HSBC HOLDINGS PLC
Form 6-K
August 02, 2010

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 August

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 June 30, 2010

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES 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	**13-2764867**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**
452 Fifth Avenue, New York	**10018**
(Address of principal executive offices)	**(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
o

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
o
No
o

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	Smaller reporting company
o	o	x	o
		(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 Exchange Act). Yes
o
No
x

As of July 30, 2010, there were 712 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 INCOME (LOSS) (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
	(in millions)			
Interest income:				
Loans	**$1,109**	$1,462	**$2,320**	$3,008
Securities	**270**	221	**512**	498
Trading assets	**35**	51	**67**	110
Short-term investments	**29**	22	**57**	46
Other	**12**	13	**23**	24
Total interest income	**1,455**	1,769	**2,979**	3,686
Interest expense:				
Deposits	**152**	267	**315**	580
Short-term borrowings	**22**	15	**43**	34
Long-term debt	**148**	210	**288**	447
Total interest expense	**322**	492	**646**	1,061
Net interest income	**1,133**	1,277	**2,333**	2,625
Provision for credit losses	**456**	1,067	**667**	2,241
Net interest income after provision for credit losses	**677**	210	**1,666**	384
Other revenues:				
Credit card fees	**249**	342	**482**	699
Other fees and commissions	**200**	216	**492**	447
Trust income	**27**	30	**53**	62
Trading revenue (loss)	**128**	153	**332**	(1)
Net other-than-temporary impairment losses(1)	**(13)**	(20)	**(41)**	(58)
Other securities gains, net	**1**	246	**22**	293
Servicing and other fees from HSBC affiliates	**37**	45	**73**	77
Residential mortgage banking revenue (loss)	**(80)**	59	**(117)**	124
Gain (loss) on instruments designated at fair value and related derivatives	**182**	(357)	**228**	(246)
Other income (expense)	**9**	(138)	**167**	(71)
Total other revenues	**740**	576	**1,691**	1,326
Operating expenses:				
Salaries and employee benefits	**280**	302	**547**	593
Support services from HSBC affiliates	**458**	419	**976**	842
Occupancy expense, net	**65**	88	**136**	151
Other expenses	**190**	279	**400**	474
Total operating expenses	**993**	1,088	**2,059**	2,060
Income (loss) before income tax expense (benefit)	**424**	(302)	**1,298**	(350)
Income tax expense (benefit)	**124**	(53)	**444**	(12)

Net income (loss)	**$300**	$(249)	**$854**	$(338)

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(1) During the three and six months ended June 30, 2010, net other-than-temporary impairment ("OTTI") on securities available-for-sale and held to maturity totaling $70 million and $103 million in recoveries, respectively, were recognized which included $83 million and $144 million in recoveries, respectively, recognized in accumulated other comprehensive income ("AOCI"), and $13 million and $41 million, respectively, of OTTI losses recognized in other revenues. During the three and six month periods ended June 30, 2009, $43 million and $159 million, respectively, of gross OTTI losses on securities available-for-sale were recognized, of which $23 million and $101 million, respectively, were recognized in AOCI, net of tax.

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

CONSOLIDATED BALANCE SHEET (UNAUDITED)

	June 30, 2010	**December 31, 2009**
	(in millions)	
Assets		
Cash and due from banks	**$2,719**	$3,159
Interest bearing deposits with banks	**14,076**	20,109
Federal funds sold and securities purchased under agreements to resell	**15,490**	1,046
Trading assets	**29,148**	25,815
Securities available-for-sale (includes $1.3 billion and $1.1 billion at June 30, 2010 and December 31, 2009, respectively, collateralizing long-term debt)(1)	**36,955**	27,806
Securities held to maturity (fair value of $3.9 billion and $2.9 billion at June 30, 2010 and December 31, 2009, respectively, and includes $1.2 billion at June 30, 2010 collateralizing short-term borrowings)(1)	**3,719**	2,762
Loans (includes $3.1 billion at June 30, 2010 and $2.7 billion at December 31, 2009 collateralizing debt)(1)	**73,661**	79,489
Less - allowance for credit losses	**2,950**	3,861
Loans, net	**70,711**	75,628
Loans held for sale (includes $1.5 billion and $1.1 billion designated under fair value option at June 30, 2010 and December 31, 2009, respectively)	**2,567**	2,908
Properties and equipment, net	**519**	533
Intangible assets, net	**350**	484
Goodwill	**2,647**	2,647
Other assets(1)	**7,540**	8,182
Total assets (1)	**$186,441**	$171,079
Liabilities		
Debt:		
Deposits in domestic offices:		
Noninterest bearing	**$21,450**	$20,813
Interest bearing (includes $5.8 billion and $4.2 billion designated under fair value option at June 30, 2010 and December 31, 2009, respectively)	**70,521**	69,894
Deposits in foreign offices:		
Noninterest bearing	**1,479**	1,105
Interest bearing	**28,113**	26,525
Total deposits	**121,563**	118,337
Short-term borrowings(1)	**16,033**	6,512
Long-term debt (includes $4.9 billion and $4.6 billion designated under fair value option at June 30, 2010 and December 31, 2009, respectively, and $2.2 billion and $3.0 billion at June 30, 2010 and December 31, 2009, respectively, collateralized by loans and available-for-sale securities)(1)	**17,751**	18,008
Total debt	**155,347**	142,857
Trading liabilities	**10,877**	8,010
Interest, taxes and other liabilities(1)	**3,817**	5,035
Total liabilities (1)	**170,041**	155,902
Shareholders' equity		
Preferred stock	**1,565**	1,565
Common shareholder's equity:		

Common stock ($5 par; 150,000,000 shares authorized; 712 shares issued and outstanding at June 30, 2010 and December 31, 2009)	**-**	-
Additional paid-in capital	**13,793**	13,795
Retained earnings	**863**	45
Accumulated other comprehensive income (loss)	**179**	(228)
Total common shareholder's equity	**14,835**	13,612
Total shareholders' equity	**16,400**	15,177
Total liabilities and shareholders' equity	**$186,441**	$171,079

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(1) The following table presents information on assets and liabilities related to variable interest entities ("VIEs") that are consolidated in the totals above at June 30, 2010 and December 31, 2009.

	June 30, 2010	**December 31, 2009**
	(in millions)	
Assets:		
Securities available-for-sale	**$1,276**	$1,138
Securities held to maturity	**1,156**	-
Loans, net	**14,953**	15,953
Other assets	**748**	753
Total assets	**$18,133**	$17,844
Liabilities:		
Short-term borrowings	**$3,191**	$-
Long-term debt	**2,242**	3,040
Interest, taxes and other liabilities	**1,117**	1,418
Total liabilities	**$6,550**	$4,458

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

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED)

Six Months Ended June 30,	2010	2009
	(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	**13,795**	11,694
Capital contributions from parent	**-**	2,167
Return of capital on preferred shares issued to CT Financial Services, Inc.	**(3)**	(55)
Employee benefit plans and other	**1**	-
Balance at end of period	**13,793**	13,806
Retained earnings		
Balance at beginning of period	**45**	245
Adjustment to initially apply new guidance for consolidation of VIEs, net of tax	**1**	-
Adjustment to initially apply new guidance for other-than-temporary impairment on debt securities, net of tax	**-**	15
Balance at beginning of period, as adjusted	**46**	260
Net income (loss)	**854**	(338)
Cash dividends declared on preferred stock	**(37)**	(37)
Balance at end of period	**863**	(115)
Accumulated other comprehensive income (loss)		
Balance at beginning of period	**(228)**	(787)
Adjustment to initially apply new guidance for consolidation of VIEs, net of tax	**(246)**	-
Adjustment to initially apply new guidance for other-than-temporary impairment on debt securities, net of tax	**-**	(15)
Balance at beginning of period, as adjusted	**(474)**	(802)
Net change in unrealized gains (losses), net of tax as applicable on:		
Securities available-for-sale, not other-than-temporarily impaired	**533**	134
Other-than-temporarily impaired securities available for sale(1)	**69**	(61)
Other-than-temporarily impaired securities held to maturity(1)	**38**	-
Derivatives classified as cash flow hedges	**13**	33
Unrecognized actuarial gains, transition obligation and prior service costs relating to pension and postretirement benefits, net of tax	**-**	6
Other comprehensive income, net of tax	**653**	112
Balance at end of period	**179**	(690)
Total shareholders' equity	**$16,400**	$14,566
Comprehensive income		
Net income (loss)	**$854**	$(338)
Other comprehensive income, net of tax	**653**	112
Comprehensive income (loss)	**$1,507**	$(226)

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(1) During the six months ended June 30, 2010, net OTTI on securities available-for-sale and held to maturity totaling $103 million in recoveries were recognized which included OTTI losses of $41 million

recognized in other revenues. During the six months ended June 30, 2009, $159 million of gross OTTI losses on securities available-for-sale were recognized, of which $58 million was recognized in other revenues.

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

CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED)

Six Months Ended June 30,	2010	2009
	(in millions)	
Cash flows from operating activities		
Net income (loss)	**$854**	$(338)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	**329**	145
Provision for credit losses	**667**	2,241
Other-than-temporarily impaired available-for-sale and held to maturity securities	**41**	58
Realized gains on securities available for sale	**(22)**	(293)
Net change in other assets and liabilities	**(130)**	1,503
Net change in loans held for sale:		
Originations of loans	**(1,903)**	(3,185)
Sales and collection of loans held for sale	**2,368**	3,204
Tax refund anticipation loans:		
Originations of loans	**(3,082)**	(9,000)
Transfers of loans to HSBC Finance, including premium	**3,086**	9,011
Net change in trading assets and liabilities	**(1,062)**	1,634
LOCOM on receivables held for sale	**(72)**	145
Mark-to-market on financial instruments designated at fair value and related derivatives	**(228)**	246
Net change in fair value of derivatives and hedged items	**13**	(162)
Net cash provided by operating activities	**859**	5,209
Cash flows from investing activities		
Net change in interest bearing deposits with banks	**6,033**	5,916
Net change in federal funds sold and securities purchased under agreements to resell	**(14,444)**	5,598
Securities available-for-sale:		
Purchases of securities available-for-sale	**(24,985)**	(22,771)
Proceeds from sales of securities available-for-sale	**15,449**	14,587
Proceeds from maturities of securities available-for-sale	**1,343**	4,390
Securities held to maturity:		
Purchases of securities held to maturity	**(1,395)**	(152)
Proceeds from maturities of securities held to maturity	**153**	194
Change in loans:		
Originations, net of collections	**20,680**	24,853
Recurring loans purchases from HSBC Finance	**(16,580)**	(18,400)
Cash paid on bulk purchase of loans from HSBC Finance	**-**	(8,821)
Loans sold to third parties	**(138)**	3,961
Net cash used for acquisitions of properties and equipment	**(24)**	(11)
Other, net	**93**	292
Net cash provided by (used in) investing activities	(13,815)	9,636
Cash flows from financing activities		
Net change in deposits	**3,156**	(10,492)
Net change in short-term borrowings	**9,521**	(2,517)
Change in long-term debt:		
Issuance of long-term debt	**1,210**	1,554
Repayment of long-term debt	**(1,499)**	(5,481)
Debt repayment by consolidated VIE	**(136)**	(408)
Debt related to the sale and leaseback of property	**303**	-

Capital contribution from parent	**-**	2,167
Return of capital on preferred shares issued to CT Financial Services, Inc.	**(3)**	(55)
Other increases in capital surplus	**1**	-
Dividends paid	(37)	(37)
Net cash provided by (used in) financing activities	**12,516**	(15,269)
Net change in cash and due from banks	**(440)**	(424)
Cash and due from banks at beginning of period	**3,159**	2,972
Cash and due from banks at end of period	**$2,719**	$2,548
Supplemental disclosure of non-cash flow investing activities		
Trading securities pending settlement	**$(596)**	$580
Transfer of loans to held for sale	**$39**	$289
Assumption of indebtedness from HSBC Finance related to the bulk loan purchase	**$-**	$6,077

The accompanying notes are an integral part of the consolidated financial statement

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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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") 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 predominant 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. and its subsidiaries 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, 2009 (the "2009 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 2010, we adopted new accounting guidance on the consolidation of variable interest entities ("VIEs") and new disclosure requirements relating to fair value measurements. See Note 20, "New Accounting Pronouncements" for further details and related impacts.

2. Trading Assets and Liabilities

Trading assets and liabilities are summarized in the following table.

	June 30, 2010	December 31, 2009
	(in millions)	
Trading assets:		
U.S. Treasury	**$727**	$615
U.S. Government agency	**74**	34
U.S. Government sponsored enterprises(1)	**52**	16
Asset-backed securities	**1,451**	1,815
Corporate and foreign bonds	**2,374**	2,369
Other securities	**78**	491
Precious metals	**16,388**	12,256
Fair value of derivatives	**8,004**	8,219
	$29,148	$25,815
Trading liabilities:		
Securities sold, not yet purchased	**$1,519**	$131
Payables for precious metals	**3,140**	2,556
Fair value of derivatives	**6,218**	5,323
	$10,877	$8,010

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(1) Includes mortgage-backed securities of $6 million and $13 million issued or guaranteed by the Federal National Mortgage Association ("FNMA") and $46 million and $3 million issued or guaranteed by the Federal Home Loan Mortgage Corporation ("FHLMC") at June 30, 2010 and December 31, 2009, respectively.

At June 30, 2010 and December 31, 2009, the fair value of derivatives included in trading assets has been reduced by $2.9 billion and $2.7 billion, respectively, relating to amounts recognized for the obligation to return cash collateral received under master netting agreements with derivative counterparties.

At June 30, 2010 and December 31, 2009, the fair value of derivatives included in trading liabilities has been reduced by $5.2 billion and $7.2 billion, respectively, relating to amounts recognized for the right to reclaim cash collateral paid under master netting agreements with derivative counterparties.

3. Securities

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

June 30, 2010	Amortized Cost	Non-Credit Gain (Loss) Component of OTTI Securities	Unrealized Gains	Unrealized Losses	Fair Value
			(in millions)		
Securities available-for-sale:					
U.S. Treasury	**$9,947**	**$-**	**$486**	**$(5)**	**$10,428**

U.S. Government sponsored enterprises:(1)					
Mortgage-backed securities	**52**	**-**	**1**	**(1)**	**52**
Direct agency obligations	**1,949**	**-**	**104**	**-**	**2,053**
U.S. Government agency issued or guaranteed:					
Mortgage-backed securities	**10,286**	**-**	**325**	**-**	**10,611**
Collateralized mortgage obligations	**6,251**	**-**	**206**	**(1)**	**6,456**
Direct agency obligations	**22**	**-**	**1**	**-**	**23**
Obligations of U.S. states and political subdivisions	**610**	**-**	**20**	**(3)**	**627**
Asset backed securities collateralized by:					
Residential mortgages	**339**	**22**	**-**	**(64)**	**297**
Commercial mortgages	**573**	**-**	**18**	**(6)**	**585**
Home equity	**546**	**(2)**	**-**	**(152)**	**392**
Auto	**21**	**-**	**-**	**-**	**21**
Student loans	**32**	**-**	**-**	**(2)**	**30**
Other	**123**	**-**	**1**	**(17)**	**107**
Corporate and other domestic debt securities(2)	**691**	**-**	**9**	**-**	**700**
Foreign debt securities(2)	**3,094**	**-**	**76**	**-**	**3,170**
Equity securities(3)	**1,399**	**-**	**4**	**-**	**1,403**
Total available-for-sale securities	**$35,935**	**$20**	**$1,251**	**$(251)**	**$36,955**
Securities held to maturity:					
U.S. Government sponsored enterprises:(4)					
Mortgage-backed securities	**$1,793**	**$-**	**$155**	**$-**	**$1,948**
U.S. Government agency issued or guaranteed:					
Mortgage-backed securities	**104**	**-**	**15**	**-**	**119**
Collateralized mortgage obligations	**333**	**-**	**36**	**-**	**369**
Obligations of U.S. states and political subdivisions	**140**	**-**	**5**	**(1)**	**144**
Asset backed securities collateralized by:					
Residential mortgages	**193**	**-**	**2**	**(12)**	**183**
Asset backed securities (predominantly credit card) and other debt securities held by consolidated VIE(5)	**1,364**	**(208)**	**-**	**-**	**1,156**
Total held-to-maturity securities	**$3,927**	**$(208)**	**$213**	**$(13)**	**$3,919**

December 31, 2009	**Amortized Cost**	**Non-Credit Loss Component of OTTI Securities**	**Unrealized Gains**	**Unrealized Losses**	**Fair Value**
			(in millions)		
Securities available-for-sale:					
U.S. Treasury	$7,448	$-	$27	$(73)	$7,402
U.S. Government sponsored enterprises:(1)					
Mortgage-backed securities	59	-	-	(1)	58
Direct agency obligations	1,948	-	5	(65)	1,888

U.S. Government agency issued or guaranteed:					
Mortgage-backed securities	4,081	-	93	(13)	4,161
Collateralized mortgage obligations	6,324	-	107	(7)	6,424
Obligations of U.S. states and political subdivisions	741	-	13	(5)	749
Asset backed securities collateralized by:					
Residential mortgages	1,041	(55)	1	(122)	865
Commercial mortgages	573	-	7	(14)	566
Home equity	620	(29)	-	(219)	372
Auto	65	-	-	(1)	64
Student loans	35	-	-	(5)	30
Other	23	-	1	-	24
Corporate and other domestic debt securities(2)	872	-	7	(15)	864
Foreign debt securities(2)	3,035	-	44	(3)	3,076
Equity securities(3)	1,260	-	3	-	1,263
Total available-for-sale securities	$28,125	$(84)	$308	$(543)	$27,806
Securities held to maturity:					
U.S. Government sponsored enterprises:(4)					
Mortgage-backed securities	$1,854	$-	$103	$(5)	$1,952
U.S. Government agency issued or guaranteed:					
Mortgage-backed securities	113	-	12	-	125
Collateralized mortgage obligations	341	-	25	(2)	364
Obligations of U.S. states and political subdivisions	161	-	6	(1)	166
Asset backed securities collateralized by:					
Residential mortgages	192	-	1	(21)	172
Foreign debt securities	101	-	-	-	101
Total held-to-maturity securities	$2,762	$-	$147	$(29)	$2,880

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(1) Includes securities at amortized cost of $33 million and $38 million issued or guaranteed by FNMA at June 30, 2010 and December 31, 2009, respectively, and $19 million and $21 million issued or guaranteed by FHLMC at June 30, 2010 and December 31, 2009, respectively.

