UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF ILLINOIS

EASTERN DIVISION

LAWRENCE E. JAFFE PENSION PLAN, On Behalf of Itself and All Others Similarly Situated, Plaintiff, vs. HOUSEHOLD INTERNATIONAL, INC., et al., Defendants.	Lead Case No. 02-C-5893 (Consolidated) <u>CLASS ACTION</u> Judge Ronald A. Guzman Magistrate Judge Nan R. Nolan

DECLARATION OF BJORN I. STEINHOLT, CFA

DATED SEPTEMBER 12, 2013

I. Background

1. On May 27, 2009, I submitted a declaration that included the monthly prime rates provided by the Federal Reserve System FRED® Database, and a multiplier table to determine the amount of prejudgment interest in this case based on the prime rate. On July 25, 2013, I wrote a declaration that explained in greater detail how the prejudgment interest was calculated, and updated the multiplier table through July 2013 using both monthly and yearly compounding ("Steinholt Declaration").

2. I have now been asked to respond to three alternative approaches to calculate the prejudgment interest included in Defendants' Response to Plaintiffs' Motion for Entry of Judgment Pursuant to Fed. R. Civ P. 54(b) and for an Award of Prejudgment Interest, dated August 30, 2013 ("Defendants' Response"), and in the Declaration of Alexander Barnett, dated August 29, 2013 ("Barnett Declaration").

II. Issues with Using the 1-Year Constant Maturity Treasury Rate

3. Defendants argue that the prejudgment interest "to compensate a plaintiff for the loss of the use of its funds," should be the 1-year constant maturity treasury yield. Defendants' Response, at 9-10. I will not address the legal merits of Defendants' argument as this is outside the scope of my assignment. Rather, below I will explain the economic implications of using the 1-year constant maturity treasury yield as the prejudgment rate, including whether using this rate in the manner proposed by Defendants will "compensate a plaintiff for the loss of the use of its funds" from an economic point of view.

4. First, it should be noted that treasury yields reflect the borrowing rate of the U.S. government, not individual companies, and is therefore commonly viewed as reflecting the so-

called risk free rate, *i.e.*, a rate reflecting no credit risk for a given maturity.[1] Unlike the U.S. government, individual companies do not issue their own currency, so there will always be some credit risk (or risk of default) associated with their ability to pay future obligations. According to Defendants' Response, "'the risk of default must be considered in deciding what a compensatory rate of interest would be.'" Defendants' Response, at 15, quoting *Gorenstein*. If one of the objectives of the prejudgment interest rate is to compensate Plaintiffs for credit risk, as stated in Defendants' Response, then the use of treasury yields is inappropriate because these yields reflect the risk free rate.

5. Second, the proposed treasury yield in this case is so low that it does not even compensate Plaintiffs for the reduced purchasing power during the prejudgment period due to inflation.[2] In other words, the real interest rate proposed by Defendants is negative.[3] One reason for this is that, following the unprecedented 2007/2008 financial crisis, the Federal Reserve has followed a policy intended to force the interest rates on these short term securities to virtually zero, resulting in the real interest rate (*i.e.*, interest rate after adjusting for inflation) to be

---

[1] Frank J. Fabozzi, *Fixed Income Analysis*, John Wiley & Sons, Inc, Ch. 3, at 40 (2007). ("U.S. Treasury securities are issued by the U.S. Department of the Treasury and are backed by the full faith and credit of the U.S. government. As noted above, market participants throughout the world view U.S. Treasury securities as having no credit risk.")

[2] Inflation is the increase in price levels (or the decrease in the value of money or purchasing power) over time and is in the U.S. generally measured in terms of the change in the Consumer Price Index. Michael Parking, *Economics*, Pearson Education, Inc., Ch. 22, at 516, (2008). To keep up with inflation, the multiplier has to be at least 1.29. Steinholt Declaration, fn 1. Defendants' proposed multiplier using the 1-year constant maturity treasury yield is 1.22, *i.e.*, less than the required multiplier to keep up with inflation. Barnett Declaration, ¶3.b.

