

**THE AUDIT AND RISK COMMITTEE (THE “COMMITTEE”) OF
THE BOARD OF DIRECTORS (“THE BOARD”) OF
HSBC BANK BERMUDA LIMITED (THE “COMPANY”)**

TERMS OF REFERENCE

Membership

The Committee shall comprise not less than three independent¹ non-executive directors².

The Chairman of the Committee shall be appointed by the Board³. Members of the Committee and the Chairman shall be appointed subject to endorsement by the Group Audit Committee and Group Risk Committee.

The Board³ may from time to time appoint⁴ to the Committee additional members whom it has determined to be independent. In the absence of sufficient independent non-executive directors, the Board³ may appoint individuals from elsewhere in the HSBC Group⁵ with no line or functional responsibility for the activities of the Group⁵.

The Committee may invite any director, executive, external auditor or other person to attend any meeting(s) of the Committee as it may from time to time consider desirable to assist the Committee in the attainment of its objective.

Meetings and Quorum

The Committee shall meet with such frequency and at such times as it may determine. It is expected that the Committee shall meet at least four times each year.

The quorum for meetings shall be two directors.

Objective

The Committee shall be accountable to the Board³ and shall have non-executive responsibility for oversight of and advice to the Board³ on matters relating to financial reporting and high level risk related matters and risk governance.

Responsibilities of the Committee

Without limiting the generality of the Committee’s objective, the Committee shall have the following non-executive responsibilities, powers, authorities and discretions:

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Endorsed by Group Audit Committee: 18th November, 2008

Approved by the Board: 19th February, 2009

Approved by the Board: 7th May, 2009

Approved by the Board: 15th July, 2010

Approved by the Board: 17th November, 2011

Approved by the Board: 10th May, 2012

Key responsibilities in relation to Audit

1. To monitor the integrity of the financial statements of the Company, and any formal announcements relating to the Company's financial performance or supplementary regulatory information, reviewing significant financial reporting judgements contained in them. In reviewing the Company's financial statements before submission to the Board³, the Committee shall focus particularly on:
 - (i) any changes in accounting policies and practices;
 - (ii) major judgemental areas;
 - (iii) significant adjustments resulting from audit;
 - (iv) the going concern assumptions and any qualifications;
 - (v) compliance with accounting standards;
 - (vi) compliance with applicable listing and other legal requirements in relation to financial reporting;
 - (vii) regulatory guidance on disclosure of areas of special interest;
 - (viii) comment letters from appropriate regulatory authorities; and
 - (ix) matters drawn to the attention of the Committee by the Company's external auditor.

In regard to the above:

- (a) members of the Committee shall liaise with the Board³; members of senior management; the external auditor; and the Company's Internal Audit representative; and
 - (b) the Committee shall consider any significant or unusual items that are, or may need to be, highlighted in the annual report and accounts and shall give due consideration to any matters raised by the staff responsible for the accounting and financial reporting function; the Company's Internal Audit representative; the Head of Compliance; the General Counsel; or the external auditor.
2. To review the Company's financial and accounting policies and practices.
 3. To review and discuss with management the effectiveness of the Company's internal control systems relating to financial reporting and, where appropriate, to endorse the content of the statement relating to internal controls over financial reporting in the annual report for submission to the Board³.
 4. To monitor and review the effectiveness of the internal audit function, consider the major findings of internal investigations and management's response, and ensure that the internal audit function is adequately resourced, has appropriate standing within the HSBC Group⁵ and is free from constraint by management or other restrictions. Where applicable, the Committee shall recommend to the Board³ the appointment and removal of the Company's Internal Audit representative.
 5. To satisfy itself that there is appropriate co-ordination between the internal and external auditors.

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6. To make recommendations to the Board³, for it to put to the shareholders for their approval in general meeting, in relation to the appointment, re-appointment and removal of the external auditor and shall be directly responsible for the approval of the remuneration and terms of engagement of the external auditor.
7. To review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant professional and regulatory requirements and reports from the external auditors on their own policies and procedures regarding independence and quality control and to oversee the appropriate rotation of audit partners with the external auditor.
8. To implement the HSBC Group⁵ policy on the engagement of the external auditor to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external audit firm; and, where required under that policy, to approve in advance any non-audit services provided by the external auditor that are not prohibited by the Sarbanes-Oxley Act -2002 (in amounts to be pre-determined by the Group Audit Committee) and the fees for any such services; to report to the Board³, identifying any matters in respect of which it considers that action or improvement is needed and make recommendations as to the steps to be taken. For this purpose "external auditor" shall include any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally.
9. To review the external auditor's annual report on the progress of the audit, its management letter, any material queries raised by the external auditor to management in respect of the accounting records, financial accounts or systems of control and, in each case, responses from management.
10. To require a timely response to be provided to the financial reporting and related control issues raised in the external auditor's management letter.
11. To discuss with the external auditor their general approach, nature and scope of their audit and reporting obligations before the audit commences including, in particular, the nature of any significant unresolved accounting and auditing problems and reservations arising from their interim reviews and final audits, major judgemental areas (including all critical accounting policies and practices used by the Company and changes thereto), all alternative accounting treatments that have been discussed with management together with the potential ramifications of using those alternatives, the nature of any significant adjustments, the going concern assumption, compliance with accounting standards and stock exchange and legal requirements, reclassifications or additional disclosures proposed by the external auditor which are significant or which may in the future become material, the nature and impact of any material changes in accounting policies and practices, any written communications provided by the external auditor to management and any other matters the external auditor may wish to discuss (in the absence of management where necessary).
12. To review and discuss the adequacy of resources, qualifications and experience of staff of the accounting and financial reporting function, their training programmes and budget and succession planning for key roles throughout the function.