(2) At June 30, 2010 and December 31, 2009, other domestic debt securities included $676 million and $677 million, respectively, of securities at amortized cost fully backed by the Federal Deposit Insurance Corporation ("FDIC") and foreign debt securities consisted of $2.2 billion and $2.7 billion of securities fully backed by foreign governments, respectively.

(3) Includes preferred equity securities at amortized cost issued by FNMA $2 million at June 30, 2010 and December 31, 2009. Balances at June 30, 2010 and December 31, 2009 reflect cumulative other-than-temporary impairment charges of $203 million.

(4) Includes securities at amortized cost of $661 million and $678 million issued or guaranteed by FNMA at June 30, 2010 and December 31, 2009, respectively, and $1.1 billion and $1.2 billion issued and guaranteed by FHLMC at June 30, 2010 and December 31, 2009, respectively.

(5) Relates to securities held by Bryant Park Funding LLC which are consolidated effective January 1, 2010. See Note 16, "Variable Interest Entities" for additional information.

A summary of gross unrealized losses and related fair values as of June 30, 2010 and December 31, 2009, classified as to the length of time the losses have existed follows:

	One Year or Less			Greater Than One Year		
June 30, 2010	**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	-	$-	$-	1	$(5)	$108
U.S. Government sponsored enterprises	3	-	-	14	(1)	11
U.S. Government agency issued or guaranteed	9	(1)	380	5	-	23
Obligations of U.S. states and political subdivisions	10	(1)	38	7	(2)	63
Asset-backed securities	8	(14)	34	75	(227)	817
Corporate and other domestic debt securities	1	-	176	-	-	-
Foreign debt securities	-	-	-	1	-	25
Equity securities	1	-	2	-	-	-
Securities available-for-sale	32	$(16)	$630	103	$(235)	$1,047
Securities held to maturity:						
U.S. Government sponsored enterprises	7	$-	$74	1	$-	$-
U.S. Government agency issued or guaranteed	8	-	3	1	-	-
	19	-	9	14	(1)	23

Obligations of U.S. states and political subdivisions						
Asset-backed securities	-	-	-	12	(12)	137
Securities held to maturity	34	$-	$86	28	$(13)	$160

	One Year or Less			Greater Than One Year		
December 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	16	$(55)	$2,978	1	$(18)	$94
U.S. Government sponsored enterprises	30	(50)	1,441	27	(16)	262
U.S. Government agency issued or guaranteed	85	(19)	1,509	18	(1)	43
Obligations of U.S. states and political subdivisions	26	(3)	166	11	(2)	79
Asset-backed securities	5	(1)	35	109	(360)	1,137
Corporate and other domestic debt securities	3	(8)	83	2	(7)	43
Foreign debt securities	5	(3)	384	1	-	25
Equity securities	2	-	-	-	-	-
Securities available-for-sale	172	$(139)	$6,596	169	$(404)	$1,683
Securities held to maturity:						
U.S. Government sponsored enterprises	10	$(5)	$261	1	$-	$-
U.S. Government agency issued or guaranteed	7	(2)	39	6	-	-
Obligations of U.S. states and political subdivisions	22	(1)	12	12	-	19
Asset-backed securities	1	(1)	6	11	(20)	121
Securities held to maturity	40	$(9)	$318	30	$(20)	$140

Gross unrealized losses within the available-for-sale and held-to-maturity portfolios decreased overall primarily due to a reduction in credit spreads for asset backed securities during the first six months of 2010 as overall market conditions improved. We have reviewed the securities for which there is an unrealized loss in accordance with our accounting policies for other-than-temporary impairment. During the three and six months ended June 30, 2010, 24 and 37 debt securities, respectively, were determined to have either initial other-than-temporary impairment or changes to previous other-than-temporary impairment estimates. We recorded net other-than-temporary impairment recoveries of $70 million and $103 million during the three and six months ended June 30, 2010 on these investments. The credit loss component of the applicable debt securities totaling $13 million and $41 million was recorded as a component of net other-than-temporary impairment losses in the accompanying consolidated statement of income (loss) for the three and six months ended June 30, 2010, respectively, while the remaining non-credit portion representing a net recovery during the six month period of a portion of previously recorded impairment

losses was recognized in other comprehensive income. During the three and six months ended June 30, 2009, eight and seventeen debt securities were determined to be other-than-temporarily impaired. As a result, we recorded other-than-temporary impairment charges of $43 million and $159 million during the three and six months ended June 30, 2009 on these investments. The credit loss component of the applicable debt securities totaling $20 million and $58 million was recorded as a component of net other-than-temporary impairment losses in the accompanying consolidated statement of income (loss) for the three and six months ended June 30, 2009, respectively, while the remaining non-credit portion of the impairment loss was recognized in other comprehensive income.

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 and we neither intend nor expect to be required to sell these securities prior to recovery, even if that equates to holding securities until their individual maturities. However, additional other-than-temporary impairments may occur in future periods if the credit quality of the securities deteriorates.

On-going 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 to indicate that a security with an unrealized loss has suffered other-than-temporary impairment. A debt security is considered impaired if the fair value is less than its amortized cost at the reporting date. If impaired, we assess whether the unrealized loss is other-than-temporary.

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, the credit loss component of an other-than-temporary impairment write-down for debt securities is recorded in earnings while the remaining portion of the impairment loss is recognized, net of tax, in other comprehensive income provided we do not intend to sell the underlying debt security and it is more-likely-than-not that we would 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. As debt securities issued by U.S. Treasury, U.S. Government agencies and government sponsored entities accounted for 78 percent and 72 percent of total available-for-sale and held to maturity securities as of June 30, 2010 and December 31, 2009, respectively, our assessment for credit loss was concentrated on private label asset backed securities. Substantially all of the private label asset-backed securities are supported by residential mortgages, home equity loans or commercial mortgages. Our assessment for credit loss was concentrated on this particular asset class because of the following inherent risk factors:

- The recovery of the U.S. economy remains sluggish;

- The continued deterioration of the U.S. housing markets with increasing delinquencies and foreclosure;

- No real traction in government sponsored programs in loan modifications;

- A lack of refinancing activities within certain segments of the mortgage market, even at the current low interest rate environment, and the re-defaulted rate for refinanced loans;

- The unemployment rate remains high despite recent modest improvement, and consumer confidence remains low;

• The decline in the occupancy rate in commercial properties; and

• The severity and duration of unrealized loss.

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;
• The level of credit enhancement provided by the structure, which includes but is not limited to credit subordination positions, over collateralization, 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.

We use a standard 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, 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.

As of June 30, 2010, available-for-sale debt securities with other-than-temporary impairment for which a portion of the impairment loss remains in accumulated other comprehensive income consisted entirely of asset-backed securities collateralized by residential mortgages or home equity loans. Specific market based assumptions were used to appropriately model and value the credit component of each individual prime, Alt-A and second lien/home equity mortgage backed security due to the diversified geographical, FICO and vintage (2005-2007) characteristics of the underlying loans. This has resulted in a wide range of assumptions across the analyzed securities as presented in the table below. Prime mortgage collateral types comprise approximately 61 percent of the other-than-temporary impairments we have recognized during the first six months of 2010. The assumptions were as follows:

June 30, 2010	Prime	Alt-A	Second liens/Home Equity Mortgages
Cumulative default rate	1-27%	8-34%	12-20%
Loss severity	16-78%	20-80%	100%
Prepayment speeds	1-31%	1-15%	6-8%

The dollar amounts of asset-backed securities for which an other-than-temporary impairment losses were recognized in the six months ended June 30, 2010 are as follows:

	Balance as of June 30, 2010			Impairment Loss Charged to Profit and Loss in 2010
	Amortized Cost	Unrealized Impairment Loss	Fair Value	
	(in millions)			
Available-for-sale:				
Asset-backed securities:				
Residential mortgages	$265	$(53)	$212	$18
Home equity loans	34	-	34	6
Sub-total	299	(53)	246	24
Held-to-maturity:				
Asset backed securities (predominately Credit Card)	255	-	255	3
Total	$554	$(53)	$501	$27

Additionally, there was $14 million of other-than-temporary impairment realized on securities sold in the six months ended June 30, 2010.

The amortized cost and fair value of those asset-backed securities with unrealized loss of more than 12 months for which no other-than-temporary-impairment has been recognized at June 30, 2010 are as follows:

	Balance as of June 30, 2010		
	Amortized Cost	Unrealized Losses for More Than 12 Months	Fair Value
	(in millions)		
Available-for-sale:			
Asset-backed securities:			
Residential mortgages	$301	$(50)	$251
Commercial mortgages	89	(6)	83
Home equity loans	511	(152)	359
Auto loans	7	-	7
Student loans	31	(2)	29
Other	105	(17)	88
Sub-total	1,044	(227)	817
Held-to-maturity classification:			
Asset-backed securities			
Residential mortgages	149	(12)	137
Total	$1,193	$(239)	$954

Although the fair value of a particular security is below its amortized cost for more than 12 months, it does not necessarily result in a credit loss and hence other-than-temporary impairment. The decline in fair value

may be caused by, among other things, the illiquidity of the market. To the extent we do not intend to sell the debt security and it is more-likely-than-not we will not be required to sell the security before the recovery of the amortized cost basis, no other-than-temporary impairment is deemed to have occurred. The fair value of most of the asset-backed securities has recovered significantly as the economy has started to recover from the financial crisis.

The excess of amortized cost over the present value of expected future cash flows recognized during the six months ended June 30, 2010 and 2009 on our other-than-temporarily impaired debt securities, which represents the credit loss associated with these securities, was $41 million and $58 million, respectively. The excess of the present value of expected future cash flows over fair value, representing the non-credit component of the unrealized loss associated with all other-than-temporarily impaired securities, was $188 million as of June 30, 2010. Since we do not have the intention to sell the securities and have sufficient capital and liquidity to hold these securities until a full recovery of the fair value occurs, only the credit loss component is reflected in the consolidated statement of income (loss). The non-credit component of the unrealized loss is recorded, net of taxes, in other comprehensive income.

The following table summarizes the roll-forward of credit losses on debt securities that were other-than-temporarily impaired which have been recognized in income:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(in millions)			
Credit losses at the beginning of the period	**$73**	$43	**$81**	$5
Credit losses related to securities for which an other-than-temporary impairment was not previously recognized	**6**	1	**20**	53
Increase in credit losses for which an other-than-temporary impairment was previously recognized	**7**	19	**21**	5
Reduction of credit losses recognized prior to the sale of securities	**(48)**	-	**(63)**	-
Reductions of credit losses for increases in cash flows expected to be collected that are recognized over the remaining life of the security	**(5)**	-	**(26)**	-
Credit losses at the end of the period	**$33**	$63	**$33**	$63

At June 30, 2010, we held 120 individual asset-backed securities in the available-for-sale portfolio, of which 33 were also wrapped by a monoline insurance company. The asset backed securities backed by a monoline wrap comprised $499 million of the total aggregate fair value of asset-backed securities of $1.4 billion at June 30, 2010. The gross unrealized losses on these securities were $168 million at June 30, 2010. We do not consider the monoline wrap of any non-investment grade monoline insurers and therefore as of June 30, 2010, we only considered the financial guarantee of monoline insurers on securities for purposes of evaluating other-than-temporary impairment with a fair value of $172 million. Four securities wrapped by below investment grade monoline insurance companies with an aggregate fair value of $34 million were deemed to be other-than-temporarily impaired at June 30, 2010.

At December 31, 2009, we held 159 individual asset-backed securities in the available-for-sale portfolio, of which 32 were also wrapped by a monoline insurance company. The asset backed securities backed by a monoline wrap comprised $441 million of the total aggregate fair value of asset-backed securities of $1.9 billion at December 31, 2009. The gross unrealized losses on these securities were $219 million at December 31, 2009. During 2009, three monoline insurers were downgraded to below investment grade. As a result, we did not take into consideration the financial guarantee from two of those monoline insurers and placed only limited reliance of the financial guarantee of the third monoline insurer. As of December 31, 2009, we considered the financial guarantee of monoline insurers on securities with a fair value of $235 million. Four of the securities wrapped by the downgraded monoline insurance companies with an aggregate fair value of $35 million were deemed to be other-than-temporarily impaired at December 31, 2009.

As discussed above, certain asset-backed securities have an embedded financial guarantee provided by monoline insurers. Because the financial guarantee is not a separate and distinct contract from the asset-backed security, they are considered as a single unit of account for fair value measurement and impairment assessment purposes. The monoline insurers are regulated by the insurance commissioners of the relevant states and certain monoline insurers that write the financial guarantee contracts are public companies. In evaluating the extent of our reliance on investment grade monoline insurance companies, consideration is given to our assessment of the creditworthiness of the monoline and other market factors. We perform both a credit as well as a liquidity analyses on the monoline insurers each quarter. Our analysis also compares market-based credit default spreads, when available, to assess the appropriateness of our monoline insurer's creditworthiness. Based on the public information available,

including the regulatory reviews and actions undertaken by the state insurance commissions and the published financial results, we determine the degree of reliance to be placed on the financial guarantee policy in estimating the cash flows to be collected for the purpose of recognizing and measuring impairment loss.

A credit downgrade to non-investment grade is a key but not the only factor in determining the credit risk or the monoline insurer's ability to fulfill its contractual obligation under the financial guarantee arrangement. Although a monoline may have been down-graded by the rating agencies or have been ordered to commute its operations by the insurance commissioners, it may retain the ability and the obligation to continue to pay claims in the near term. We evaluate the short-term liquidity of and the ability to pay claims by the monoline insurers in estimating the amounts of cash flows expected to be collected from specific asset-backed securities for the purpose of assessing and measuring credit loss.

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 June 30, 2010:			
Securities available-for-sale	**$67**	**$(81)**	**$(14)**
Securities held to maturity	**2**	**-**	**2**
	$69	**$(81)**	**$(12)**
Three months ended June 30, 2009:			
Securities available-for-sale	$226	$(48)	$178
Securities held to maturity	-	-	-
	$226	$(48)	$178
Six months ended June 30, 2010:			
Securities available-for-sale	**$99**	**$(115)**	**$(16)**
Securities held to maturity	**-**	**(3)**	**(3)**
	$99	**$(118)**	**$(19)**
Six months ended June 30, 2009:			
Securities available-for-sale	$287	$(100)	$187
Securities held to maturity	-	-	-
	$287	$(100)	$187

The amortized cost and fair values of securities available-for-sale and securities held to maturity at June 30, 2010, are summarized in the table below by contractual maturity. 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 June 30, 2010, 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 securities outstanding at June 30, 2010. Yields on tax-exempt

obligations have been computed on a taxable equivalent basis using applicable statutory tax rates.

Taxable Equivalent Basis as of June 30, 2010	**Within One Year**		**After One But Within Five Years**		**After Five But Within Ten Years**		**After Ten Years**	
	Amount	**Yield**	**Amount**	**Yield**	**Amount**	**Yield**	**Amount**	**Yield**
	(dollars are in millions)							
Available-for-sale:								
U.S. Treasury	$-	-%	$4,249	1.07%	$2,742	3.42%	$2,956	4.38%
U.S. Government sponsored enterprises	-	-	8	3.79	1,319	3.96	674	4.22
U.S. Government agency issued or guaranteed	4	4.45	-	-	251	4.79	16,304	4.13
Obligations of U.S. states and political subdivisions	-	-	-	-	253	4.23	357	4.47
Asset-backed securities	7	2.23	122	5.34	43	1.06	1,482	3.26
Corporate and other domestic debt securities	115	1.53	576	1.57	-	-	-	-
Foreign debt securities	321	1.98	2,738	2.65	35	3.22	-	-
Total amortized cost	$447	1.89%	$7,693	1.74%	$4,643	3.67%	$21,773	4.11%
Total fair value	$449		$7,818		$4,892		$22,393	
Held to maturity:								
U.S. Government sponsored enterprises	$-	-%	$30	7.95%	$2	6.82%	$1,761	6.19%
U.S. Government agency issued or guaranteed	-	-	-	-	6	7.62	431	6.67
Obligations of U.S. states and political subdivisions	9	5.29	29	5.53	15	4.67	87	5.30
Asset-backed securities	-	-	-	-	-	-	193	6.11
Asset backed securities issued by consolidated VIE	352	1.51	550	1.58	254	.35	-	-
Total amortized cost	$361	1.61%	$609	2.07%	$277	.77%	$2,472	6.24%
Total fair value	$361		$613		$278		$2,667	

Investments in FHLB stock and FRB stock of $119 million and $476 million, respectively, were included in other assets at June 30, 2010. Investments in FHLB stock and FRB stock of $152 million and $476 million, respectively, were included in other assets at December 31, 2009.

