million and 7,782 million, respectively, of liquidity facilities to provide liquidity support to the commercial paper issued by various conduits.

***Principal Protected Products***

We structure and sell products that guarantee the return of principal to investors on a future date. These structured products have various reference assets and we are obligated to cover any shortfall between the market value of the underlying reference portfolio and the principal amount at maturity. We manage such shortfall risk by, among other things, establishing structural and investment constraints. Additionally, the structures require liquidation of the underlying reference portfolio when certain pre-determined triggers are breached and the proceeds from liquidation

are required to be invested in zero-coupon bonds that would generate sufficient funds to repay the principal amount upon maturity. We may be exposed to market (gap) risk at liquidation and, as such, may be required to make up the shortfall between the liquidation proceeds and the purchase price of the zero coupon bonds. These principal protected products are accounted for on a fair value basis. The notional amounts of these principal protected products were not material as of March 31, 2009 and December 31, 2008, respectively. We have not made any payment under the terms of these structured products and we consider the probability of payments under these guarantees to be remote.

***Sale of Mortgage Loans***

We originate and sell mortgage loans to government sponsored entities and provide various representations and warranties related to, among other things, the ownerships of the loans, the validity of the liens, the loan selection and origination process, and the compliance to the origination criteria established by the agencies. In the event of a breach of our representations and warranties, we may be obligated to repurchase the loans with identified defects or to indemnify the buyers. Our contractual obligation arises only when the representations and warranties are breached. A liability was recorded for our obligations arising from the breach of representations and warranties, however it was not material as of March 31, 2009 or December 31, 2008.

***Visa Covered Litigations***

We are an equity member of Visa Inc. ("Visa"). Prior to its initial public offering ("IPO") on March 19, 2008, Visa completed a series of transactions to reorganize and restructure its operations and to convert membership interests into equity interests. Pursuant to the restructuring, we, along with all the Class B shareholders, agreed to indemnify Visa for the claims and obligations arising from certain specific covered litigations. Class B shares are convertible into listed Class A shares upon (i) settlement of the covered litigations or (ii) the third anniversary of the IPO, whichever is earlier. The indemnification is subject to the accounting and disclosure requirements under FIN No. 45. Visa used a portion of the IPO proceeds to establish a $3.0 billion escrow account to fund future claims arising from those covered litigations (the escrow was subsequently increased to $4.1 billion). In the event the escrow is insufficient to satisfy the legal claims, Visa may raise funds from a secondary offering and seek reimbursement from the Class B shareholders by reducing the conversion ratio into Class A shares. As of March 31, 2009, we do not expect the indemnity obligation to result in a material adverse effect on our liquidity position.

***Clearinghouses and Exchanges***

We are a member of various exchanges and clearinghouses that trade and clear securities and/or futures contracts. As a member, we may be required to pay a proportionate share of the financial obligations of another member who defaults on its obligations to the exchange or the clearinghouse. Our guarantee obligations would arise only if the exchange or clearinghouse had exhausted its resources. Any potential contingent liability under these membership agreements cannot be estimated. However, we believe that any potential requirement to make payments under these agreements is remote.

***Pledged Assets***

Pledged assets included in the consolidated balance sheet are summarized in the following table.

| | **March 31, 2009** | **December 31, 2008** |
|---|---|---|
| | **(in millions)** | |
| Interest bearing deposits | **$3,396** | $3,338 |

| | | |
|---|---|---|
| with banks | | |
| Trading assets(1) | **1,000** | 1,085 |
| Securities available for sale(2) | **9,556** | 9,919 |
| Securities held to maturity | **613** | 623 |
| Loans(3) | **8,809** | 3,926 |
| Other assets(4) | **6,032** | 6,872 |
| Total | **$29,406** | $25,763 |

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(1) Trading assets are primarily pledged against liabilities associated with consolidated variable interest entities.

(2) Securities available for sale are primarily pledged against various short-term borrowings.

(3) Loans are primarily private label and other credit card receivables pledged against long-term secured borrowings and residential mortgage loans pledged against long-term borrowings from the Federal Home Loan Bank.

(4) Other assets represent cash on deposit with non-banks related to derivative collateral support agreements.

***19. Fair Value Measurements***

FASB Statement No. 157, "Fair Value Measurements," ("SFAS 157") provides 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. SFAS No. 157 establishes a three-tiered fair value hierarchy with Level 1 representing quoted prices (unadjusted) in active markets for identical assets or liabilities. 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 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.

***Assets and Liabilities Recorded at Fair Value on a Recurring Basis***

The following table presents information about our assets and liabilities measured at fair value on a recurring basis as of March 31, 2009 and December 31, 2008, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value.

| | Fair Value Measurements on a Recurring Basis as of March 31, 2009 | | | | | |
|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Gross Balance | Netting(1) | Net Balance |
| **Assets:** | | | | | | |
| Trading Securities :(2) | | | | | | |
| U.S. Treasury. U.S. Government agencies and sponsored enterprises | $334 | $380 | $- | $714 | $- | $714 |
| Obligations of U.S. states and political subdivisions | - | - | - | - | - | - |
| Residential mortgage-backed securities | - | 362 | 510 | 872 | - | 872 |
| Commercial mortgage-backed securities | - | - | - | - | - | - |
| Collateralized debt obligations | - | 23 | 594 | 617 | - | 617 |
| Other asset-backed securities | - | 38 | 28 | 66 | - | 66 |
| Other domestic debt securities | - | 1,414 | 527 | 1,941 | - | 1,941 |
| Debt Securities issued by foreign entities | - | 165 | 77 | 242 | - | 242 |
| Equity securities | - | 473 | 144 | 617 | - | 617 |
| Precious metals trading | - | 5,552 | - | 5,552 | - | 5,552 |
| Derivatives(3) | 506 | 125,524 | 7,262 | 133,292 | (113,898) | 19,394 |
| Securities available for sale: | | | | | | |
| U.S. Treasury. U.S. Government agencies and sponsored enterprises | 3,969 | 13,335 | - | 17,304 | - | 17,304 |
| Obligations of U.S. states and political subdivisions | - | 710 | 2 | 712 | - | 712 |
| Residential mortgage-backed securities | - | 650 | 333 | 983 | - | 983 |
| Commercial mortgage-backed securities | - | 792 | 5 | 797 | - | 797 |
| Collateralized debt obligations | - | - | - | - | - | - |
| Other asset-backed securities | - | 223 | 256 | 479 | - | 479 |
| Other domestic debt securities | - | 987 | - | 987 | - | 987 |
| Debt Securities issued by foreign entities | - | 1,048 | - | 1,048 | - | 1,048 |
| Equity securities | - | 672 | - | 672 | - | 672 |
| Loans(4) | - | 770 | 155 | 925 | - | 925 |
| Intangible Assets(5) | - | - | 313 | 313 | - | 313 |
| Total Assets | $4,809 | $153,118 | $10,206 | $168,133 | $(113,898) | $54,235 |
| **Liabilities:** | | | | | | |