[3] Parking, *Economics*, at G-10, (2008). ("Real interest rate: The quantity of goods and services that a unit of capital earns. It is the nominal interest rate adjusted for inflation and is approximately equal to the nominal interest rate minus the inflation rate.")

negative.[4] If one of the objectives of the prejudgment rate is to compensate Plaintiffs for their loss of purchasing power due to inflation, then the use of the 1-year constant maturity treasury yield (especially following the 2007/2008 financial crisis) is inappropriate because it provides Plaintiffs with a negative real interest rate.[5]

6. Third, Defendants also inexplicably claim that "the return on one-year constant maturity Treasury bills during this prejudgment interest period is, in fact, roughly equivalent to the return 'for "securities" comparable in riskiness' to Plaintiffs' investment in financial sector stocks." Defendants' Response, at 11, partly quoting *Gorenstein*. This is incorrect. A common measure of risk is the standard deviation.[6] In this case, the annual standard deviation of the real rate of return for the S&P Financials index (dividends reinvested) was approximately 14 times greater than that of the 1-year treasury yield. Similarly, the annual standard deviation of the real rate of return for the S&P 500 was approximately 10 times that of the 1 year treasury yield. Consequently, if one of the objectives of the prejudgment rate is to replicate the risk and return characteristics of financial stocks, then the use of the 1-year constant maturity treasury yield is inappropriate because it has vastly different risk and return characteristics than financial stocks, or stocks in general.

---

[4] Board of Governors of the Federal Reserve System: "The financial crisis that began in 2007 was the most intense period of global financial strains since the Great Depression, and it led to a deep and prolonged global economic downturn. The Federal Reserve took extraordinary actions in response to the financial crisis to help stabilize the U.S. economy and financial system. These actions included reducing the level of short-term interest rates to near zero.") http://www.federalreserve.gov/faqs/money_12849.htm [8/30/2013 1:18:51 PM]

[5] Because of the declining purchasing power, Plaintiffs would have been better off spending the funds than investing in treasury yields. In the Steinholt Declaration, I also explained that some Class members may have needed the funds for uses other than investment (such as older Class members needing their funds for retirement), but that the benefit of having the option to use their funds for other purposes would be difficult to quantify. Steinholt Declaration, fn 4.

[6] Richard A. Brealey, Stewart C. Myers & Franklin Allen, *Principles of Corporate Finance*, 11th Ed., McGraw-Hill (2013), Ch. 7, at 7-2, p. 167.

7. As explained above, using the 1-year constant maturity treasury yield to calculate the prejudgment interest does not fully compensate Plaintiffs for the loss of the use of their funds, not even the loss of their purchasing power due to inflation.

III. Issues with Using HSBC's Short Term Commercial Paper Rate

8. Defendants next argue that the prejudgment interest should not exceed the "'interest rate paid by the defendant for unsecured loans,'" explaining that "[t]he rational for using the defendants' cost of borrowing is that '[t]he plaintiff is an unsecured, uninsured creditor, and the risk of default must be considered in deciding what a compensatory rate of interest would be.'"[7] Defendants' Response, at 14-15. Defendants further argue that the relevant rate for this purpose is the average interest HSBC Finance Corporation ("HSBCFC", formerly Household) paid on its commercial paper. Below I will explain the economic implications of using HSBCFC's commercial paper interest rate to calculate the prejudgment interest rate, including whether using this rate in the manner proposed by Defendants will compensate a plaintiff "for the risk of default" from an economic point of view.