4. Loans

Loans consisted of the following:

	June 30, 2010	December 31, 2009
	(in millions)	
Commercial loans:		
Construction and other real estate	**$8,574**	$8,858
Other commercial	**20,928**	21,446
Total commercial	**29,502**	30,304
Consumer loans:		
Home equity mortgages	**3,972**	4,164
Other residential mortgages	**13,566**	13,722
Private label cards	**12,747**	15,091
Credit cards	**11,274**	13,048
Auto finance	**1,279**	1,701
Other consumer	**1,321**	1,459
Total consumer	**44,159**	49,185
Total loans	**$73,661**	$79,489

Secured financings of $2.2 billion at June 30, 2010 are secured by $1.5 billion of credit cards and restricted available-for-sale securities of $1.3 billion. Secured financings of $550 million and $2.5 billion at December 31, 2009 were secured by $180 million and $2.6 billion of private label cards and credit cards, respectively, and restricted available-for-sale securities of $417 million and $721 million, respectively.

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 Corporation ("HSBC Finance").

Purchased loans for which at the time of acquisition there was evidence of deterioration in credit quality since origination and for which it was probable that all contractually required payments would not be collected and that the associated line of credit has been closed were recorded upon acquisition at an amount based upon the cash flows expected to be collected ("Purchased Credit-Impaired Loans"). The difference between these expected cash flows and the purchase price represents accretable yield which is amortized to interest income over the life of the loan. At June 30, 2010, the accretable yield has been fully amortized to interest income and there is no remaining difference between the carrying value and the outstanding contractual balances of these Purchased Credit-Impaired Loans for the GM portfolio. At June 30, 2010, we no longer have any receivables from the purchased GM portfolio which are subject to these accounting requirements. The carrying amount of the Purchased Credit-Impaired Loans, net of credit loss reserves at June 30, 2010 totaled $36 million for the UP Portfolio, and is included in credit card loans. The outstanding contractual balance at June 30, 2010 for these receivables was $55 million for the UP Portfolio. The carrying amount of the Purchased Credit-Impaired Loans, net of credit loss reserves at December 31, 2009 totaled $63 million and $52 million for the GM and UP Portfolios, respectively, and is included in credit card loans. The outstanding contractual balances at December 31, 2009 for these receivables were $73 million and $86 million for the GM and UP Portfolios, respectively. Credit loss reserves of $6 million and $18 million as of June 30, 2010 and December 31, 2009, respectively, were held for the acquired GM and UP receivables subject to the accounting requirements for Purchased Credit-Impaired Loans due to a decrease in the expected future cash flows since the acquisition. The following summarizes the change in

accretable yield associated with the Purchased Credit-Impaired Loans:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
	(in millions)			
Accretable yield at beginning of period	**$(22)**	$(80)	**$(29)**	$(95)
Accretable yield amortized to interest income during the period	**4**	14	**11**	29
Reclassification to non-accretable difference	**6**	16	**6**	16
Accretable yield at end of period(1)	**$(12)**	$(50)	**$(12)**	$(50)

(1) At June 30, 2010, the entire remaining accretable yield is related to the UP portfolio. The accretable yield related to the GM portfolio was fully amortized to interest income during the second quarter of 2010.

Troubled Debt Restructurings

The following tables present information about our TDR Loans and the related credit loss reserves for TDR Loans:

	June 30, 2010	December 31, 2009
	(in millions)	
TDR Loans:		
Commercial loans:		
Construction and other real estate	**$200**	$100
Other commercial	**151**	68
Total commercial	**351**	168
Consumer loans:		
Residential mortgages	**299**	173
Private label cards	**237**	216
Credit cards	**176**	102
Auto finance(1)	**46**	52
Total consumer	**758**	543
Total TDR Loans(3)	**$1,109**	$711

	June 30, 2010	December 31, 2009
	(in millions)	
Allowance for credit losses for TDR Loans(2):		
Commercial loans:		
Construction and other real estate	**$41**	$14
Other commercial	**17**	2
Total commercial	**58**	16
Consumer loans:		
Residential mortgages	**51**	34
Private label cards	**83**	51
Credit cards	**62**	24

Auto finance	**12**	11
Total consumer	**208**	120
Total Allowance for credit losses for TDR Loans	**$266**	$136

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(1) The TDR loan balances include $12 million of auto finance loans held for sale at December 31, 2009, for which there are no credit loss reserves as these loans are carried at the lower of cost or fair value.

(2) Included in the allowance for credit losses. The allowance for credit losses for TDR Loans is determined using a discounted cash flow impairment analysis.

(3) Includes balances of $241 million and $65 million at June 30, 2010 and December 31, 2009, respectively which are classified as non-accrual loans.

The following table presents information about average TDR Loan balances and interest income recognized on TDR loans:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
	(in millions)			
Average balance of TDR Loans	**$973**	$420	**$867**	$398
Interest income recognized on TDR Loans	**17**	7	**30**	13

Concentrations of Credit Risk

Our loan portfolio includes the following types of loans:

- High loan-to-value ("LTV") loans - Certain residential mortgages 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.

- Interest-only loans - A loan which allows a customer to pay the interest-only portion of the monthly payment for a period of time which results in lower payments during the initial loan period. However, subsequent events affecting a customer's financial position could affect the ability of customers to repay the loan in the future when the principal payments are required.

- Adjustable rate mortgage ("ARM") loans - A loan which allows us to adjust pricing on the loan in line with market movements. 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.

The following table summarizes the balances of high LTV, interest-only and ARM loans in our loan portfolios, including certain loans held for sale, at June 30, 2010 and December 31, 2009, respectively.

	June 30, 2010	December 31, 2009
	(in billions)	
Residential mortgage loans with high LTV and no mortgage insurance(1)	**$1.1**	$1.2
Interest-only residential mortgage loans	**2.8**	3.3
ARM loans(2)	**7.7**	7.7

(1) Residential mortgage loans with high LTV and no mortgage insurance includes both fixed rate and adjustable rate mortgages. Excludes $149 million and $232 million of sub-prime residential mortgage loans held for sale at June 30, 2010 and December 31, 2009, respectively.

(2) ARM loan balances above exclude $139 million and $209 million of sub-prime residential mortgage loans held for sale at June 30, 2010 and December 31, 2009, respectively. During the remainder of 2010 and during 2011, approximately $49 million and $448 million, respectively, of these ARM loans will experience their first interest rate reset.

Concentrations of first and second liens within the outstanding residential mortgage loan portfolio are summarized in the following table. Amounts in the table exclude closed end first lien loans held for sale of $1.0 billion and $1.4 billion at June 30, 2010 and December 31, 2009, respectively.

	June 30, 2010	December 31, 2009
	(in millions)	
Closed end:		
First lien	**$13,566**	$13,722
Second lien	**500**	570
Revolving:		
Second lien	**3,472**	3,594
Total	**$17,538**	$17,886

5. Allowance for Credit Losses

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	**2009**	**2010**	**2009**
	(in millions)			
Balance at beginning of period	**$3,224**	$3,465	**$3,861**	$2,397
Provision for credit losses	**456**	1,067	**667**	2,241
Charge-offs	**(816)**	(865)	**(1,750)**	(1,479)
Recoveries	**82**	81	**164**	152
Allowance on loans transferred to held for sale	**-**	(8)	**-**	(8)
Allowance related to bulk loan purchase from HSBC Finance	**-**	-	**-**	437
Other	**4**	-	**8**	-
Balance at end of period	**$2,950**	$3,740	**$2,950**	$3,740

6. Loans Held for Sale

Loans held for sale consisted of the following:

	June 30, 2010	December 31, 2009
	(in millions)	
Commercial loans	**$1,554**	$1,126
Consumer loans:		
Residential mortgages	**985**	1,386
Auto finance	**-**	353
Other consumer	**28**	43
Total consumer	**1,013**	1,782
Total loans held for sale	**$2,567**	$2,908

We originate certain 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 commercial loans held for sale at June 30, 2010 and December 31, 2009. The fair value of commercial loans held for sale under this program was $1.0 billion and $1.1 billion at June 30, 2010 and December 31, 2009, respectively, all of which are recorded at fair value as we have elected to designate these loans under fair value option. During the first six months of 2010, the market value of these loans decreased slightly due to wider credit spreads. In 2010, we provided foreign currency denominated loans to a third party which are classified as commercial loans held for sale and for which we elected to apply fair value option. The fair value of these commercial loans was $543 million at June 30, 2010. See Note 10, "Fair Value Option," for additional information.

Residential mortgage loans held for sale include sub-prime residential mortgage loans with a fair value of $478 million and $757 million at June 30, 2010 and December 31, 2009, respectively, which 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 government sponsored enterprises. During the second quarter of 2010, we sold subprime residential mortgage loans with a book value of $215 million to unaffiliated third

parties.

During the first quarter of 2010, auto finance loans held for sale with a carrying value of $353 million were sold to HSBC Finance to facilitate completion of a loan sale to a third party.

Other consumer loans held for sale consist of student loans.

Excluding the commercial loans designated under fair value option discussed above, loans held for sale are recorded at the lower of cost or fair value. While the initial book value of loans held for sale continued to exceed fair value at June 30, 2010, we experienced a decrease in the valuation allowance during the first six months of 2010 due primarily to lower balances and sales. The valuation allowance on loans held for sale was $535 million and $910 million at June 30, 2010 and December 31, 2009, respectively.

Loans held for sale are subject to market risk, liquidity 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 revenue associated with this economic hedging program, which are included in net interest income and trading revenue (loss) in the consolidated statement of income (loss), were losses of $10 million and $16 million during the three and six months ended June 30, 2010, respectively compared to gains of $28 million and $57 million during the three and six months ended June 30, 2009, respectively.

7. Intangible Assets

Intangible assets consisted of the following:

	June 30, 2010	December 31, 2009
	(in millions)	
Mortgage servicing rights	**$326**	$457
Other	**24**	27
Intangible assets	**$350**	$484

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 2009 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:

	June 30, 2010	December 31, 2009
Annualized constant prepayment rate ("CPR")	**23.5%**	14.6%
Constant discount rate	**15.1%**	17.9%
Weighted average life	**3.3 years**	4.8 years

Residential MSRs activity is summarized in the following table:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
	(in millions)			

Fair value of MSRs:				
Beginning balance	**$444**	$313	**$450**	$333
Additions related to loan sales	**10**	37	**26**	65
Changes in fair value due to:				
Change in valuation inputs or assumptions used in the valuation models	**(119)**	88	**(114)**	60
Realization of cash flows	**(18)**	(4)	**(45)**	(24)
Ending balance	**$317**	$434	**$317**	$434

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

	June 30, 2010	December 31, 2009
	(in millions)	
Outstanding principal balances at period end	**$48,803**	$50,390
Custodial balances maintained and included in noninterest bearing deposits at period end	**$945**	$923

Servicing fees collected are included in residential mortgage banking revenue and totaled $30 million and $62 million during the three and six months ended June 30, 2010, respectively. Servicing fees totaled $32 million and $66 million during the three and six months ended June 30, 2009, respectively.

Commercial Mortgage Servicing Rights
Commercial MSRs, which are accounted for using the lower of cost or fair value method, totaled $9 million and $7 million at June 30, 2010 and December 31, 2009.

Other Intangible Assets
Other intangible assets, which result from purchase business combinations, are comprised of favorable lease arrangements of $18 million and $20 million at June 30, 2010 and December 31, 2009, respectively, and customer lists in the amount of $6 million and $7 million at June 30, 2010 and December 31, 2009, respectively.

8. Goodwill

Goodwill was $2.6 billion at June 30, 2010 and December 31, 2009 and includes accumulated impairment losses of $54 million. As a result of the continued focus on economic and credit conditions in the U.S., we performed interim impairment tests of the goodwill associated with our Global Banking and Markets and Private Banking reporting units as of both June 30, 2010 and March 31, 2010. As a result of these tests, the fair value of our Global Banking and Markets and Private Banking reporting units continue to exceed their carrying value, including goodwill. Our goodwill impairment testing however is highly sensitive to certain assumptions and estimates used. If significant deterioration in the economic and credit conditions occur, or changes in the strategy or performance of our business or product offerings occur, an interim impairment test will again be required.

9. Derivative Financial Instruments

In our normal course of business, we enter into derivative contracts for trading, 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 as a qualifying hedge under derivative accounting principles 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. 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 hedge accounting under derivative accounting principles.

Accounting principles for qualifying hedges require 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.

In the tables that follow below, the fair value disclosed does not include swap collateral that we either receive or deposit with our interest rate swap counterparties. Such swap collateral is recorded on our balance sheet at an amount which approximates fair value and is netted on the balance sheet with the fair value amount recognized for derivative instruments.

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 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 of $17 million and $22 million during the three and six months ended June 30, 2010, respectively, compared to net losses of $1.6 million and net gains of $2.5 million during the three and six months ended June 30, 2009, respectively, which are reported in other income (expense) in the consolidated statement of income (loss), which represents the ineffective portion of all fair value hedges. The interest accrual related to the derivative contract is recognized in interest income.

The changes in fair value of the hedged item designated in a qualifying 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 active fair value hedges which increased the carrying value of our debt by $28 million and decreased the carrying value of our debt by $272 million during the six months ended June 30, 2010 and 2009, respectively. We amortized $2.5 million and $4.3 million of basis adjustments related to terminated and/or re-designated fair value hedge relationships during the three and six months ended June 30, 2010, respectively. We amortized $4 million and $7 million of basis adjustments related to terminated and/or re-designated fair value hedge relationships during the three and six months ended June 30, 2009, respectively. The total accumulated unamortized basis adjustment amounted to an increase in the carrying value of our debt of $81 million and $57 million as of June 30, 2010 and December 31, 2009, respectively.

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(1)			Derivative Liabilities(1)		
		Fair Value as of			Fair Value as of	
	Balance Sheet Location	June 30, 2010	December 31, 2009	Balance Sheet Location	June 30, 2010	December 31, 2009
			(in millions)			
Interest rate contracts	Other assets	**$37**	$133	Interest, taxes & other liabilities	**$327**	$15

(1) The derivative assets and derivative liabilities presented above may be eligible for netting 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.

	Location of Gain or (Loss) Recognized in Income on Derivatives	Amount of Gain (Loss) Recognized in Income on Derivatives(1)			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2010	2009	2010	2009
Interest rate contracts	Other income (expense)	**$(473)**	$(75)	**$(486)**	$(86)
Interest rate contracts	Interest income	**20**	(85)	**37**	(70)
Total		**$(453)**	$(160)	**$(449)**	$(156)

(1) The gains and losses associated with the contracts were presented in multiple lines on the consolidated statement of income (loss) 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 income (loss).

	Gain/(Loss) on Derivative		Gain (Loss) on Hedged Items		Gain (Loss) on Derivative		Gain (Loss) on Hedged Items	
	Interest Income (Expense)	Other Income (Expense)	Interest Income (Expense)	Other Income (Expense)	Interest Income (Expense)	Other Income (Expense)	Interest Income (Expense)	Other Income (Expens
	2010				2009			
	(in millions)							
Three Months Ended June 30,								
Interest rate contracts/AFS securities	**$(15)**	**$(473)**	**$88**	**$485**	$(8)	$123	$20	$(12
Interest rate contracts/commercial loans	**-**	**-**	**-**	**-**	-	-	-	
Interest rate contracts/subordinated debt	**35**	**-**	**(22)**	**5**	(77)	(198)	(83)	1
Total	**$20**	**$(473)**	**$66**	**$490**	$(85)	$(75)	$(63)	$
Six Months Ended June 30,								
Interest rate contracts/AFS securities	**$(18)**	**$(513)**	**$132**	**$524**	$(16)	$187	$38	$(18
Interest rate contracts/commercial loans	**(1)**	**1**	**1**	**(1)**	-	(1)	1	
Interest rate contracts/subordinated debt	**56**	**26**	**(63)**	**(15)**	(54)	(272)	(164)	2
Total	**$37**	**$(486)**	**$70**	**$508**	$(70)	$(86)	$(125)	$

Cash Flow Hedges

We own or issue floating rate financial instruments and enter into forecasted transactions that give rise to variability in future cash flows. 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. We also hedge the variability in interest cash flows arising from on-line savings deposits.

Changes in fair value associated with the effective portion of a derivative instrument designated as a qualifying cash flow hedge are recognized initially in accumulated other comprehensive income. 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 accumulated other comprehensive income is recognized in earnings. 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 accumulated other

comprehensive income unless the hedged forecasted transaction is no longer expected to occur, at which time the cumulative gain or loss is released into earnings. As of June 30, 2010, and December 31, 2009, active cash flow hedge relationships extend or mature through January 2012 and June 2010, respectively. During the three and six months ended June 30, 2010, $2 million and $5 million, respectively, of losses related to terminated and/or re-designated cash flow hedge relationships were amortized to earnings from accumulated other comprehensive income. During the next twelve months, we expect to amortize $9 million of remaining losses to earnings resulting from these terminated and/or re-designated cash flow hedges. During the three and six months ended June 30, 2009, $13 million and $30 million, respectively, of losses related to terminated and/or re-designated cash flow hedge relationships were amortized to earnings from accumulated other comprehensive income. The interest accrual related to the derivative contract is recognized in interest income.

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

	Derivative Assets(1)			Derivative Liabilities(1)		
		Fair Value as of			Fair Value as of	
	Balance Sheet Location	June 30, 2010	December 31, 2009	Balance Sheet Location	June 30, 2010	December 31, 2009
			(in millions)			
Interest rate contracts	Other assets	$-	$-	Interest, taxes & other liabilities	$13	$33

(1) The derivative assets and derivative liabilities presented above may be eligible for netting 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.

	Gain (Loss) Recognized in AOCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)	Gain (Loss) Reclassified from AOCI into Income (Effective Portion)		Location of Gain or (Loss) Recognized in Income on the Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Gain (Loss) Reclassed from AOCI into Income (Ineffective Portion)	
	2010	2009		2010	2009		2010	2009
				(In millions)				
Three Months Ended June 30,			Other income			Other income		

Interest rate contracts	**$8**	$64(expense)	**$(2)**	$13(expense)	**$-**	$-
Six Months Ended June 30,		Other income		Other income		
Interest rate contracts	**$15**	$90(expense)	**$(5)**	$30(expense)	**$-**	$7

Trading and Other Derivatives

In addition to risk management, we enter into derivative instruments for trading and market making 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 revenue (loss). 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 hedge accounting are recorded at fair value through profit and loss. 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 June 30, 2010, 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 (expense). In addition, we also from time to time have 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 consolidated balance sheet.