13. To consider any findings of major investigations of internal control over financial reporting matters as delegated by the Board³ or on the Committee's initiative and assess management's response.
14. To receive an annual report, and other reports from time to time as may be required by applicable laws and regulations, from the principal executive officer and principal financial officer to the effect that such persons have disclosed to the Committee and to the external auditor all significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which could adversely affect the Company's ability to record and report financial data and any fraud, whether material or not, that involves management or other employees who have a significant role in the Company's internal controls over financial reporting.
15. To provide to the Board³ such assurances as it may reasonably require regarding compliance by the Company, its subsidiaries and those of its associates for which it provides management services with all supervisory and other regulations to which they are subject.
16. To provide to the Board³ such additional assurance as it may reasonably require regarding the reliability of financial information submitted to it.
17. To receive from the Compliance function reports on the treatment of substantiated complaints regarding accounting, internal accounting controls or auditing matters received through the Group Disclosure Line (or such other system as the Group Audit Committee or Group Risk Committee may approve) for the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.⁶
18. To report any significant actual, suspected or alleged fraud (involving misconduct or unethical behaviour related to financial reporting) or misrepresentations of assets which has not been included in a report submitted by management to the Committee to the Group Chief Risk Officer and Group Finance Director.
19. To agree with the Board³ the Company's policy for the employment of former employees of the external auditor, within the terms of the HSBC Group's⁵ policy.

Key responsibilities in relation to Risk

20. To oversee and advise the Board³ on all high-level risk-related matters.

In providing such oversight and advice to the Board³, the Committee shall oversee (i) current and forward-looking risk exposures; (ii) the Company's risk appetite and future risk strategy, including capital and liquidity management strategy; and (iii) management of risk within the Company.

21. To advise the Board³ on risk appetite and tolerance in determining strategy.

In preparing advice to the Board³ on risk appetite and tolerance, the Committee shall (i) satisfy itself that risk appetite informs the Company's strategy; (ii) seek such assurance as it may deem appropriate that account has been taken of the current and prospective macroeconomic and financial environment, drawing on financial stability assessments published by authoritative sources that may be relevant; (iii) review and approve the methodology used in establishing the Company's risk

appetite including for example risk asset ratios, limits on exposures and concentrations, leverage ratios, economic capital ratios and stress and scenario testing; and (iv) review the results of appropriate stress and scenario testing.

22. To advise the Board³ and/or the committee with non-executive responsibility in relation to remuneration on alignment of remuneration with risk appetite.
23. To consider and advise the Board³ on the risks associated with proposed strategic acquisitions or disposals as requested from time to time by any director in consultation with the Chairman of the Committee.

In preparing such advice the Committee shall satisfy itself that a due diligence appraisal of the proposition is undertaken, focussing in particular on risk aspects and implications for the risk appetite and tolerance of the HSBC Group⁵, drawing on independent external advice where appropriate and available, before the Board³ takes a decision whether to proceed.

24. To require regular risk management reports from management which:
 - (i) enable the Committee to assess the risks involved in the Company's business and how they are controlled and monitored by management; and
 - (ii) give clear, explicit and dedicated focus to current and forward-looking aspects of risk exposure which may require a complex assessment of the Company's vulnerability to hitherto unknown or unidentified risks.
25. To review the effectiveness of the Company's risk management framework and internal control systems (other than internal financial control systems).
In undertaking this responsibility the Committee shall:
 - (i) satisfy itself that there are adequate procedures for monitoring in a sufficiently timely and accurate manner, large exposures or risk types whose relevance may become of critical importance;
 - (ii) satisfy itself that there are adequate procedures in place for requiring compliance with HSBC Group⁵ policies;
 - (iii) consider any material findings from regulatory reviews and interactions with regulators in relation to risk governance or risk assessment or management process;
 - (iv) discuss the internal control systems with management and satisfy itself that management has discharged its duty to have an effective internal control system;
 - (v) satisfy itself that the risk management function is adequately resourced (including taking into account qualifications and experience of staff and training programmes and budget), has appropriate standing within the Company and is free from constraint by management or other restrictions; and
 - (vi) seek assurance from internal audit that internal control processes for risk management are adequate for the strategy determined by the Board³.
26. Where applicable, the Committee shall approve the appointment and removal of the Chief Risk Officer.