9. First, as an initial matter, it is important to point out that the information needed to perform the calculation that Defendants purport to perform is not publicly available. For example, the interest HSBCFC paid on its commercial paper from October through December of 2002 is not known, at least not publicly. Defendants work around this problem by using the interest rate for the entire 2002, but then improperly give the same weight to the 2002 interest

---

7 Fabozzi, *Fixed Income Analysis*, Ch. 3, at 59. ("A corporate debt obligation may be secured or unsecured. Secured debt means that there is some form of collateral pledged to ensure payment of the debt. Remove the pledged collateral and we have unsecured debt." This means that, all else equal, the cost of unsecured debt is greater than that on secured debt.)

rate as the other years, unnecessarily biasing the result in the favor of Defendants.[8] Furthermore, and perhaps more problematic, "[d]uring the second quarter of 2012, [HSBCFC] ceased new commercial paper issuances and at December 31, 2012 no longer [had] any commercial paper balances outstanding." HSBCFC 2012 Form 10-K, at 32-33. In fact, HSBCFC's "wind-down of the commercial paper program and shift to affiliate funding" would, at a minimum, require the use of the average rate due affiliates instead of the rate for commercial paper, resulting in an increase in the 2012 interest rate from 0.30% (commercial paper rate used by Defendants) to 2.03% (average rate due affiliates), or an increase of more than 576%. *Id.*, at 89, 100. This further means that the calculation submitted by Defendants based on the interest rate for its commercial paper is not a viable approach due to lack of information.[9]

10. Second, Defendants incorrectly use yearly compounding, even though commercial paper is very short term in nature, usually less than 60 days.[10] If the commercial paper has a maturity of 30 days and is rolled over on a monthly basis, the correct compounding period from an economic point of view should be monthly.[11] In other words, after the first month the investor receives the initial funds invested plus the interest, so that for the second month the investor now can reinvest both the initial funds and the interest earned, not only the

---

[8] Because the interest rate for 2002 of 1.9% is less than the average used in Defendants' prejudgment calculation of 2.13%, the inclusion of the 2002 interest rate as if the entire year is part of the prejudgment period improperly overweights this year, and biases the result in favor of defendants.

[9] As I noted in my previous declaration, one of the benefits of using the prime rate to calculate the prejudgment interest is that the relevant interest rate is available on a monthly (and even daily) basis from the Federal Reserve. Steinholt Declaration, ¶3.

[10] Brealey, Myers & Allen, *Principles of Corporate Finance*, Ch. 24, at 628. ("Commercial paper in the United States has a maximum maturity of nine months, though most paper is for fewer than 60 days.")

[11] This is also why it is appropriate to compound the 1-year constant maturity treasury yield on a yearly basis, because it has a one year maturity. This reality was also explained in the Steinholt Declaration, ¶5.

initial funds as erroneously assumed by Defendants. The reinvestment of the interest earned is the same economic principle used by both I and Defendants' expert when we accounted for the reinvestment of dividends for the S&P 500 index and the S&P Financials index. Steinholt Declaration, fn 2; Barnett Declaration, ¶5. There is no reason to ignore this economic reality for commercial paper. Consequently, the compounding period used by Defendants is incorrect and provides a windfall to Defendants.

11. Third, HSBCFC funded its operation through various means, not just through issuing commercial paper, including "by collecting receivable balances; issuing commercial paper, medium and long term debt; borrowing from HSBC subsidiaries and customers; securitizing and selling consumer receivables; and borrowing under secured financing facilities." HSBCFC 2004 Form 10-K, at 4, *see* Ex. A attached hereto. The costs of these various funding sources varied. For example, in 2003, the first full year of the prejudgment interest period, the average rate for commercial paper used by Defendants was 1.6%, significantly below the average rate: (a) for deposits which were 3.6%, (b) for bank and other borrowings which were 3.9%, and (c) due to affiliates which were 2.4%. Ex. A, at 87. In fact, the average rate for all debt in 2003 was 3.4%, or more than twice that for HSBCFC's commercial paper. *Id.* Moreover, the coupon rate on HSBCFC's publicly traded debt ranged from 6% to 8.875%, and the weighted average interest rates on its long term debt was 5.1% (excluding purchase accounting adjustments). Ex. A, cover page and at 140. Also, the average interest rate earned in 2003 by HSBCFC on its interest-earning assets was 10.9%, resulting in an interest spread of 7.5%.[12] In other words, for 2003 the average commercial paper rate proposed by Defendants is