	Derivative Assets(1)			**Derivative Liabilities(1)**		
		Fair Value as of			**Fair Value as of**	
	Balance Sheet Location	**June 30, 2010**	**December 31, 2009**	**Balance Sheet Location**	**June 30, 2010**	**December 31, 2009**
		(in millions)				
Interest rate contracts	Trading assets	**$35,659**	$27,085	Trading Liabilities	**$36,324**	$27,546
Foreign exchange contracts	Trading assets	**14,814**	12,920	Trading Liabilities	**14,520**	14,087
Equity contracts	Trading assets	**1,424**	2,281	Trading Liabilities	**1,375**	2,297
Precious Metals contracts	Trading assets	**734**	918	Trading Liabilities	**1,030**	897
Credit contracts	Trading assets	**17,281**	17,772	Trading Liabilities	**17,160**	17,687
Other	Trading assets	**22**	6	Trading Liabilities	**1**	23
Total		**$69,934**	$60,982		**$70,410**	$62,537

(1) The derivative assets and derivative liabilities presented above may be eligible for netting 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 the fair value of derivative instruments held for other purposes and their location on the balance sheet.

	Derivative Assets(1)			Derivative Liabilities(1)		
		Fair Value as of			Fair Value as of	
	Balance Sheet Location	June 30, 2010	December 31, 2009	Balance Sheet Location	June 30, 2010	December 31, 2009
		(in millions)				
Interest rate contracts	Other assets	**$504**	$229	Interest, taxes & other liabilities	**$5**	$15
Foreign exchange contracts	Other assets	**45**	51	Interest, taxes & other liabilities	**20**	2
Equity contracts	Other assets	**-**	180	Interest, taxes & other liabilities	**185**	16
Credit contracts	Other assets	**5**	15	Interest, taxes & other liabilities	**12**	16
Total		**$554**	$475		**$222**	$49

(1) The derivative assets and derivative liabilities presented above may be eligible for netting 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 income (loss).

	Location of Gain (Loss) Recognized in Income on Derivatives	Amount of Gain (Loss) Recognized in Income on Derivatives			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2010	2009	2010	2009
Interest rate contracts	Trading revenue (loss)	**$35**	$(243)	**$(18)**	$(147)
Foreign exchange contracts	Trading revenue (loss)	**67**	489	**(11)**	571
Equity contracts	Trading revenue (loss)	**(4)**	131	**10**	121
Precious Metals contracts	Trading revenue (loss)	**139**	9	**304**	29
Credit contracts	Trading revenue (loss)	**64**	484	**31**	(151)
Other	Trading revenue (loss)	**17**	(74)	**38**	(32)
Total		**$318**	$796	**$354**	$391

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

	Location of Gain (Loss) Recognized in Income on Derivatives	Amount of Gain (Loss) Recognized in Income on Derivatives			
		Three Months Ended June 30,		Six Months Ended June 30,	
		2010	2009	2010	2009
Interest rate contracts	Other income (expense)	**$344**	$(283)	**$401**	$(420)
Foreign exchange contracts	Other income (expense)	**(14)**	29	**(24)**	35
Equity contracts	Other income (expense)	**(267)**	167	**(125)**	166
Credit contracts	Other income (expense)	**5**	(85)	**(4)**	(94)
Total		**$68**	$(172)	**$248**	$(313)

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 product transactions. As of June 30, 2010, HSBC Bank USA was given credit ratings of AA and Aa3 by S&P and Moody's, respectively, and was given a short-term debt rating of A-1+ and P-1 by S&P and Moody's, respectively. If HSBC Bank USA's credit ratings were to fall below the 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 HSBC Bank USA is downgraded by one or more notches as well as whether the downgrade is in relation to 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 June 30, 2010, is $8.6 billion for which we have posted collateral of $6.8 billion. The aggregate fair value of all derivative instruments with credit-risk-related contingent features that are in a liability position as of December 31, 2009, is $9.3 billion for which we posted collateral of $8.6 billion. Substantially all of the collateral posted is in the form of cash which is reflected in either interest bearing deposits with banks or other assets. See Note 17, "Guarantee Arrangements, Contingencies and Pledged Assets" for further details.

In the event of a credit downgrade, we do not expect HSBC Bank USA's long-term ratings to go below A2 and A+ and the 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 the obligation in hypothetical rating scenarios is not mutually exclusive.

Moody's

Short-Term Ratings	Long-Term Ratings		
	Aa3	A1	A2
	(in millions)		
P-1	$-	$22	$112
P-2	122	125	209

S&P

Short-Term Ratings	Long-Term Ratings		
	AA	AA-	A+
	(in millions)		
A-1+	$-	$168	$220
A-1	126	294	346

We would be required to post $183 million of additional collateral on total return swaps and certain other transactions if HSBC Bank USA is downgraded by S&P and Moody's by two notches on our long term rating accompanied by one notch downgrade in our short term rating.

Notional Value of Derivative Contracts

The following table summarizes the notional values of derivative contracts.

	June 30, 2010	December 31, 2009
	(in billions)	
Interest rate:		
Futures and forwards	**$353.4**	$156.0
Swaps	**1,530.3**	1,221.5
Options written	**179.3**	59.5
Options purchased	**178.3**	66.0
	2,241.3	1,503.0
Foreign Exchange:		
Swaps, futures and forwards	**554.8**	486.2
Options written	**30.4**	43.0
Options purchased	**30.9**	43.1
Spot	**57.0**	39.4
	673.1	611.7
Commodities, equities and precious metals:		
Swaps, futures and forwards	**41.9**	26.4
Options written	**8.2**	10.3
Options purchased	**14.5**	15.3
	64.6	52.0
Credit derivatives	**760.2**	768.5
Total	**$3,739.2**	$2,935.2

10. Fair Value Option

We report our results to HSBC in accordance with its reporting basis, International Financial Reporting Standards ("IFRSs"). We have elected to apply fair value option accounting to selected financial instruments in most cases 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 certain commercial loans including commercial leveraged acquisition finance loans and related unfunded commitments, certain fixed rate long-term debt issuances and hybrid instruments which include all structured notes and structured deposits. Changes in fair value for these assets and liabilities are reported as gain (loss) on instruments designated at fair value and related derivatives in the consolidated statement of income (loss).

Loans
We elected to apply FVO to all commercial leveraged acquisition finance loans held for sale and related 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 June 30, 2010, commercial leveraged acquisition finance loans held for sale and unfunded commitments of $1.0 billion carried at fair value had an aggregate unpaid principal balance of $1.1 billion. As of December 31, 2009, commercial leveraged acquisition finance loans held for sale and unfunded commitments of $1.1 billion carried at fair value had an aggregate unpaid principal balance of $1.3 billion.

In 2010, we provided foreign currency denominated loans to a third party for which we simultaneously entered into a series of derivative transactions to hedge certain risks associated with these loans. We elected to apply fair value option to these loans which allows us to account for them in a manner which is consistent with how the instruments are managed. At June 30, 2010, these commercial foreign currency denominated loans for which we elected fair value option had a fair value of $543 million and an unpaid principal balance of $540 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 income (loss). Because a substantial majority 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 factors. The components of gain (loss) related to loans designated at fair value are summarized in the table below. As of June 30, 2010 and December 31, 2009, no loans for which the fair value option has been elected are 90 days or more past due or on nonaccrual status.

Long-Term Debt (Own Debt Issuances)
We elected to apply FVO for fixed rate long-term debt for which we had applied or otherwise would elect to apply fair value hedge accounting. The election allows us to achieve a similar accounting effect without meeting the rigorous 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 interest rates.

Fixed rate debt accounted for under FVO at June 30, 2010 totaled $1.7 billion and had an aggregate unpaid principal balance of $1.8 billion. Fixed rate debt accounted for under FVO at December 31, 2009 totaled $1.7 billion and had an aggregate unpaid principal balance of $1.8 billion. Interest on the fixed rate debt elected for FVO is recorded as interest expense in the consolidated statement of income (loss). The components of gain (loss) related to long-term debt designated at fair value are summarized in the table below.

Hybrid Instruments

We elected to apply fair value option accounting principles to all of our hybrid instruments, inclusive of structured notes and structured deposits, issued after January 1, 2006. As of June 30, 2010, interest bearing deposits in domestic offices included $5.8 billion of structured deposits accounted for under FVO which had an unpaid principal balance of $5.8 billion. As of December 31, 2009, interest bearing deposits in domestic offices included $4.2 billion of structured deposits accounted for under FVO which had an unpaid principal balance of $4.2 billion. Long-term debt at June 30, 2010 included structured notes of $3.2 billion accounted for under FVO which had an unpaid principal balance of $3.2 billion. Long-term debt at December 31, 2009 included structured notes of $2.9 billion accounted for under FVO which had an unpaid principal balance of $2.7 billion. Interest on this debt is recorded as interest expense in the consolidated statement of income (loss). The components of gain (loss) related to hybrid instruments designated at fair value which reflect the instruments described above are summarized in the table below.

Components of Gain on instruments at fair value and related derivatives
Gain (loss) on instruments designated at fair value and related derivatives 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 (loss) on instruments designated 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 June 30,							
	2010				2009			
	Loans	Long-Term Debt	Hybrid Instruments	Total	Loans	Long-Term Debt	Hybrid Instruments	Total
	(in millions)							
Interest rate component	**$2**	**$(178)**	**$191**	**$15**	$-	$164	$(232)	$(68)
Credit risk component	**(45)**	**123**	**23**	**101**	95	(325)	36	(194)
Total mark-to-market on financial instruments designated at fair value	**(43)**	**(55)**	**214**	**116**	95	(161)	(196)	(262)
Mark-to-market on the related derivatives	**(5)**	**239**	**(188)**	**46**	-	(299)	181	(118)
Net realized gain (losses) on the related derivatives	**-**	**20**	**-**	**20**	-	17	6	23
Gain (loss) on instruments designated at fair value and related derivatives	**$(48)**	**$204**	**$26**	**$182**	$95	$(443)	$(9)	$(357)

	Six Months Ended June 30,							
	2010				2009			
	Loans	Long-Term Debt	Hybrid Instruments	Total	Loans	Long-Term Debt	Hybrid Instruments	Total
	(in millions)							
Interest rate component	**$3**	**$(187)**	**$17**	**$(167)**	$-	$255	$(243)	$12
Credit risk component	**(51)**	**134**	**46**	**129**	130	(214)	64	(20)
Total mark-to-market on financial instruments designated at fair value	**(48)**	**(53)**	**63**	**(38)**	130	41	(179)	(8)
Mark-to-market on the related derivatives	**(1)**	**250**	**(24)**	**225**	-	(467)	257	(210)
Net realized gain (losses) on the related derivatives	**-**	**41**	**-**	**41**	-	31	(59)	(28)
Gain (loss) on instruments designated at fair value and related derivatives	**$(49)**	**$238**	**$39**	**$228**	$130	$(395)	$19	$(246)

11. Income Taxes

The following table presents our effective tax rates.

	2010		2009	
	(dollars are in millions)			
Three Months Ended June 30,				
Statutory federal income tax rate	**$148**	**35.0%**	$(106)	(35.0)%
Increase (decrease) in rate resulting from:				
State and local taxes, net of federal benefit	**5**	**1.2**	4	1.3
Sale of minority stock interest	**-**	**-**	-	-

Valuation allowance on deferred tax assets	**(12)**	**(2.7)**	70	23.1
Tax exempt income	**(5)**	**(1.3)**	(4)	(1.3)
Low income housing and other tax credits	**(22)**	**(5.2)**	(16)	(5.1)
Effects of foreign operations	**14**	**3.3**	-	-
Uncertain tax provision	**(2)**	**(.5)**	1	.4
State rate change effect on net deferred tax assets	**-**	**-**	(1)	(.4)
Other	**(2)**	**(.6)**	(1)	(.9)
Effective tax rate	**$124**	**29.2%**	$(53)	(17.9)%
Six Months Ended June 30,				
Statutory federal income tax rate	**$454**	**35.0%**	$(123)	(35.0)%
Increase (decrease) in rate resulting from:				
State and local taxes, net of federal benefit	**8**	**.6**	9	2.7
Sale of minority stock interest	**-**	**-**	74	21.1
Valuation allowance on deferred tax assets	**1**	**.1**	77	21.9
Tax exempt income	**(7)**	**(.5)**	(8)	(2.2)
Low income housing and other tax credits	**(44)**	**(3.4)**	(31)	(8.8)
Effects of foreign operations	**14**	**1.1**	-	-
Uncertain tax provision	**20**	**1.5**	(1)	(.3)
IRS Audit Effective Settlement	**-**	**-**	(8)	(2.3)
State rate change effect on net deferred tax assets	**-**	**-**	1	.3
Other	**(2)**	**(.2)**	(2)	(.8)
Effective tax rate	**$444**	**34.2%**	$(12)	(3.4)%

The effective tax rate for the three and six months ended June 30, 2010 reflects a substantially higher level of pre-tax income, an increased level of low income housing tax credits, the impact of a planned liquidation of a foreign subsidiary and an adjustment of uncertain tax positions. The effective tax rate for the three and six months ended June 30, 2009 was significantly impacted by the relative level of pre-tax income, the sale of a minority stock interest that was treated as a dividend for tax purposes and the settlement of an IRS audit of our 2004 and 2005 federal income tax returns.

HSBC North America Consolidated Income Taxes

We are included in HSBC North America's consolidated Federal income tax return and in various combined state income tax returns. As such, we have entered into a tax allocation agreement with HSBC North America and its subsidiary entities ("the HNAH Group") included in the consolidated returns which govern the current amount of taxes to be paid or received by the various entities included in the consolidated return filings. As a result, we have looked at the HNAH Group's consolidated deferred tax assets and various sources of taxable income, including the impact of HSBC and HNAH Group tax planning strategies, in reaching conclusions on recoverability of deferred tax assets. Where a valuation allowance is determined to be necessary at the HSBC North America consolidated level, such allowance is allocated to principal subsidiaries within the HNAH Group as described below in a manner that is systematic, rational and consistent with the broad principles of accounting for income taxes.

The HNAH Group evaluates deferred tax assets for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including historical financial performance, projections of future taxable income, future reversals of existing taxable temporary differences, tax planning strategies and any available carryback capacity.

In evaluating the need for a valuation allowance, the HNAH Group estimates future taxable income based on management approved business plans, future capital requirements and ongoing tax planning strategies, including capital support from HSBC necessary as part of such plans and strategies. The HNAH Group has continued to consider the impact of the economic environment on the North American businesses and the expected growth of the deferred tax assets. This evaluation process involves significant management judgment about assumptions that are subject to change from period to period.

In conjunction with the HNAH Group deferred tax evaluation process, based on our forecasts of future taxable income, which include assumptions about the depth and severity of home price depreciation and the U.S. economic downturn, 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 our deferred tax assets. However, 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 from continuing operations 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 remain fully committed and have the capacity and willingness to provide capital as needed to run operations, maintain sufficient regulatory capital, and fund certain tax planning strategies.

Only those tax planning strategies that are both prudent and feasible, and which management has the ability and intent to implement, are incorporated into our analysis and assessment. The primary and most significant strategy is HSBC's commitment to reinvest excess HNAH Group capital to reduce debt funding or otherwise invest in assets to ensure that it is more likely than not that the deferred tax assets will be utilized.

Currently, it has been determined that the HNAH Group's primary tax planning strategy, in combination with other tax planning strategies, provides support for the realization of the net deferred tax assets recorded for the HNAH Group. Such determination is based on HSBC's business forecasts and assessment as to the most efficient and effective deployment of HSBC capital, most importantly including the length of time such capital will need to be maintained in the U.S. for purposes of the tax planning strategy.

Notwithstanding the above, the HNAH Group has valuation allowances against certain specific tax attributes such as foreign tax credits, certain state related deferred tax assets and certain tax loss carryforwards for which the aforementioned tax planning strategies do not provide appropriate support.

HNAH Group valuation allowances are allocated to the principal subsidiaries, including us. The methodology allocates the valuation allowance to the principal subsidiaries based primarily on the entity's relative contribution to the growth of the HSBC North America consolidated deferred tax asset against which the valuation allowance is being recorded.

If future results differ from the HNAH Group's current forecasts or the primary tax planning strategy were to change, a valuation allowance against the remaining net deferred tax assets may need to be established which could have a material adverse effect on our results of operations, financial condition and capital position. The HNAH Group will continue to update its assumptions and forecasts of future taxable income, including relevant tax planning strategies, and assess the need for such incremental valuation allowances.

Absent the capital support from HSBC and implementation of the related tax planning strategies, the HNAH Group, including us, would be required to record a valuation allowance against the remaining deferred tax assets.

HSBC USA Inc. Income Taxes

We recognize deferred tax assets and liabilities for the future tax consequences related to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and for tax credits and state net operating losses. Our net deferred tax assets, net of both deferred tax liabilities and valuation allowances, totaled $1.0 billion and $1.7 billion as of June 30, 2010 and December 31, 2009 respectively. The decrease in net deferred tax assets is primarily due to the reduction in the allowance for credit losses and a decrease in the overall net unrealized losses on available-for-sale securities.

The Internal Revenue Service began its audit of our 2006 and 2007 income tax returns in 2009, with an anticipated completion by the end of 2010. 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.