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The Committee shall seek such assurance as it may deem appropriate that the Chief Risk Officer:

- (i) participates in the risk management and oversight process at the highest level on an enterprise-wide basis;
 - (ii) has satisfied himself or herself that risk originators in the business units are aware of and aligned with the Company's risk appetite;
 - (iii) has a status of total independence from individual business units;
 - (iv) reports to the Committee alongside an internal functional reporting line to the Group Chief Risk Officer;
 - (v) cannot be removed from office without the prior agreement of the Board³; and
 - (vi) has direct access to the Chairman of the Committee in the event of need.
27. To seek to embed and maintain throughout the Company a supportive culture in relation to the management of risk and maintenance of internal controls alongside prescribed rules and procedures.
28. To review any issue which arises from any report from internal audit, the external auditor's annual report on the progress of the external audit, the management letter from the external auditor, any queries raised by the external auditor to management or, in each case, responses from management, which relates to the management of risk or internal control as this Committee shall consider appropriate.
29. To require a timely response to be provided by management on material issues relating to the management of risk or internal control (other than internal financial control) raised in the external auditor's management letter which are considered by the Committee.
30. To review and endorse the content of the statements made in relation to internal controls (other than internal financial controls) in the annual report and accounts for submission to the Board³.
31. Where applicable, to (i) review at least annually the terms of reference of the executive risk management meetings; and (ii) to review the minutes of such meetings and such further information as the executive risk management meeting may request from time to time.
32. To provide to the Board³ such additional assurance as it may reasonably require regarding the reliability of risk information submitted to it.
33. The Committee shall meet alone with the external auditor and with the Chief Risk Officer and the Company's Internal Audit representative at least once each year to ensure that there are no unresolved issues or concerns.
34. Where applicable to review the composition, powers, duties and responsibilities of subsidiary companies' non-executive audit and risk committees. The Group Audit Committee and/or Group Risk Committee (as appropriate) will review the core terms of reference for adoption by such committees and approve material deviations from such core terms.
35. To undertake or consider on behalf of the Chairman or the Board³ such other related tasks or topics as the Chairman or the Board³ may from time to time entrust to it.

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36. The Committee may appoint, employ or retain such professional advisors as the Committee may consider appropriate. In particular, the Committee shall consider whether external advice on risk matters should be taken to challenge analysis undertaken and assessments made by the Committee and the risk management function, for example an external advisor might be asked for input on the stress and scenario testing of a business strategy. Any such appointment shall be made through the Secretary to the Committee, who shall be responsible for the contractual arrangements and payment of fees by the Company on behalf of the Committee.
37. The Committee shall review annually the Committee's terms of reference and its own effectiveness and recommend to the Board³ any necessary changes.
38. To report to the Board³ on the matters set out in these terms of reference.
39. To provide half-yearly certificates to the Group Audit Committee or Group Risk Committee, or to any audit committee of an intermediate holding company in the form required by the Group Audit Committee or Group Risk Committee. Such certificates are to include a statement that the members of the Committee are independent^{1, 2, 4}

The Committee may consider any matter relating to, and may request any information as it considers appropriate, from any audit committee, risk committee or other committee which has responsibility for the oversight of risk with the Group⁵.

Where the Committee's monitoring and review activities reveal cause for concern or scope for improvement, it shall make recommendations to the Board³ on action needed to address the issue or to make improvements and shall report any such concerns to the Group Audit Committee and/ or the Group Risk Committee as appropriate; or to any audit and/or risk committee of an intermediate holding company as appropriate.

Notes

1. The determination of independence should take into account the following:
 - if the director has been an employee of the company or group within the last five years;
 - if the director has, or has had within the last three years, a material business relationship with the Company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the Company;
 - if the director has received or receives additional remuneration from the Company apart from a director's fee, participates in the Company's share option or a performance-related pay scheme, or is a member of the Company's pension scheme;
 - if the director has close family ties with any of the Company's advisers, directors or senior employees;
 - if the director holds cross-directorships or has significant links with other directors through involvement in other companies or bodies;
 - if the director represents a significant shareholder;

- if the director has served on the board for more than nine years from the date of their first election; and

any other circumstances which might, or might be perceived, to compromise the ability of the committee member to reach an objective and impartial decision about matters relating to the Company, its business or its customers. For example, the independence of a lawyer, accountant, auditor, or business associate of a customer would need to be considered carefully in relation to the affairs of that customer.
- 2. If there are no or insufficient independent non-executive directors available, the Group Audit Committee or the Group Risk Committee (as appropriate) will consider non-director appointees.
- 3. In the context of these terms of reference, “HSBC Board” means the Board of HSBC Holdings plc and “Board” means the Board of the subsidiary company.
- 4. Appointments shall be subject to the endorsement of the Group Audit Committee or the Group Risk Committee (as appropriate), which will wish to be satisfied that there are no circumstances which compromise the individual’s independence.
- 5. In the context of these terms of reference, “HSBC Group” means HSBC Holdings plc and its subsidiaries and “Group” means the group of companies headed by the subsidiary company.
- 6. A system is in place for a Group Disclosure Line (or such other system as the Group Audit Committee or Group Risk Committee may approve). Unless prohibited by law, it is recommended that this system be used, in which case the Committee should discharge this responsibility by ensuring that the system is accessible within the areas in which the Company operates.