---

[12] Ex. A, at 87, fn 4. (The interest spread is "the difference between the yield earned on interest-earning assets and the cost of the debt used to fund the assets." This is more properly viewed as a measure of gross profits rather than net profits.)

less than half of that for deposits, less than half of that for HSBCFC's bank and other borrowings, substantially less than that paid by HSBCFC to their affiliates, less than half of that for all debt (including secured debt which should have a lower rate), and does not compensate Plaintiffs for any interest-earned by HSBCFC on their interest-earning assets funded by the debt.[13]

12. Fourth, the average rate HSBCFC paid on their commercial paper does not reflect what it would have paid if its potential obligation to Plaintiffs was viewed as an unsecured loan. For example, HSBCFC maintained "various bank credit agreements primarily to support commercial paper borrowings," including a "$4.0 billion revolving credit facility with HSBC Private Bank (Suisse) SA . . . to allow temporary increases in commercial paper issuances." Ex. A, at 139. Such credit facilities are not free. I am not aware of any similar arrangements made by HSBCFC to support, or guarantee, Defendants' potential obligation to Plaintiffs. Consequently, it is incorrect to simply assume that the interest rate on HSBCFC's commercial paper is the same rate it would have had to pay on an unsecured loan to Plaintiffs, as evidenced by the significantly greater interest rate HSBCFC had to pay its affiliates.

13. Fifth, a substantial portion of HSBCFC's commercial paper was issued abroad to foreign investors and in foreign currencies. Ex. A, at 67. This means that the commercial paper rate, at least to some degree, is more reflective of the interest rates that existed abroad and fluctuations in the relevant exchange rates than the actual interest HSBCFC would have to pay Plaintiffs if their potential obligation was an unsecured loan.

---

[13] While Defendants focus solely on debt, a more relevant measure from an economic point of view is the weighted average cost of capital, which also includes the cost of equity (*i.e.*, from an economic point of view one would consider the cost of all the capital used by an entity). As explained in the Steinholt Declaration, fn 5, the weighted average cost of capital for HSBC Holdings PLC during the prejudgment period exceeded the average prime rate.

14. Sixth, HSBCFC's commercial paper consisted of short term promissory notes which necessarily would reflect a significantly lower default risk than that of Defendants' potential obligation to Plaintiffs. For example, an investor in HSBCFC's commercial paper would have had the opportunity to decide, every time the commercial paper matured, whether or not to roll over their investment. This means that, if HSBCFC's financial condition started to deteriorate, investors in the commercial paper could shift their funds into less risky investments, thereby avoiding losses due to a potential default by HSBCFC. In contrast, Plaintiffs have had no ability over the past 10 years to reduce or limit their credit risk exposure to HSBCFC.

15. Seventh, Defendants' sole focus on HSBCFC's cost of debt ignores that Plaintiffs' borrowing costs is also relevant. As I previously explained, "if Class members had debt, they could have used these funds to reduce this debt, thereby benefitting from reducing their respective borrowing costs during the Prejudgment Period," and that "individual Class members' borrowing cost would obviously vary greatly depending on the individual circumstances of the Class member," but "would in almost all circumstances be equal to or greater than the prime rate." Steinholt Declaration, ¶2, fn 3.

16. Eight, as was true with the treasury yield, the proposed commercial paper rate in this case is so low that it does not even compensate Plaintiffs for the reduced purchasing power due to inflation.[14] In other words, the real interest rate proposed by Defendants is again negative. Consequently, if one of the objectives of the prejudgment rate is to compensate Plaintiffs for their loss of purchasing power due to inflation, then the use of the commercial paper rate is inappropriate because it provides Plaintiffs with a negative real interest rate.

---

[14] The multiplier calculated by Defendants of 1.26 is less than the 1.29 needed to keep up with inflation. Barnett Declaration, ¶4.b.; Steinholt Declaration, fn 1.