12. Pensions and Other Post Retirement Benefits

The components of pension expense for the 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 (either the HSBC North America Pension Plan" or the "Plan") which has been allocated to HSBC USA Inc.:

	Three Months Ended June 30,		**Six Months Ended June 30,**	
	2010	**2009**	**2010**	**2009**
	(in millions)			
Service cost - benefits earned during the period	**$5**	$6	**$10**	$13
Interest cost on projected benefit obligation	**16**	19	**33**	37
Expected return on assets	**(16)**	(12)	**(31)**	(25)
Recognized losses	**9**	9	**18**	18
Amortization of prior service cost	**(1)**	-	**(2)**	-
Net periodic pension cost	**$13**	$22	**$28**	$43

Pension expense declined in 2010 due to lower service cost and interest cost as a result of reduced headcount. Also contributing to lower pension expense was the recognition of higher returns on plan assets solely due to higher asset levels.

During the first quarter of 2010, we announced that the Board of Directors of HSBC North America had approved a plan to cease all future benefit accruals for legacy participants under the final average pay formula components of the HSBC North America Pension Plan (the "Plan") effective January 1, 2011. Future accruals to legacy participants under the Plan will thereafter be provided under the cash balance based formula which is now used to calculate benefits for employees hired after December 31, 1996. Furthermore, all future benefit accruals under the Supplemental Retirement Income Plan will also cease effective January 1, 2011.

The aforementioned changes to the Plan have been accounted for as a negative plan amendment and, therefore, the reduction in our share of HSBC North America's projected benefit obligation as a result of this decision will be amortized to net periodic pension cost over the future service periods of the affected employees. The changes to the Supplemental Retirement Income Plan have been accounted for as a plan curtailment, which resulted in no significant immediate recognition of income or expense.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	**2010**	2009
	(in millions)			
Service cost - benefits earned during the period	**$-**	$-	**$-**	$-
Interest cost	**1**	2	**2**	3
Recognized losses	**1**	-	**1**	1
Transition amount amortization	**-**	-	**-**	(1)
Net periodic postretirement benefit cost	**$2**	$2	**$3**	$3

On March 23, 2010, the Patient Protection and Affordable Care Act was enacted and subsequently amended on March 30, 2010 by the Health Care and Education Reconciliation Act of 2010 (collectively referred to as the "Act"). The Act is intended to ensure that more Americans have access to quality, affordable health care insurance with the provisions of the Act being phased in beginning in 2010 and continuing for a number of years. Based on an intensive analysis of the Act, there has been no impact on our consolidated financial statements for the period ended June 30, 2010 as it relates to either our ongoing active employee benefit plans or our postretirement retiree-only medical plans. We have also performed an analysis related to the provisions to be implemented in future periods and based on the Act as currently written, we currently do not believe there will be a material impact to our financial position or results of operation in future periods. Should the provisions of the Act be amended in future periods, the estimated impact to our financial position or results of operations in future periods could change.

13. 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 and include funding arrangements, derivative execution, purchases and sales of receivables, servicing arrangements, information technology and some centralized services, item and statement processing services, banking and other miscellaneous services. The following tables present related party balances and the income and expense generated by related party transactions:

	June 30, 2010	December 31, 2009
	(in millions)	
Assets:		
Cash and due from banks	**$445**	$362
Interest bearing deposits with banks	**223**	198
Federal funds sold and securities purchased under resale agreements	**719**	294
Trading assets(1)	**17,605**	12,811
Loans	**1,134**	1,476
Other	**312**	852
Total assets	**$20,438**	$15,993
Liabilities:		
Deposits	**$12,209**	$9,519
Trading liabilities(1)	**19,776**	16,848
Short-term borrowings	**2,505**	446

Other	**1,719**	1,677
Total liabilities	**$36,209**	$28,490

(1) Trading assets and liabilities exclude the impact of netting which allow the offsetting of amounts relating to certain contracts if certain conditions are met.

	Three Months Ended June 30,	Six Months Ended June 30,

	2010	2009	2010	2009
		(in millions)		
Income/(Expense):				
Interest income	**$30**	$50	**$66**	$97
Interest expense	**(12)**	(5)	**(22)**	(12)
Net interest income	**$18**	$45	**$44**	$85
HSBC affiliate income:				
Fees and commissions:				
HSBC Finance	**$2**	$3	**$4**	$6
HSBC Markets (USA) Inc. ("HMUS")	**7**	7	**10**	9
Other HSBC affiliates	**25**	30	**46**	41
Fees on transfers of refund anticipation loans to HSBC Finance	**-**	1	**4**	11
Other HSBC affiliates income	**3**	4	**9**	10
Total affiliate income	**$37**	$45	**$73**	$77
Support services from HSBC affiliates:				
HSBC Finance	**$(165)**	$(184)	**$(389)**	$(373)
HMUS	**(57)**	(66)	**(144)**	(137)
HSBC Technology & Services (USA) Inc. ("HTSU")	**(191)**	(136)	**(363)**	(247)
Other HSBC affiliates	**(45)**	(33)	**(80)**	(85)
Total support services from HSBC affiliates	**$(458)**	$(419)	**$(976)**	$(842)
Stock based compensation expense with HSBC	**$(11)**	$(15)	**$(22)**	$(33)

Transactions Conducted with HSBC Finance Corporation

In March 2003, HSBC Holdings plc acquired Household International, Inc. ("Household"), the predecessor to HSBC Finance. A stated reason for the acquisition was to bring together HSBC, one of the world's most successful deposit gatherers, with Household, one of the world's largest generators of assets. In connection with the acquisition, HSBC also announced its expectation that funding costs for the Household business would be lower as a result of the financial strength and funding diversity of HSBC. As a result, we work with our affiliates under the oversight of HSBC North America to maximize opportunities and efficiencies in HSBC's operations in the U.S., including the funding efficiencies contemplated at the time of the Household acquisition. The purchases of the private label portfolio, the GM and UP Portfolios and certain auto finance loans from HSBC Finance as discussed in more detail below are indicative of such efficiencies contemplated.

- In January 2009, we purchased the GM and UP Portfolios from HSBC Finance, with an outstanding principal balance of $12.4 billion 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. HSBC Finance continues to service these credit card loans for us for a fee. Information regarding these loans is summarized in the table below.

- 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, at a total net discount of $226 million. Discounts are amortized to interest income over the estimated life of the receivables purchased. In March 2010, we sold

$379 million of auto finance receivables to HSBC Finance including $353 million previously classified as held for sale, a substantial majority of which were comprised of the loans previously purchased from HSBC Finance, who immediately sold them to a third party who also purchased HSBC Finance's auto finance servicing operations. These loans, which were previously serviced by HSBC Finance, are now serviced by this third party provider. Information regarding these loans is summarized in the table below.

- In July 2004, we sold the account relationships associated with $970 million of credit card receivables to HSBC Finance and on a daily basis, we purchase new originations on these credit card receivables. HSBC Finance continues to service these loans for us for a fee. Information regarding these loans is summarized in the table below.

- In December 2004, we purchased the private label credit card receivable portfolio as well as private label commercial and closed end loans from HSBC Finance. HSBC Finance retained the customer account relationships and by agreement we purchase on a daily basis all new private label originations from HSBC Finance. HSBC Finance continues to service these loans for us for a fee. Information regarding these loans is summarized in the table below.

- In 2003 and 2004, we purchased approximately $3.7 billion of residential mortgage loans from HSBC Finance. HSBC Finance continues to service these loans for us for a fee. Information regarding these loans is summarized in the table below.

The following table summarizes the private label card, private label commercial and closed end loans, credit card (including the GM and UP credit card portfolios), auto finance and real estate secured loans serviced for us by HSBC Finance as well as the daily loans purchased during the three and six months ended June 30, 2010 and 2009:

	Private Label		Credit Cards					
	Cards	Commercial and Closed End Loans(1)	General Motors	Union Privilege	Other	Auto Finance	Residential Mortgage	Total
				(in billions)				
Loans serviced by HSBC Finance:								
June 30, 2010	**$12.6**	**$.5**	**$4.5**	**$4.5**	**$1.9**	**$-**	**$1.7**	**$25.7**
December 31, 2009	15.0	.6	5.4	5.3	2.1	2.1	1.8	32.3
Total loans purchased on a daily basis from HSBC Finance during:								
Three months ended June 30, 2010	**3.4**	**-**	**3.5**	**.8**	**1.0**	**-**	**-**	**8.7**
Three months ended June 30, 2009	3.8	-	3.7	1.0	1.1	-	-	9.6
Six months ended June 30, 2010	**6.4**	**-**	**6.6**	**1.5**	**2.0**	**-**	**-**	**16.5**
Six months ended June 30, 2009	7.4	-	7.1	1.8	2.1	-	-	18.4

(1) Private label commercial are included in other commercial loans and private label closed end loans are included in other consumer loans in Note 4, "Loans."

Fees paid for servicing these loan portfolios totaled $159 million and $323 million during the three and six months ended June 30, 2010, respectively, compared to $178 million and $360 million during the three and six months ended June 30, 2009, respectively.

- The GM and UP credit card receivables as well as the private label credit card receivables are purchased from HSBC Finance on a daily basis at a sales price for each type of portfolio determined using a fair value calculated semi-annually in April and October by an independent third party based on the projected future cash flows of the receivables. The projected future cash flows are developed using various assumptions reflecting the historical performance of the receivables and adjusting for key factors such as the anticipated economic and regulatory environment. The independent third party uses these projected future cash flows and a discount rate to determine a range of fair values. We use the mid-point of this range as the sales price.

- In the fourth quarter of 2009, an initiative was begun to streamline the servicing of real estate secured receivables across North America. As a result, certain functions that we had previously performed for our mortgage customers are now being performed by HSBC Finance for all North America mortgage customers, including our mortgage customers. Additionally, we are currently performing certain functions for all North America mortgage customers where these functions had been previously provided separately by each entity. During the three and six months ended June 30, 2010, we paid $1 million and $2 million, respectively, for services we received from HSBC Finance and received $2 million and $4 million, respectively, for services we provided to HSBC Finance.

- 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 and beginning in 2010, the servicing of certain tax refund anticipation loans as more fully discussed below, as well as other operational and administrative support. Fees paid for these services totaled $165 million and $389 million during the three and six months ended June 30, 2010, respectively. During the three and six months ended June 30, 2009, fees paid for these services totaled $184 million and $373 million, respectively.

- Our wholly-owned subsidiaries, HSBC Bank USA and HSBC Trust Company (Delaware), N.A. ("HTCD"), are the originating lenders on behalf of HSBC Finance for a federal income tax refund anticipation loan program for clients of a single third party tax preparer which is managed by HSBC Finance. By agreement, HSBC Bank USA and HTCD process applications, fund and subsequently transfer a portion of these loans to HSBC Finance. Prior to 2010, all loans were transferred to HSBC Finance. Beginning in 2010, we began keeping a portion of these loans on our balance sheet and earn a fee. The loans we keep are transferred to HSBC Finance at par only upon reaching a defined delinquency status. We pay HSBC Finance a fee to service the loans we retain on our balance sheet and to assume the credit risk associated with these receivables. HSBC Bank USA and HTCD originated approximately $9.4 billion and $9.0 billion of loans during the six months ended June 30, 2010 and 2009, respectively, of which $3.1 billion and $9.0 billion, respectively, were transferred to HSBC Finance during these periods. During the six months ended June 30, 2010 and 2009, we received fees of $4 million and $11 million, respectively, for the loans we originated and sold to HSBC Finance. Fees earned on the loans retained on balance sheet and fees paid to HSBC Finance for servicing and assuming the credit risk for these loans totaled $65 million and $58 million, respectively, during the six months ended June 30, 2010.

- 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 June 30, 2010 and December 31, 2009.

- We extended a secured $1.5 billion uncommitted 364 day credit facility to HSBC Finance in December 2009. There were no balances outstanding at June 30, 2010 and December 31, 2009.

- We extended a $1.0 billion committed unsecured 364 day credit facility to HSBC Bank Nevada, a subsidiary of HSBC Finance, in December 2009. There were no balances outstanding at June 30, 2010 and December 31, 2009.

- We service a portfolio of residential mortgage loans owned by HSBC Finance with an outstanding principal balance of $1.3 billion and $1.5 billion at June 30, 2010 and December 31, 2009, respectively. The related servicing fee income was $.3 million and $.6 million during the three and six months ended June 30, 2010, respectively, which is included in residential mortgage banking revenue in the consolidated statement of income (loss). During the three and six months ended June 30, 2009, the related servicing fee income totaled $3 million and $5 million, respectively.

Transactions Conducted with HMUS

- We utilize HSBC Securities (USA) Inc. ("HSI"), a subsidiary of HMUS, 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 $3.3 billion at June 30, 2010 and $4.1 billion at December 31, 2009, of which $1.0 billion was outstanding at both June 30, 2010 and December 31, 2009. Interest income on these loans and lines totaled $5 million and $10 million during the three and six months ended June 30, 2010, respectively, compared to $9 million and $20 million during the three and six months ended June 30, 2009, respectively.

Other Transactions with HSBC Affiliates

- In June 2010, we sold certain securities with a book value of $302 million to HSBC Bank plc and recognized a pre-tax loss of $40 million.

- HSBC North America extended a $1.0 billion senior note to us in August 2009. This is a five year floating rate note which matures on August 28, 2014 with interest due quarterly beginning in November 2009. Interest expense on this note totaled $4 million and $8 million during the three and six month periods ended June 30, 2010, respectively.

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

- We have an unused line of credit with HSBC Bank plc of $2.5 billion at June 30, 2010 and December 31, 2009.

- We have an unused line of credit with HSBC North America Inc. ("HNAI") of $150 million at June 30, 2010 and December 31, 2009.

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We have extended loans and lines of credit to various other HSBC affiliates totaling $1.0 billion at June 30, 2010 and $1.7 billion at December 31, 2009, of which $15 million and $527 million was outstanding at June 30, 2010 and December 31, 2009, respectively. Interest income on these lines totaled $2 million and $5 million during the three and six months ended June 30, 2010, respectively. During the three and six months ended June 30, 2009, interest income on these lines totaled $3 million and $6 million, respectively.

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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. At June 30, 2010 we held $55 million of commercial paper issued by an HSBC affiliate sponsored asset backed commercial paper conduit. At December 31, 2009, no ABCP issued by such conduits was held.

- 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 contracts related to these contracts was approximately $762.3 billion and $673.3 billion at June 30, 2010 and December 31, 2009, respectively. The net credit exposure (defined as the recorded fair value of derivative receivables) related to the contracts was approximately $17.6 billion and $12.8 billion at June 30, 2010 and December 31, 2009, 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. The recorded fair value of derivative assets related to these derivative transactions was approximately $51 million and $70 million at June 30, 2010 and December 31, 2009, respectively.

- Technology and some centralized operational services including human resources, finance, treasury, corporate affairs, compliance, legal, tax and other shared services in North America are centralized within HTSU. Technology related assets and software purchased 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 income (loss).

- Our domestic employees participate in a defined benefit pension plan sponsored by HSBC North America. Additional information regarding pensions is provided in Note 12, "Pension and Other Post-retirement Benefits."

- 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 $11 million and $22 million during the three and six months ended June 30, 2010, respectively. During the three and six months ended June 30, 2009, our share of the expense of these plans totaled $15 million and $33 million, respectively and is included in Salaries and employee benefits in the consolidated statement of income (loss).

- We use HSBC Global Resourcing (UK) Ltd., an HSBC affiliate located outside of the United States, to provide various support services to our operations including among other areas customer service, systems, collection and accounting functions. The expenses related to these services of $7 million and $14 million during the three and six months ended June 30, 2010 are included as a component of Support services from HSBC affiliates in the consolidated statement of income (loss). Billing for these services was processed by HTSU.

14. 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.

	June 30, 2010			December 31, 2009		
	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.	**$19,488**	**10.00%**	**15.35%**	$19,087	10.00%	14.19%
HSBC Bank USA	**19,982**	**10.00**	**15.93**	19,532	10.00	14.81
Tier 1 capital ratio:						
HSBC USA Inc.	**13,691**	**6.00**	**10.79(3)**	12,934	6.00	9.61
HSBC Bank USA	**14,154**	**6.00**	**11.28(3)**	13,354	6.00	10.13
Tier 1 leverage ratio:						
HSBC USA Inc.	**13,691**	**3.00(2)**	**7.34**	12,934	3.00(2)	7.59
HSBC Bank USA	**14,154**	**5.00**	**7.71**	13,354	5.00	8.07
Risk weighted assets:						
HSBC USA Inc.	**126,916(3)**			134,553		
HSBC Bank USA	**125,467(3)**			131,854		

(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.

(3) Effective January 1, 2010, we began consolidating a commercial paper conduit managed by HSBC Bank USA as a result of adopting new guidance related to the consolidation of variable interest entities as more fully discussed in Note 16, "Variable Interest Entities." Since we elected to adopt the transition mechanism for Risk Based Capital Requirements, there is no change to the risk weighted assets or the Tier 1 capital ratios for the first two quarters of 2010. Had we fully transitioned to the Risk Based Capital requirements at June 30, 2010, our risk weighted assets would have been higher by approximately $2.4 billion which would not have had a significant impact to our Tier 1 capital ratio.

We did not receive any capital contributions from our immediate parent, HNAI, during the first half of 2010.

As part of the regulatory approvals with respect to the aforementioned receivable purchases completed in January 2009, 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 may become "low-quality assets," as defined by the Federal Reserve Act. These capital requirements, which require a risk-based capital charge of 100 percent for each "low-quality asset" transferred or arising in the purchased portfolios rather than the eight percent capital charge applied to similar assets that are not part of the transferred portfolios, are applied both for purposes of satisfying the terms of the commitments and for purposes of measuring and reporting HSBC Bank USA's risk-based capital and related ratios. This treatment applies as long as the low-quality assets are owned by an insured bank. During the first half of 2010, HSBC Bank USA sold low-quality auto finance loans with a net book value of approximately $178 million to a non-bank subsidiary of HSBC USA Inc. to reduce the capital requirement associated with these assets. In 2009, the net book value of such sales totaled $455 million. Capital ratios and amounts at June 30, 2010 and December 31, 2009 in the table above reflect this reporting.

Regulatory guidelines impose certain restrictions that may limit the inclusion of deferred tax assets in the computation of regulatory capital. Continued losses, including losses associated with FVO elections, coupled with bad debt provisions that exceed charge-offs are creating additional deferred tax assets, which could, from time to time, result in such exclusion. We closely monitor the deferred tax assets for potential limitations or exclusions. At June 30, 2010 and December 31, 2009, deferred tax assets of $292 million and $331 million, respectively, were excluded in the computation of regulatory capital.

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.

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. These inter-segment transactions are accounted for as if they were with third parties.

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. We continue to monitor capital adequacy, establish dividend policy and report to regulatory agencies on a U.S. GAAP legal entity basis.

Reconciliation of our IFRS Management Basis segment results to the U.S. GAAP consolidated totals are as follows:

	IFRSs Consolidated Amounts									
	PFS	CF	CMB	Global Banking and Markets	PB	Other	Adjustments/ Reconciling Items	Total	(2) IFRSs Adjustments	(IF Reclass
							(in millions)			
Three months ended June 30, 2010										
Net interest income	$238	$484	$176	$143	$45	$(1)	$(5)	$1,080	$(13)	
Other operating income	17	36	96	303	35	216	5	708	(114)	
Total operating income (loss)	255	520	272	446	80	215	-	1,788	(127)	
Loan impairment charges	29	355	47	(72)	-	(2)	-	357	76	
	226	165	225	518	80	217	-	1,431	(203)	
	316	28	171	198	62	13	-	788	16	

Operating expenses(1)									
Profit (loss) before tax expense	**$(90)**	**$137**	**$54**	**$320**	**$18**	**$204**	**$-**	**$643**	$(219)
Balances at end of period:									
Total assets	**$20,903**	**$26,199**	**$15,752**	**$182,683**	**$5,051**	**$18**	**$-**	**$250,606**	**$(63,964)**
Total loans, net	**16,464**	**23,956**	**14,091**	**33,934**	**4,233**	**-**	**-**	**92,678**	**(1,909)**
Goodwill	**876**	**-**	**368**	**497**	**326**	**-**	**-**	**2,067**	**580**
Total deposits	**47,991**	**47**	**23,120**	**35,253**	**11,324**	**-**	**-**	**117,735**	**(3,073)**
Three months ended June 30, 2009									
Net interest income	$240	$520	$180	$222	$46	$(2)	$(3)	$1,203	$3
Other operating income	43	84	82	288	29	(498)	3	31	449
Total operating income (loss)	283	604	262	510	75	(500)	-	1,234	452
Loan impairment charges	172	477	90	197	7	-	-	943	169
	111	127	172	313	68	(500)	-	291	283
Operating expenses(1)	335	37	158	236	63	38	-	867	9
Profit (loss) before tax expense	$(224)	$90	$14	$77	$5	$(538)	$-	$(576)	$274
Balances at end of period:									
Total assets	$22,338	$31,837	$17,954	$172,779	$5,830	$104	$-	$250,842	$(82,409)
Total loans, net	17,572	29,547	16,499	26,171	4,617	-	-	94,406	(3,802)
Goodwill	876	-	368	497	326	-	-	2,067	580
Total deposits	47,632	46	21,639	28,429	10,667	-	-	108,413	(3,620)
Six months ended June 30, 2010									
Net interest income	**$479**	**$1,007**	**$364**	**$285**	**$91**	**$(10)**	**$(13)**	**$2,203**	**$46**
	63	**53**	**249**	**741**	**69**	**232**	**13**	**1,420**	(87

Other operating income									)
Total operating income (loss)	**542**	**1,060**	**613**	**1,026**	**160**	**222**	**-**	**3,623**	**(41)**
Loan impairment charges	**26**	**565**	**48**	**(148)**	**(11)**	**-**	**-**	**480**	**178**
	516	**495**	**565**	**1,174**	**171**	**222**	**-**	**3,143**	**(219)**
Operating expenses(1)	**587**	**55**	**321**	**407**	**117**	**30**	**-**	**1,517**	**109**
Profit (loss) before tax expense	**$(71)**	**$440**	**$244**	**$767**	**$54**	**$192**	**$-**	**$1,626**	**$(328)**
Six months ended June 30, 2009									
Net interest income	$427	$1,049	$356	$454	$88	$-	$(14)	$2,360	$106
Other operating income	83	165	163	509	62	(343)	14	653	548
Total operating income (loss)	510	1,214	519	963	150	(343)	-	3,013	654
Loan impairment charges	372	1,031	171	426	4	-	-	2,004	382
	138	183	348	537	146	(343)	-	1,009	272
Operating expenses(1)	630	51	312	435	122	52	-	1,602	29
Profit (loss) before tax expense	$(492)	$132	$36	$102	$24	$(395)	$-	$(593)	$243

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

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

(3) 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

Effective interest rate
- The calculation of effective interest rates under IFRS 39, "Financial Instruments: Recognition and Measurement ("IAS 39"), requires an estimate of "all fees and points paid or recovered between parties to the contract" that are an integral part of the effective interest rate be included. U.S. GAAP generally prohibits recognition of interest income to the extent the net interest in the loan would increase to an amount greater than the amount at which the borrower could settle the obligation. Under U.S. GAAP, prepayment penalties are generally recognized as received. U.S. GAAP also includes interest income on loans held for sale which is included in other revenues for IFRSs.

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 estimated 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.

Derivative interest expense
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 profit at inception 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, 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, and classified in other assets.

Loans held for sale
- IFRSs requires loans originated with the intent to sell to be classified 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 related to receivables held for sale are reported in net interest income or trading revenue. Under U.S. GAAP, the income 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, "Financial Instruments: Recognition and Measurement" ("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 amortized cost or fair value. Under U.S. GAAP, the initial component of the lower of cost or fair value adjustment related to credit risk is recorded in the consolidated statement of income (loss) as provision for credit losses while the component related to interest rates and liquidity factors is reported in the consolidated statement of income (loss) in other revenues (losses).

Reclassification of financial assets -
Certain securities were reclassified from "trading assets" to "loans and receivables" under IFRSs as of July 1, 2008 pursuant to an amendment to IAS 39 and are no longer marked to market. 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.

Additionally, 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 reclassified to "loans and advances" as of July 1, 2008 pursuant to the IAS 39 amendment discussed above. Under U.S. GAAP, these loans are classified as "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. Subsequent adjustments to fair value are generally reflected in current period earnings.

Securities -
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 accumulated other comprehensive income provided we have concluded we do not intend to sell the security and it is more-likely-than-not that we will not have to sell the security prior to recovery. Under IFRSs, there is no bifurcation of other-than temporary impairment and the entire decline in value is recognized in earnings. Also under IFRSs, recoveries in other-than-temporary impairment related to improvement in the underlying credit characteristics of the investment are recognized immediately in earnings while under U.S. GAAP, they are amortized to income over the remaining life of the security. There are also other less significant differences in measuring other-than-temporary impairment under IFRSs versus U.S. GAAP.
Under IFRSs, securities include HSBC shares held for stock plans at fair value. These shares held for stock plans 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. There is no similar requirement under 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.

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

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." Furthermore, in 2010, changes to future accruals for legacy participants under the HSBC North America Pension Plan were accounted for as a plan curtailment under IFRSs, which resulted in immediate income recognition. Under US GAAP, these changes were considered to be a negative plan amendment which resulted in no immediate income recognition.

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.

Assets

Customer loans (Loans)
- On an IFRSs basis loans designated as held for sale at the time of origination and accrued interest are classified as trading assets. However, the accounting requirements governing when receivables previously held for investment are transferred to a held for sale category are more stringent under IFRSs than under U.S. GAAP.

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.

16. Variable Interest Entities

On January 1, 2010, we adopted new guidance issued by the Financial Accounting Standards Board in June 2009 which amends the accounting for the consolidation of variable interest entities ("VIEs"). The new guidance changed the approach for determining the primary beneficiary of a VIE from a quantitative approach focusing on risk and reward to a qualitative approach focusing on (a) the power to direct the activities of the VIE and (b) the obligation to absorb losses and/or the right to receive benefits that could be significant to the VIE. The adoption of the new guidance has resulted in the consolidation of one commercial paper conduit managed by HSBC Bank USA as discussed more fully below. The impact of consolidating this entity beginning on January 1, 2010 resulted in an increase to our assets and liabilities of $3.2 billion and $3.5 billion, respectively, which resulted in a $1 million increase to the opening balance of retained earnings in common shareholder's equity and a $246 million reduction to the opening balance of other comprehensive income in common shareholder's equity. Since we elected to adopt the transition mechanism for Risk Based Capital requirements, there was no change to the way we calculate risk weighted assets against the Bryant Park facility for the first half of 2010 and as a result, there is also no impact to our Tier 1 capital ratios at June 30, 2010. Had we fully transitioned to the Risk Based Capital requirements at June 30, 2010, our risk weighted assets would have been higher by approximately $2.4 billion which would not have had a significant impact to our Tier 1 capital ratios. See asset-backed commercial paper conduit portion of the table "Consolidated VIE's" presented below for additional details of the assets and liabilities relating to this newly consolidated entity.

In the ordinary course of business, we have organized 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, risk characteristics and business activities of the SPEs. Special purpose entities can be a VIE, which is an entity that lacks sufficient equity investment at risk to finance its activities without additional subordinated financial support or, as a group, the holders of the equity investment at risk lack either a) the power to direct the activities of an entity that most significantly impacts the entity's economic performance; b) the obligation to absorb the expected losses of the entity, the right to receive the expected residual returns of the entity, or both.

Variable Interest Entities

We consolidate VIEs in which we hold a controlling financial interest as evidenced by the power to direct the activities of a VIE that most significantly impact its economic performance and the obligation to absorb losses of, or the right to receive benefits from, the VIE that could be potentially significant to the VIE and therefore are deemed to be the primary beneficiary. We take into account our entire involvement in a VIE (explicit or implicit) in identifying variable interests 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. 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; (iv) design, organize and structure the transaction; and (v) retain a financial or servicing interest in the VIE.

We are required to evaluate whether to consolidate a VIE when we first become involved and on an ongoing basis. In almost all 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.

Consolidated VIEs

The following table summarizes the assets and liabilities of our consolidated VIEs as of June 30, 2010 and December 31, 2009:

	June 30, 2010		December 31, 2009	
	Consolidated Assets	Consolidated Liabilities	Consolidated Assets	Consolidated Liabilities
	(in millions)			
Asset-backed commercial paper conduit:				
Held to maturity securities	**$1,156**	**$-**	$-	$-
Loans	**1,598**	**-**	-	-
Other assets	**2**	**-**	-	-
Short-term borrowings	**-**	**3,191**	-	-
Other liabilities	**-**	**2**	-	-
Subtotal	**2,756**	**3,193**	-	-
Securitization vehicles:				
Loans	**13,355**	**-**	15,953	-
Available-for-sale securities	**1,276**	**-**	1,138	-
Other assets	**207**	**-**	168	-
Long-term debt	**-**	**2,187**	-	2,985
Other liabilities	**-**	**1,009**	-	1,283
Subtotal	**14,838**	**3,196**	17,259	4,268
Low income housing limited liability partnership:				
Other assets	**539**	**-**	585	-
Long term debt	**-**	**55**	-	55
Other liabilities	**-**	**106**	-	135
Subtotal	**539**	**161**	585	190
Total	**$18,133**	**$6,550**	$17,844	$4,458

Asset-Backed Commercial Paper Conduit

As discussed in more detail below, 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 third parties. These conduits support the financing needs of customers by facilitating the customers' access to commercial paper markets.

One of these commercial paper conduits otherwise known as Bryant Park Funding LLC ("Bryant Park"), was sponsored, organized and managed to facilitate clients in securing asset-backed financing collateralized by diverse pools of loan and lease receivables or investment securities. Bryant Park funds the purchase of the eligible assets by issuing short-term commercial paper notes to third party investors. One of our affiliates provides a program wide letter of credit enhancement ("PWE") to support the creditworthiness of the commercial paper issued up to a certain amount. We also entered into a liquidity asset purchase agreement ("LAPA"), to provide liquidity support for the commercial paper notes issued to fund the asset purchases. Prior to the adoption of the new VIE consolidation guidance in 2010, determination of the primary beneficiary was predominantly based on a quantitative risk and reward analysis and, because our affiliate held the PWE that absorbs (receives) a majority of the expected losses (residual returns), the affiliate was considered to be the primary beneficiary. However, under the new guidance adopted January 1, 2010, we are considered to be the primary beneficiary because we have the power to direct the activities of the conduit that most significantly impact its economic performance including a) determining which eligible assets to acquire; b) risk managing the portfolio held; and c) managing the refinancing of commercial paper.

The liquidity facility we provide in the form of a LAPA can be drawn upon by the conduit in the event it cannot issue commercial paper notes or does not have sufficient funds available to pay maturing commercial paper. Under the LAPA, we are obligated, subject to certain conditions, to purchase the eligible assets previously funded for an amount not to exceed the face value of the commercial paper in order to provide the conduit with funds to repay the maturing notes. As such, we are exposed to the market risk and the credit risk of the underlying assets held by Bryant Park only to the extent the liquidity facility is drawn.

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 certain private label and other credit card receivables to these trusts which in turn issue debt instruments collateralized by the transferred receivables. As our affiliate is the servicer of the assets of these trusts we performed a detailed analysis and determined that we retain the benefits and risks and are the primary beneficiary of the trusts and, as a result, consolidate them.

At June 30, 2010 and December 31, 2009, the consolidated assets of these trusts were $14.8 billion and $17.3 billion, respectively. Debt securities issued by these VIEs are reported as secured financings in long-term debt. Certain assets of the consolidated VIEs serve as collateral for the obligations of the VIEs. The holders of the debt securities issued by these vehicles have no recourse to our general credit.

Low Income Housing Limited Liability Partnership

During the third quarter of 2009, all low income housing investments held by us were transferred to a Limited Liability Partnership ("LLP") in exchange for debt and equity while a non-affiliated third party invested cash for an equity interest that is mandatorily redeemable at a future date. The LLP was created in order to ensure the utilization of future tax benefits from these low income housing tax projects. The LLP was deemed to be a VIE as it does not have sufficient equity investment at risk to finance its activities. Upon entering into this transaction, we concluded that we are the primary beneficiary of the LLP due to the nature of our continuing involvement and, as a result, consolidate the LLP and report the equity interest issued to the third party investor as other liabilities and the consolidated assets of the LLP in other assets in our consolidated financial statements. The investments held by the LLP represent equity investments in the underlying low income housing partnerships for which the LLP applies equity-method accounting. The LLP does not consolidate the underlying partnerships because it does not have the power to direct the activities of the partnerships that most significantly impact the economic performance of the partnerships.

Unconsolidated VIEs

We also have variable interests with other VIEs that were not consolidated at June 30, 2010 and December 31, 2009 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 June 30, 2010 and December 31, 2009:

	June 30, 2010				**December 31, 2009**	
	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	**$-**	**$-**	**$13,851**	**$1,424**	$10,485	$5,050
	178	**122**	**7,933**	**960**	7,890	569

Structured note vehicles						
Total	**$178**	**$122**	**$21,784**	**$2,384**	$18,375	$5,619

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
Separately from the facility discussed above, 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 those 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, other than Bryant Park as discussed above. Credit risk related to the liquidity facilities provided is managed by subjecting them to our normal underwriting and risk management processes. The $1.4 billion 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. The reduction in amounts outstanding since December 31, 2009 reflects the consolidation of Bryant Park effective January 1, 2010, as more fully described above.

Structured Note Vehicles
Our involvement in structured note vehicles includes 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 June 30, 2010, we recorded approximately $169 million of trading assets and $196 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, 2009, we recorded

approximately $169 million of trading assets and $205 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 our 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 are 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.

Beneficial Interests Issued by Third-party Sponsored Securitization Entities
We hold certain beneficial interests issued by third-party sponsored securitization entities which may be considered as variable interest entities. The investments are transacted at arm's-length and decisions to invest are based on credit analysis on underlying collateral assets or the issuer. We are a passive investor in these issuers and do not have the power to direct the activities of these issuers. As such, we do not consolidate these securitization entities. Additionally, we do not have other involvements in servicing or managing the collateral assets or provide financial or liquidity support to these issuers that potentially give rise to risk of loss exposure. These investments are an integral part of the disclosure in Note 3, "Securities" and Note 18, "Fair Value Measurements" and therefore, were not disclosed in this Note to avoid redundancy.

17. Guarantee Arrangements, Contingencies and Pledged Assets

Guarantee Arrangements
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 June 30, 2010 and December 31, 2009. Following the table is a description of the various arrangements.

	June 30, 2010		**December 31, 2009**	
	Carrying Value	**Notional/Maximum Exposure to Loss**	**Carrying Value**	**Notional/Maximum Exposure to Loss**
		(in millions)		
Credit derivatives(1)(2)	**$(8,076)**	**$381,699**	$(5,751)	$387,225
Financial standby letters of credit, net of participations(3)(4)	**-**	**4,381**	-	4,545
Performance (non-financial) guarantees	**-**	**2,994**	-	3,100
Liquidity asset purchase agreements(4)		**1,424**	-	6,791
Total	**$(8,076)**	**$390,498**	$(5,751)	$401,661

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(1) Includes $51.9 billion and $57.3 billion issued for the benefit of HSBC affiliates at June 30, 2010 and December 31, 2009, respectively.

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

(3) Includes $745 million and $774 million issued for the benefit of HSBC affiliates at June 30, 2010 and December 31, 2009, respectively.

(4) 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.

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. 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.