17. As explained above, using HSBCFC's commercial paper rate to calculate the prejudgment interest does not fully compensate Plaintiffs for the risk of default. Nor does this measure compensate Plaintiffs for the loss of their purchasing power due to inflation.

IV. Issues with the S&P 500 Financial Index

18. Defendants also argue that "it is appropriate to look to the return on an investment in a relevant financial index as a proxy for the rate of return a plaintiff would have earned had the plaintiff been able to invest its funds during the prejudgment interest period." Defendants' Response, fn 6. They then claim that Plaintiffs "cherry-pick[ed] the S&P 500 Index, rather than the Financials Index that more accurately reflects the return on investments in the sector at issue." In my previous declaration, I noted that the multiple would be 2.58 if one assumed that Plaintiffs would have invested their funds in the S&P 500 (dividends reinvested), during the prejudgment interest period. Steinholt Declaration, fn 2. Below I will explain my reason for including this multiple.

19. First, the S&P 500 is a commonly used benchmark for the performance of the overall U.S. stock market and is therefore relevant when examining what returns Plaintiffs would have earned had they been able to invest their funds during the prejudgment period.[15] In examining Plaintiffs' potential returns, it is important to recognize what is known and what is not known. What specific stocks, or sectors, Plaintiffs would have invested any additional funds in during the prejudgment period is not known. That reasonable investors seek to diversify their portfolio by owning more than one stock, and investing in more than one sector, is known,

---

[15] Standard & Poors: "The S&P 500® is widely regarded as the best single gauge of large cap U.S. equities. There is over USD 5.14 trillion benchmarked to the index, with index assets comprising approximately USD 1.6 trillion of this total. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization." http://www.spindices.com/indices/equity/sp-500.

although the degree to which they would have diversified is not known.[16] Consequently, the returns on a broad based U.S. market index are informative because they reflect the returns that fully diversified equity investors could have expected during the prejudgment period.

20. Second, while Plaintiffs invested in Household which operated in the financial sector, this does not mean that they only invested in financial sector stocks and did not seek to diversify their holdings by also investing in other sectors. In fact, by definition, investors who wanted to be fully diversified would also have included investments in financial sector stocks, such as Household, in their equity portfolios. Consequently, Defendants' assumption that 100% of Plaintiffs would only have invested any additional funds in financial stocks is unreasonable. It is more reasonable to assume that Plaintiffs have generally invested their funds during the prejudgment period incorporating some degree of diversification, and that any additional funds would have been invested in the same manner.

21. Third, it should be noted that during the prejudgment period, the financial sector performed exceptionally poorly, particularly in 2008, as a result of the financial crisis. Consequently, the real return adjusted for inflation during this period was negative.[17] Therefore, if one of the objectives of the prejudgment rate is to compensate Plaintiffs for their loss of purchasing power due to inflation, then the use of the S&P Financial index is inappropriate because it only provides Plaintiffs with a negative real interest rate.

---

16 In fact, investment managers have a fiduciary duty to incorporate some diversification into clients' portfolios to reduce risk (*i.e.*, avoid putting all of their clients' eggs in one basket). CFA Institute, *Standards of Practices Handbook*, (9th Ed., 2005), at 56. ("Members and candidates should diversify investments to reduce the risk of loss, unless diversification is not consistent with plan guidelines or is contrary to the account objectives.")

17 The multiplier calculated by Defendants of 1.27 is less than the 1.29 needed to keep up with inflation. Barnett Declaration, ¶5; Steinholt Declaration, fn 1.

22. As explained above, using the S&P Financial index to calculate the prejudgment interest is based on the unrealistic assumption that 100% of Plaintiffs would only have invested any additional funds in the financial sector. Nor does this measure compensate Plaintiffs for the loss of their purchasing power due to inflation.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed this 12th day of September, 2013, at San Diego, California.