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 June 30, 2010 and December 31, 2009:

	June 30, 2010		December 31, 2009	
	Carrying (Fair) Value	**Notional**	**Carrying (Fair) Value**	**Notional**
	(in millions)			
Sell-protection credit derivative positions	**$(8,076)**	**$(381,699)**	$(5,751)	$(387,225)
Buy-protection credit derivative positions	**8,986**	**378,514**	6,693	381,258
Net position(1)	**$910**	**$(3,185)**	$942	$(5,967)

(1) Positions are presented net in the table above to provide a complete analysis of our risk exposure and depict the way we manage our credit derivative portfolio. The offset of the sell-protection credit derivatives against the buy-protection credit derivatives may not be legally binding in the absence of master netting agreements with the same counterparty.

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 June 30, 2010, the total amount of outstanding financial standby letters of credit (net of participations) and performance guarantees were $4.4 billion and $3.0 billion, respectively. As of December 31, 2009, the total amount of outstanding financial standby letters of credit (net of participations) and performance guarantees were $4.5 billion and $3.1 billion, 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 $53 million and $48 million at June 30, 2010 and December 31, 2009, respectively. Also included in other liabilities is an allowance for credit losses on unfunded standby letters of credit of $29 million and $27 million at June 30, 2010 and December 31, 2009.

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 June 30, 2010 as an indicative proxy of payment risk:

		Credit Ratings of the Obligors or the Transactions		
Notional/Contractual Amounts	Average Life (in years)	Investment Grade	Non-Investment Grade	Total
		(dollars are in millions)		
Sell-protection Credit Derivatives(1)				
Single name CDS	3.2	$152,487	$70,722	$223,209
Structured CDS	3.0	75,262	5,338	80,600
Index credit derivatives	3.8	63,546	1,930	65,476
Total return swaps	8.6	12,094	320	12,414
Subtotal		303,389	78,310	381,699
Standby Letters of Credit(2)	1.1	7,080	295	7,375
Total		$310,469	$78,605	$389,074

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

(2) 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 HSBC's 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 agency benchmarks, where possible, at the time of formal review and regularly monitor whether our risk ratings are comparable to the external ratings benchmark data.

A non-investment grade rating of a referenced obligor has a negative impact to the fair value of the credit derivative and increases the likelihood that we will be required to perform under the credit derivative contract. We employ market-based parameters and, where possible, use the observable credit spreads of the referenced obligors as measurement inputs in determining the fair value of the credit derivatives. We believe that such market parameters are more indicative of the current status of payment/performance risk than external ratings by the rating agencies which may not be forward-looking in nature and, as a result, lag behind those market-based indicators.

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 June 30, 2010 and December 31, 2009, we have issued $1.4 billion and $6.8 billion, respectively, of liquidity facilities to provide liquidity support to the commercial paper issued by various conduits. The decline since December 31, 2009 reflects our consolidation of the Bryant Park commercial paper conduit effective January 1, 2010. See Note 16, "Variable Interest Entities" for further information.

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 June 30, 2010 and December 31, 2009. 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 ownership 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. Our estimated liability for obligations arising from the breach of representations and warranties was $205 million and $66 million as of June 30, 2010 and December 31, 2009, respectively. The increase from year-end was due to an increase in the reserve for potential repurchase liability exposures related primarily to previously originated mortgages through broker channels.

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. 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 July 2009, Visa exercised its rights to sell shares of existing Class B shareholders in order to increase the escrow account and announced that it had deposited an additional $700 million into the escrow account. As a result, we re-evaluated the contingent liability we have recorded relating to this litigation and reduced our liability by $9 million during 2009. In May 2010, Visa funded an additional $500 million into the escrow account and we reduced our liability by an additional $6 million in the second quarter of 2010. At June 30, 2010, the contingent liability recorded was $19 million.

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.

Contingencies
In connection with the resolution of ongoing regulatory and governmental examinations and inquiries, it is likely we will be subject to some form of formal enforcement action concerning processes or governance relating to the subject areas, which may include a written agreement or a cease and desist order requiring additional remedial measures and further enhancements to our Bank Secrecy Act and Anti-Money Laundering policies and procedures. If we are found to have violated the law, relevant authorities have the power to impose civil money penalties, fines and other financial penalties. We are unable at this time to determine the terms on which these matters will be resolved, the timing of any formal enforcement action, or the amount of fines or penalties, if any, that may be imposed by the regulators or agencies, and, as a result, no accrual for such costs has been recorded at June 30, 2010.

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

	June 30, 2010	**December 31, 2009**
	(in millions)	
Interest bearing deposits with banks	**$1,431**	$1,496
Trading assets(1)	**588**	708
Securities available- for-sale(2)	**14,964**	11,416
Securities held to maturity(3)	**1,504**	457
Loans(4)	**4,566**	3,933
Other assets(5)	**4,890**	6,459
Total	**$27,943**	$24,469

(1) Trading assets are primarily pledged against liabilities associated with consolidated variable interest entities.
Securities available-for-sale are primarily pledged against various short-term and long-term borrowings.

(2)

(3) Securities held to maturity include federal home loan bank collateral at June 30, 2010 and December 31, 2009, as well as the investment securities of a consolidated asset backed commercial paper conduit at June 30, 2010 that collateralize the conduit's outstanding commercial paper.

(4) Loans are primarily private label card 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. At June 30, 2010 loans also include the loans of a consolidated asset backed commercial paper conduit that collateralize the conduit's outstanding commercial paper.

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

18. Fair Value Measurements

Accounting principles related to fair value measurements provide a framework for measuring fair value and focuses on an exit price in the principal (or alternatively, the most advantageous) market accessible in an orderly transaction between willing market participants (the "Fair Value Framework"). The Fair Value Framework establishes a three-tiered fair value hierarchy with Level 1 representing quoted prices (unadjusted) in active markets for identical assets or liabilities. Fair values determined by Level 2 inputs are inputs that are observable for the identical 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 disorderly, 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. Transfers between leveling categories are recognized at the end of each reporting period.

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 June 30, 2010 and December 31, 2009, 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 June 30, 2010					
	Level 1	Level 2	Level 3	Gross Balance	Netting(1)	Net Balance
			(in millions)			
Assets:						
Trading Securities:						
U.S. Treasury. U.S. Government agencies and sponsored enterprises	**$727**	**$126**	**$-**	**$853**	**$-**	**$853**
Collateralized debt obligations	**-**	**-**	**791**	**791**	**-**	**791**
Asset-backed securities:						
Residential mortgages	**-**	**45**	**560**	**605**	**-**	**605**
Home equity	**-**	**-**	**32**	**32**	**-**	**32**
Student loans	**-**	**5**	**-**	**5**	**-**	**5**
Other	**-**	**4**	**13**	**17**	**-**	**17**
Corporate and other domestic debt securities	**-**	**750**	**717**	**1,467**	**-**	**1,467**
Debt Securities issued by foreign entities:						

Corporate	-	311	197	508	-	508
Government	-	430	-	430	-	430
Equity securities	-	28	19	47	-	47
Precious metals trading	-	16,388	-	16,388	-	16,388
Derivatives(2):						
Interest rate contracts	210	35,990	-	36,200	-	36,200
Foreign exchange contracts	4	14,578	277	14,859	-	14,859
Equity contracts	3	1,377	44	1,424	-	1,424
Precious metals contracts	9	725	-	734	-	734
Credit contracts	-	14,411	2,875	17,286	-	17,286
Other	5	5	12	22	-	22
Derivatives netting	-	-	-	-	(61,930)	(61,930)
Total derivatives	231	67,086	3,208	70,525	(61,930)	8,595
Securities available-for-sale:						
U.S. Treasury. U.S. Government agencies and sponsored enterprises	12,485	17,138	-	29,623	-	29,623
Obligations of U.S. states and political subdivisions	-	627	-	627	-	627
Asset-backed securities:						
Residential mortgages	-	23	274	297	-	297
Commercial mortgages	-	575	10	585	-	585
Home equity	-	172	220	392	-	392
Auto	-	14	7	21	-	21
Student loans	-	17	13	30	-	30
Other	-	20	87	107	-	107
Corporate and other domestic debt securities	-	700	-	700	-	700
Debt Securities issued by foreign entities:						
Corporate	-	514	-	514	-	514
Government	-	2,656	-	2,656	-	2,656
Equity securities	-	1,402	-	1,402	-	1,402
Loans(3)	-	1,501	11	1,512	-	1,512
Intangible(4)	-	-	317	317	-	317
Total assets	$13,443	$110,532	$6,476	$130,451	$(61,930)	$68,521
Liabilities:						
Deposits in domestic offices(5)	$-	$3,398	$2,381	$5,779	$-	$5,779
Trading liabilities, excluding derivatives	1,499	3,160	-	4,659	-	4,659
Derivatives(2):						
Interest rate contracts	114	36,555	-	36,669	-	36,669
Foreign exchange contracts	26	14,234	280	14,540	-	14,540
Equity contracts	-	1,375	185	1,560	-	1,560
Precious metals contracts	46	984	-	1,030	-	1,030
Credit contracts	-	15,937	1,235	17,172	-	17,172
Other	-	1	-	1	-	1
Derivatives netting	-	-	-	-	(64,192)	(64,192)
Total derivatives	186	69,086	1,700	70,972	(64,192)	6,780
Long-term debt(6)	-	4,682	201	4,883	-	4,883
Total liabilities	$1,685	$80,326	$4,282	$86,293	$(64,192	$22,101

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	Fair Value Measurements on a Recurring Basis as of December 31, 2009					
	Level 1	Level 2	Level 3	Gross Balance	Netting(1)	Net Balance
			(in millions)			
Assets:						
Trading Securities:						
U.S. Treasury. U.S. Government agencies and sponsored enterprises	$615	$50	$-	$665	$-	$665
Residential mortgage-backed securities	-	129	821	950	-	950
Collateralized debt obligations	-	-	831	831	-	831
Other asset-backed securities	-	9	25	34	-	34
Corporate and other domestic debt securities	-	792	1,202	1,994	-	1,994
Debt Securities issued by foreign entities	-	213	196	409	-	409
Equity securities	-	436	21	457	-	457
Precious metals trading	-	12,256	-	12,256	-	12,256
Derivatives(2)	129	58,391	3,074	61,594	(52,763)	8,831
Securities available-for-sale:						
U.S. Treasury. U.S. Government agencies and sponsored enterprises	9,291	10,639	3	19,933	-	19,933
Obligations of U.S. states and political subdivisions	-	749	-	749	-	749
Residential mortgage-backed securities	-	350	515	865	-	865
Commercial mortgage-backed securities	-	558	8	566	-	566
Other asset-backed securities	-	273	217	490	-	490
Corporate and other domestic debt securities	-	864	-	864	-	864
Debt Securities issued by foreign entities	-	3,076	-	3,076	-	3,076
Equity securities	-	1,263	-	1,263	-	1,263
Loans(3)	-	1,122	4	1,126	-	1,126
Intangible(4)	-	-	450	450	-	450
Total assets	$10,035	$91,170	$7,367	$108,572	$(52,763)	$55,809
Liabilities:						
Deposits in domestic offices(5)	$-	$2,589	$1,643	$4,232	$-	$4,232
Trading liabilities, excluding derivatives	34	2,653	-	2,687	-	2,687
Derivatives(2)	213	60,639	1,781	62,633	(57,214)	5,419
Long-term debt(6)	-	4,149	419	4,568	-	4,568
Total liabilities	$247	$70,030	$3,843	$74,120	$(57,214)	$16,906

(1) Represents counterparty and cash collateral netting which allow the offsetting of amounts relating to certain contracts if certain conditions are met.

(2) Includes trading derivative assets of $8.0 billion and $8.2 billion and trading derivative liabilities of $6.2 billion and $5.3 billion as of June 30, 2010 and December 31, 2009, respectively, as well as derivatives held for hedging and commitments accounted for as derivatives.

(3) Includes leveraged acquisition finance and other commercial loans held for sale or risk-managed on a fair value basis for which we have elected to apply the fair value option. See Note 6, "Loans Held for Sale," for further information.

(4) Represents residential mortgage servicing rights. See Note 7, "Intangible Assets," for further information on residential mortgage servicing rights.

(5) Represents structured deposits risk-managed on a fair value basis for which we have elected to apply the fair value option.

(6) Includes structured notes and own debt issuances which we have elected to measure on a fair value basis.

Significant Transfers into/out of Levels 1 and 2
There were no significant transfers between levels 1 and 2 for the three and six months ended June 30, 2010.

Information on Level 3 Assets and Liabilities
The following table summarizes additional information about changes in the fair value of Level 3 assets and liabilities during the three and six months ended June 30, 2010 and 2009. As a risk management practice, we may risk manage the Level 3 assets and liabilities, in whole or in part, using securities and derivative positions that are classified as Level 1 or Level 2 measurements within the fair value hierarchy. Since those Level 1 and Level 2 risk management positions are not included in the table below, the information provided does not reflect the effect of such risk management activities related to the Level 3 assets and liabilities.

		Total Gains and (Losses) Included in(1)						
	April 1, 2010	Trading Revenue (Loss)	Other Revenue	Other Comprehensive Income	Purchases	Issuances	Settlements	Transfers Into Level 3
						(in millions)		
Assets:								
Trading assets, excluding derivatives								
Collateralized debt obligations	$755	$(106)	$-	$-	$154	$-	$(12)	$
Asset-backed securities:								
Residential mortgages	826	29	-	-	35	-	(330)	
Commercial mortgages	-	-	-	-	-	-	-	
Home equity	25	27	-	-	-	-	(25)	
Other	-	-	-	-	-	-	-	1
Corporate and other domestic debt securities	644	6	-	-	70	-	(3)	

Debt Securities issued by foreign entities:								
Corporate	**222**	**(25)**	**-**	**-**	**-**	**-**	**-**	
Equity securities	**19**	**-**	**-**	**-**	**-**	**-**	**-**	
Foreign exchange contracts	**(119)**	**(10)**	**-**	**-**	**-**	**(3)**	**129**	
Equity contracts	**50**	**(126)**	**-**	**-**	**-**	**-**	**(56)**	**(18**
Credit contracts	**1,344**	**331**	**-**	**-**	**-**	**-**	**(20)**	
Other	**2**	**-**	**10**	**-**	**-**	**-**	**-**	
Securities available-for-sale:								
U.S. Treasury, U.S. Government agencies and sponsored enterprises	-	**-**	**-**	**-**	**-**	**-**	**-**	
Asset-backed securities:								
Residential mortgages	**529**	**-**	**-**	**(1)**	**-**	**-**	**(266)**	**1**
Commercial mortgages	**8**	**-**	**-**	**2**	**-**	**-**	**-**	
Home equity	**215**	**-**	**-**	**11**	**-**	**-**	**(7)**	
Auto	**29**	**-**	**-**	**-**	**-**	**-**	**(22)**	
Student loans	**12**	**-**	**-**	**1**	**-**	**-**	**-**	
Other	-	**-**	**-**	**-**	**-**	**-**	**-**	**8**
Loans(3)	**12**	**-**	**(1)**	**-**	**-**	**-**	**-**	
Other assets, excluding derivatives(4)	**444**	**-**	(108)	**-**	**-**	**-**	(19)	
Total assets	**$5,017**	**$126**	$(99)	**$13**	**$259**	$(3)	$(631)	**$10**
Liabilities:								
Deposits in domestic offices	**$(1,940)**	**$94**	**$-**	**$-**	**$-**	**$(624)**	**$73**	**$(168**
Long-term debt	(604)	**40**	**-**	**-**	**-**	(12)	**50**	(3
Total liabilities	$(2,544)	**$134**	**$-**	**$-**	**$-**	$(636)	**$123**	$(20

	Total Gains and (Losses) Included in(1)						
	Trading		Other	Net Purchases	Transfers Into or		Current Period
April 1,	(Loss)	Other	Comprehensive	Issuances and	Out	June 30,	Unrealized
2009	Revenue	Revenue	Income	Settlements	of Level 3	2009	Gains (Losses)
			(in millions)				

Assets:								
Trading assets, excluding derivatives								
Residential mortgage-backed securities	$510	$(10)	$-	$-	$(25)	$102	$577	$(49)
Collateralized debt obligations	594	(279)	-	-	363	-	678	(81)
Other asset-backed securities	28	1	-	-	(6)	9	32	1
Corporate and other domestic debt securities	527	165	-	-	(1)	318	1,009	162
Debt Securities issued by foreign entities	77	61	-	-	-	-	138	61
Equity securities	144	(113)	-	-	(6)	1	26	(113)
Precious metals	-	-	-	-	-	-	-	-
Derivatives, net(2)	4,687	(1,538)	(12)	-	(37)	9	3,109	(2,265)
Securities available-for-sale								
U.S. Treasury, U.S. Government agencies and sponsored enterprises	-	-	-	-	-	3	3	-
Obligations of U.S. states and political subdivisions	2	-	-	-	-	(2)	-	-
Residential mortgage-backed securities	333	-	-	19	(28)	(6)	318	3
Commercial mortgage-backed securities	5	-	-	-	-	-	5	-
Collateralized debt obligations	-	-	-	-	-	-	-	-
Other asset-backed securities	256	-	-	53	(38)	(32)	239	45
Loans(3)	155	-	11	-	(38)	-	128	8
Other assets, excluding derivatives(4)	313	-	84	-	37	-	434	89
Total Assets	$7,631	$(1,713)	$83	$72	$221	$402	$6,696	$(2,139)
Liabilities:								
	$(404)	$-	$(4)	$-	$(314)	$2	$(720)	$(3)

Deposits in domestic offices								
Long term debt	(82)	-	(11)	-	(125)	2	(216)	(10)
Total liabilities	$(486)	$-	$(15)	$-	$(439)	$4	$(936)	$(13)

		Total Gains and (Losses) Included in(1)						
	Jan. 1, 2010	**Trading Revenue (Loss)**	**Other Revenue**	**Other Comprehensive Income**	**Purchases**	**Issuances**	**Settlements**	**Transfers Into Level 3**
					(in millions)			
Assets:								
Trading assets, excluding derivatives								
Collateralized debt obligations	**$832**	**$(38)**	**$-**	**$-**	**$235**	**$-**	**$(238)**	**$**
Asset-backed securities:								
Residential mortgages	**817**	**79**	**-**	**-**	**54**	**-**	**(411)**	**2**
Commercial mortgages	**4**	**(4)**	**-**	**-**	**-**	**-**	**-**	
Home equity	**24**	**(48)**	**-**	**-**	**215**	**-**	**(163)**	
Other	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**1**
Corporate and other domestic debt securities	**1,202**	**(26)**	**-**	**-**	**96**	**-**	**(371)**	
Debt Securities issued by foreign entities:								
Corporate	**195**	**1**	**-**	**-**	**-**	**-**	**1**	
Equity securities	**21**	**(1)**	**-**	**-**	**-**	**-**	**(1)**	
Foreign exchange contracts	**(95)**	**(34)**	**-**	**-**	**-**	**(3)**	**129**	
Equity contracts	**81**	**(44)**	**-**	**-**	**-**	**-**	**(112)**	**(75**
Credit contracts	**1,311**	**150**	**-**	**-**	**-**	**-**	**(90)**	**21**
Other	**(3)**	**-**	**16**	**-**	**-**	**-**	**(1)**	
Securities available-for-sale:								
U.S. Treasury, U.S. Government agencies and sponsored enterprises	**3**	**-**	**-**	**-**	**-**	**-**	**-**	
Asset-backed securities:								

Residential mortgages	**515**	**-**	**-**	**15**	**-**	**-**	**(337)**	**8**
Commercial mortgages	**8**	**-**	**-**	**3**	**-**	**-**	**(1)**	
Home equity	**175**	**-**	**-**	**56**	**-**	**-**	**(11)**	
Auto	**43**	**-**	**-**	**-**	**-**	**-**	**(36)**	
Student loans	**-**	**-**	**-**	**1**	**-**	**-**	**-**	**1**
Other	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**8**
Loans(3)	**4**	**-**	**-**	**-**	**-**	**-**	**(1)**	**1**
Other assets, excluding derivatives(4)	**450**	**-**	(87)	**-**	**-**	**-**	(46)	
Total assets	**$5,587**	**$35**	$(71)	**$75**	**$600**	$(3)	$(1,689)	**$37**
Liabilities:								
Deposits in domestic offices	**$(1,643)**	**$22**	**$-**	**$-**	**$-**	**$(934)**	**$148**	**$(164**
Long-term debt	(419)	**28**	**-**	**-**	**-**	(221)	**79**	(3
Total liabilities	$(2,062)	**$50**	**$-**	**$-**	**$-**	$(1,155)	**$227**	$(20

		Total Gains and (Losses) Included in(1)						
	January 1, 2009	Trading (Loss) Revenue	Other Revenue	Other Comprehensive Income	Net Purchases Issuances and Settlements	Transfers Into or Out of Level 3	June 30, 2009	Current Period Unrealized Gains (Losses)
				(in millions)				
Assets:								
Trading assets, excluding derivatives								
Residential mortgage-backed securities	$475	$(51)	$-	$-	$(5)	$158	$577	$(88)
Collateralized debt obligations	668	(338)	-	-	348	-	678	(133)
Other asset-backed securities	36	(6)	-	-	(7)	9	32	(5)
Corporate and other domestic debt securities	480	170	-	-	14	345	1,009	166
Debt Securities issued by foreign entities	87	52	-	-	(1)	-	138	52
Equity securities	147	(94)	-	-	(28)	1	26	(94)

Precious metals	-	-	-	-	-	-	-	-
Derivatives, net(2)	5,283	(2,098)	(13)	-	(17)	(46)	3,109	(2,471)
Securities available-for-sale								
U.S. Treasury, U.S. Government agencies and sponsored enterprises	-	-	-	-	-	3	3	-
Obligations of U.S. states and political subdivisions	-	-	-	-	-	-	-	-
Residential mortgage-backed securities	164	-	-	9	(40)	185	318	(6)
Commercial mortgage-backed securities	-	-	-	-	-	5	5	-
Collateralized debt obligations	-	-	-	-	-	-	-	-
Other asset-backed securities	307	-	-	17	(63)	(22)	239	7
Loans(3)	136	-	11	-	(19)	-	128	8
Other assets, excluding derivatives(4)	333	-	36	-	65	-	434	61
Total Assets	$8,116	$(2,365)	$34	$26	$247	$638	$6,696	$(2,503)
Liabilities:								
Deposits in domestic offices	$(234)	$-	$6	$(500)	$8	$-	$(720)	$7
Long term debt	(57)	-	(12)	(151)	4	-	(216)	(14)
Total liabilities	$(291)	$-	$(6)	$(651)	$12	$-	$(936)	$(7)

(1) Includes realized and unrealized gains and losses.

(2) Level 3 net derivatives included derivative assets of $3.2 billion and $5.1 billion and derivative liabilities of $1.7 billion and $2.0 billion at June 30, 2010 and 2009, respectively.

(3) Includes Level 3 corporate lending activities risk-managed on a fair value basis for which we have elected the fair value option.

(4) Represents residential mortgage servicing activities. See Note 7, "Intangible Assets," for additional information.

Assets and Liabilities Recorded at Fair Value on a Non-recurring Basis

The following table presents information about our assets and liabilities measured at fair value on a non-recurring basis as of June 30, 2010 and June 30, 2009, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value.

	Non-Recurring Fair Value Measurements as of June 30, 2010				Total Gains (Losses) For the Three Months Ended	Total Gains (Losses) For the Six Months Ended
	Level 1	Level 2	Level 3	Total	June 30, 2010	June 30, 2010
	(in millions)					
Residential mortgage loans held for sale(1)	$-	$16	$501	$517	$(27)	$(32)
Other consumer loans held for sale(1)	-	-	28	28	-	-
Impaired loans(2)	-	-	377	377	19	32
Real estate owned(3)	-	82	-	82	2	6
Repossessed vehicles(3)	-	4	-	4	-	-
Commercial loans held for sale	-	23	-	23	-	-
Held to maturity asset-backed securities held by consolidated VIE(4)	-	127	128	255	2	(3)
Building held for use	-	-	15	15	-	-
Total assets at fair value on a non-recurring basis	$-	$252	$1,049	$1,301	$(4)	$3

	Non-Recurring Fair Value Measurements as of June 30, 2009				Total Gains (Losses) For the Three Months Ended	Total Gains (Losses) For the Six Months Ended
	Level 1	Level 2	Level 3	Total	June 30, 2009	June 30, 2009
	(in millions)					
Residential mortgage loans held for sale(1)	$ -	$290	$990	$1,280	$(66)	$(159)
Auto finance loans held for sale(1)	-	-	288	288	-	-
Other consumer loans held for sale(1)	-	-	45	45	-	-
Impaired loans(2)	-	-	198	198	10	27
Real estate owned(3)	-	75	-	75	1	2
Repossessed vehicles(3)	-	5	-	5	-	-
Building held for use	-	-	15	15	(20)	(20)
Total assets at fair value on a non-recurring basis	$ -	$370	$1,536	$1,906	$(75)	$(150)

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(1) As of June 30, 2010 and 2009, the fair value of the loans held for sale was below cost. Certain residential mortgage loans held for sale have been classified as a Level 3 fair value measurement within the fair value hierarchy as the underlying real estate properties which determine fair value are illiquid assets as a result of market conditions and significant inputs in estimating fair value were unobservable. Additionally, the fair value of these properties is affected by, among other things, the location, the payment history and the completeness of the loan documentation.

(2) Represents impaired commercial loans. Certain commercial loans have undergone troubled debt restructurings and are considered impaired. As a matter of practical expedient, we measure the credit impairment of a collateral-dependent loan based on the fair value of the collateral asset. The collateral often involves real estate properties that are illiquid due to market conditions. As a result, these commercial loans are classified as a Level 3 fair value measurement within the fair value hierarchy.

(3)

Real estate owned and repossessed vehicles are required to be reported on the balance sheet net of transaction costs. The real estate owned and repossessed vehicle amounts in the table above reflect the fair value of the underlying asset unadjusted for transaction costs.

(4) Represents held to maturity securities which were held at fair value at June 30, 2010. See Note 16, "Variable Interest Entities" for additional information.

Fair Value of Financial Instruments
The fair value estimates, methods and assumptions set forth below for our financial instruments, including those financial instruments carried at cost, are made solely to comply with disclosures required by generally accepted
accounting principles in the United States and should be read in conjunction with the financial statements and notes included in this quarterly report.

	June 30, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in millions)			
Financial assets:				
Short-term financial assets	**$17,706**	**$17,706**	$24,094	$24,094
Federal funds sold and securities purchased under resale agreements	**15,490**	**15,490**	1,046	1,046
Non-derivative trading assets	**21,144**	**21,144**	17,596	17,596
Derivatives	**8,595**	**8,595**	8,831	8,831
Securities	**40,674**	**40,874**	30,568	30,686
Commercial loans, net of allowance for credit losses	**28,804**	**29,135**	29,366	29,298
Commercial loans designated under fair value option and held for sale	**1,554**	**1,554**	1,126	1,126
Consumer loans, net of allowance for credit losses	**41,907**	**36,834**	46,262	41,877
Consumer loans held for sale:				
Residential mortgages	**985**	**1,001**	1,386	1,389
Auto finance	-	-	353	353
Other consumer	**28**	**28**	43	43
Financial liabilities:				
Short-term financial liabilities	**$18,954**	**$18,954**	$11,121	$11,121
Deposits:				
Without fixed maturities	**112,064**	**112,064**	106,890	106,890
Fixed maturities	**3,720**	**3,730**	7,215	7,259
Deposits designated under fair value option	**5,779**	**5,779**	4,232	4,232
Non-derivative trading liabilities	**4,659**	**4,659**	2,687	2,687
Derivatives	**6,780**	**6,780**	5,419	5,419
Long-term debt	**12,868**	**13,133**	13,440	13,693
Long-term debt designated under fair value option	**4,883**	**4,883**	4,568	4,568

Loan values presented in the table above were determined using the Fair Value Framework for measuring fair value, which is based on our best estimate of the amount within a range of value we believe would be received in a sale as of the balance sheet date (i.e. exit price). The secondary market demand and estimated value for our loans has been heavily influenced by the deteriorating economic conditions during the past few years, including house price depreciation, rising unemployment, changes in consumer behavior, and changes in discount rates. Many investors are non-bank financial institutions or hedge funds with high equity levels and a high cost of debt. For certain consumer loans, investors incorporate numerous assumptions in predicting cash flows, such as higher charge-off levels and/or slower voluntary prepayment speeds than we, as the servicer of these loans, believe will ultimately be the case. The investor discount

rates reflect this difference in overall cost of capital as well as the potential volatility in the underlying cash flow assumptions, the combination of which may yield a significant pricing discount from our intrinsic value. The estimated fair values at June 30, 2010 and December 31, 2009 reflect these market conditions.

Valuation Techniques
Following is a description of valuation methodologies used for assets and liabilities recorded at fair value and for estimating fair value for those financial instruments not recorded at fair value for which fair value disclosure is required.

Short-term financial assets and liabilities
- The carrying value of certain financial assets and liabilities recorded at cost is considered to approximate fair value because they are short-term in nature, bear interest rates that approximate market rates, and generally have negligible credit risk. These items include cash and due from banks, interest bearing deposits with banks, accrued interest receivable, customer acceptance assets and liabilities and short-term borrowings.

Federal funds sold and purchased and securities purchased and sold under resale and
repurchase agreements -
Federal funds sold and purchased and securities purchased and sold under resale and repurchase agreements are recorded at cost. A significant majority of these transactions are short-term in nature and, as such, the recorded amounts approximate fair value. For transactions with long-dated maturities, fair value is based on dealer quotes for instruments with similar terms and collateral.

Loans
- Except for leveraged loans, selected residential mortgage loans and certain foreign currency denominated commercial loans, we do not record loans at fair value on a recurring basis. From time to time, we record on a non-recurring basis negative adjustment to loans. The write-downs can be based on observable market price of the loan or the underlying collateral value. In addition, fair value estimates are determined based on the product type, financial characteristics, pricing features and maturity. Where applicable, similar loans are grouped based on loan types and maturities and fair values are estimated on a portfolio basis.

- Mortgage Loans Held for Sale - Certain residential mortgage loans are classified as held for sale and are recorded at the lower of cost or fair value. As of June 30, 2010, the fair value of these loans is below their amortized cost. The fair value of these mortgage loans is determined based on the valuation information observed in alternative exit markets, such as the whole loan market, adjusted for portfolio specific factors. These factors include the location of the collateral, the loan-to-value ratio, the estimated rate and timing of default, the probability of default or foreclosure and loss severity if foreclosure does occur.

- Leveraged Loans - We record leveraged loans and revolvers held for sale at fair value. Where available, market consensus pricing obtained from independent sources is used to estimate the fair value of the leveraged loans and revolvers. In determining the fair value, we take into consideration the number of participants submitting pricing information, the range of pricing information and distribution, the methodology applied by the pricing services to cleanse the data and market liquidity. Where consensus pricing information is not available, fair value is estimated using observable market prices of similar instruments or inputs, including bonds, credit derivatives, and loans with similar characteristics. Where observable market parameters are not available, fair value is determined based on contractual cash flows, adjusted for the probability of default and estimated recoveries where applicable, discounted at the rate demanded by market participants under current market conditions. In those cases, we also consider the loan specific attributes and inherent credit risk and risk mitigating factors such as collateral arrangements in determining fair value.

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Commercial Loans - Commercial loans and commercial real estate loans are valued by discounting the contractual cash flows, adjusted for prepayments and the borrower's credit risk, using a discount rate that reflects the current rates offered to borrowers of similar credit standing for the remaining term to maturity and our own estimate of liquidity premium.

- Commercial impaired loans - Fair value is determined based on the pricing quotes obtained from an independent third party appraisal.

- Consumer Loans - The estimated fair value of our consumer loans were determined by developing an approximate range of value from a mix of various sources as appropriate for the respective pool of assets. These sources included, among other things, value estimates from an HSBC affiliate which reflect over-the-counter trading activity, forward looking discounted cash flow models using assumptions we believe are consistent with those which would be used by market participants in valuing such receivables; trading input from other market participants which includes observed primary and secondary trades; where appropriate, the impact of current estimated rating agency credit tranching levels with the associated benchmark credit spreads; and general discussions held directly with potential investors.

  Model inputs include estimates of future interest rates, prepayment speeds, loss curves and market discount rates reflecting management's estimate of the rate that would be required by investors in the current market given the specific characteristics and inherent credit risk of the receivables. Some of these inputs are influenced by home price changes and unemployment rates. To the extent available, such inputs are derived principally from or corroborated by observable market data by correlation and other means. We perform periodic validations of our valuation methodologies and assumptions based on the results of actual sales of such receivables. In addition, from time to time, we may engage a third party valuation specialist to measure the fair value of a pool of receivables. Portfolio risk management personnel provide further validation through discussions with third party brokers and other market participants. Since an active market for these receivables does not exist, the fair value measurement process uses unobservable significant inputs which are specific to the performance characteristics of the various receivable portfolios.

Lending-related Commitments
- The fair value of commitments to extend credit, standby letters of credit and financial guarantees are not included in the table. The majority of the lending related commitments are not carried at fair value on a recurring basis nor are they actively traded. These instruments generate fees, which approximate those currently charged to originate similar commitments, which are recognized over the term of the commitment period. Deferred fees on commitments and standby letters of credit totaled $53 million and $48 million at June 30, 2010 and December 31, 2009, respectively.

Precious Metals Trading
- Precious metals trading primarily include physical inventory which are valued using spot prices.

Securities
- Where available, debt and equity securities are valued based on quoted market prices. If a quoted market price for the identical security is not available, the security is valued based on quotes from similar securities, where possible. For certain securities, internally developed valuation models are used to determine fair values or validate quotes obtained from pricing services. The following summarizes the valuation methodology used for our major security classes:

- U.S. Treasury, U.S. Government agency issued or guaranteed and Obligations of U.S. state and political subdivisions - As these securities transact in an active market, fair value measurements are based on quoted prices for the identical security or quoted prices for similar securities with adjustments as

necessary made using observable inputs which are market corroborated.

- U.S. Government sponsored enterprises - For certain government sponsored mortgage-backed securities which transact in an active market, fair value measurements are based on quoted prices for the identical security or quoted prices for similar securities with adjustments as necessary made using observable inputs which are market corroborated. For government sponsored mortgage-backed securities which do not transact in an active market, fair value is determined primarily based on pricing information obtained from pricing services and is verified by internal review processes.

- Asset-backed securities, including collateralized debt obligations - Fair value is primarily determined based on pricing information obtained from independent pricing services adjusted for the characteristics and the performance of the underlying collateral.

Additional information relating to asset-backed securities and collateralized debt obligations is presented in the following tables:

Trading asset-backed securities and related collateral:

		Prime		Alt-A		Sub-prime		
Rating of Securities:	**Collateral Type:**	**Level 2**	**Level 3**	**Level 2**	**Level 3**	**Level 2**	**Level 3**	**Total**
			(in millions)					
AAA -A	Residential mortgages	$4	$-	$41	$80	$-	$339	$464
	Home equity	-	-	-	13	-	-	13
	Student loans	-	-	5	-	-	-	5
	Other	-	-	-	-	-	-	-
	Total AAA -A	4	-	46	93	-	339	482
BBB -B	Residential mortgages	-	-	-	65	-	-	65
	Home equity	-	-	-	3	-	2	5
	Total BBB -B	-						