Respectfully submitted,

Bjorn Steinholt

BJORN I. STEINHOLT, CFA

Exhibit A

UNITED STATES SECURITIES AND
EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2004
OR

☐ 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 1-8198

HSBC FINANCE CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**86-1052062**
(State of incorporation)	**(I.R.S. Employer Identification No.)**
2700 Sanders Road Prospect Heights, Illinois	**60070**
(Address of principal executive offices)	**(Zip Code)**

(847) 564-5000
Registrant's telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
8.875% Adjustable Conversion-Rate Equity Security Units	New York Stock Exchange
6 3/4% Notes, due May 15, 2011	New York Stock Exchange
6.875% Notes, due January 30, 2033	New York Stock Exchange
6% Notes, due November 30, 2033	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

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 ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

As of February 25, 2005, there were 50 shares of the registrant's common stock outstanding, all of which are owned by HSBC Investments

PART I

Item 1. Business.

Introduction

On March 28, 2003, Household International, Inc. (“Household”) was acquired by HSBC Holdings plc (“HSBC”) by way of merger with H2 Acquisition Corporation (“H2”), a wholly owned subsidiary of HSBC, in a purchase business combination. Following the merger, H2 was renamed “Household International, Inc.” Subsequently, HSBC transferred its ownership interest in Household to a wholly owned subsidiary, HSBC North America Holdings Inc., who subsequently contributed Household to its wholly owned subsidiary, HSBC Investments (North America) Inc.

On December 15, 2004, Household merged with its wholly owned subsidiary, Household Finance Corporation (“HFC”). Following the merger, Household changed its name to HSBC Finance Corporation. The name change was a continuation of the rebranding of the Household businesses to the HSBC brand. These actions were taken to establish a single brand in North America to create a stronger platform to advance growth across all HSBC business lines. By operation of law, following the merger, all obligations of HFC became direct obligations of HSBC Finance Corporation.

General

HSBC Finance Corporation is the principal fund raising company for its subsidiaries. Its subsidiaries primarily provide middle-market consumers with several types of loan products in the United States, the United Kingdom, Canada, the Republic of Ireland, the Czech Republic and Hungary. HSBC Finance Corporation and its subsidiaries may also be referred to in this Form 10-K as “we,” “us” or “our.” We offer real estate secured loans, auto finance loans, MasterCard* and Visa* credit card loans, private label credit card loans and personal non-credit card loans. We also initiate tax refund anticipation loans in the United States and offer specialty insurance products in the United States, United Kingdom and Canada. We generate cash to fund our businesses primarily by collecting receivable balances; issuing commercial paper, medium and long term debt; borrowing from HSBC subsidiaries and customers; securitizing and selling consumer receivables; and borrowing under secured financing facilities. We use the cash generated to invest in and support receivable growth, to service our debt obligations and to pay dividends to our parent. At December 31, 2004, we had approximately 31,500 employees and over 58 million customers.

2004 Developments

- On September 30, 2004, we commenced rebranding the Household businesses to the HSBC brand. On that date, signs on each major facility were changed to HSBC, several business units began operating under the HSBC name and all communications converted from Household to HSBC. On December 15, after Household Finance Corporation was merged into Household International, Inc., the surviving company was renamed HSBC Finance Corporation. In 2005, the rebranding efforts will continue with name changes for our Canadian branch offices and our domestic auto finance business and credit card banking subsidiary. Our branch based consumer finance business will retain the HFC and Beneficial brands, accompanied by the endorsement signature, “Member HSBC Group.” The move to a single brand in North America will promote increased awareness of HSBC, allowing all HSBC businesses in North America to align themselves to merchants and our suppliers and customers, resulting in a stronger platform for growth.

Following the merger of HFC into HSBC Finance Corporation, HSBC Finance Corporation became the principal vehicle for funding the operations of its subsidiaries. With the merger, all previous obligations of HFC became direct obligations of HSBC Finance Corporation. The merger also

* MasterCard is a registered trademark of MasterCard International, Incorporated and Visa is a registered trademark of Visa USA, Inc.

eliminates the need for separate financial statements by HFC that because of the substantial commonality of assets, were substantially the same as those of its parent, HSBC Finance Corporation.

- On December 22, 2004, our affiliate, HSBC Bank USA, National Association ("HSBC Bank USA") received regulatory approval to purchase our domestic private label portfolio, including the retained interests associated with securitized private label credit card receivables. The sale of $12.2 billion of receivables ($15.6 billion on a managed basis) occurred on December 29, 2004 at a purchase price of $12.4 billion. We retained the related account relationships and entered into an agreement to sell additional domestic private label receivables originated under current and future private label accounts to HSBC Bank USA on a daily basis. Under a separate agreement with HSBC Bank USA, we will continue to service the portfolio for a fee. In the fourth quarter, we recorded a gain from the bulk sale of the portfolio, including retained securitization interests, of $663 million ($423 million after-tax). Included in this gain was a release of $505 million of owned credit loss reserves associated with the portfolio.

  In future periods, our net interest income, fee income and provision for credit losses for private label receivables will be substantially reduced, while other income will substantially increase as reduced securitization revenue associated with private label receivables will be more than offset by gains from continuing sales of private label receivables and receipt of servicing revenue on the portfolio from HSBC Bank USA. We anticipate that the net effect of these sales could result in a reduction to our 2005 net income by up to 10%. The amount of other income recorded will be dependent upon the volume of new receivables we originate during the year and will be subject to competitive factors as we sign agreements with new merchants and extend agreements with existing merchants. We and HSBC Bank USA will consider potential sales of some of our MasterCard and Visa receivables to HSBC Bank USA in the future based on the continuing evaluation of the capital and liquidity needs at each entity.

- Upon receipt of regulatory approval for the sale of the domestic private label portfolio, we adopted charge-off and account management policies in accordance with the Uniform Retail Credit Classification and Account Management Policy issued by the Federal Financial Institutions Examination Council ("FFIEC Policies") for our domestic private label and MasterCard and Visa credit card portfolios. The adoption of FFIEC Policies resulted in a reduction to net income of approximately $121 million in the fourth quarter of 2004. We do not expect the adoption of FFIEC Policies for our domestic private label and MasterCard and Visa portfolios will have a significant impact on results of operations or cash flows in future periods.

- In the third quarter, we announced our intention to structure all new collateralized funding transactions as secured financings. Because existing public MasterCard and Visa credit card transactions were structured as sales to revolving trusts that require replenishments of receivables to support previously issued securities, receivables will continue to be sold to the credit card trusts until the revolving periods end, the last of which is expected to occur in early 2008 based on current projections. Private label trusts that publicly issued securities will now be replenished by HSBC Bank USA as a result of the daily sale of new domestic private label credit card originated to HSBC Bank USA. We will continue to replenish, at reduced levels, certain non-public personal non-credit card and MasterCard and Visa securities issued to conduits and record the resulting replenishment gains for a period of time in order to manage liquidity. Termination of gain on sale treatment for new collateralized funding activity reduced our reported net income under U.S. GAAP in 2004 and will continue to in future periods. In 2004, our net interest-only strip receivables, excluding both the mark-to-market adjustment recorded in accumulated other comprehensive income and the private label portion purchased by HSBC Bank USA, decreased $466 million. There was no impact in 2004, however, on cash received from operations or on U.K. GAAP reported results.

- Funding synergies resulting from our acquisition by HSBC have continued to reduce our reliance on traditional sources to fund our growth. Because we are now a subsidiary of HSBC, our credit spreads relative to Treasuries have tightened compared to those we experienced during the months leading up to the announcement of our acquisition by HSBC. Primarily as a result of these tightened credit spreads, reduced liquidity requirements and lower costs due to shortening the maturity of our liabilities, principally through increased issuance of commercial paper, we recognized cash funding expense savings of approximately $350 million in 2004 and $125 million in 2003 compared to the funding costs we would have incurred using average spreads from the first half of 2002. It is anticipated that these tightened credit spreads and other funding synergies including asset transfers will eventually enable HSBC to realize annual cash funding expense savings, including external fee savings, in excess of $1 billion per year as our existing term debt matures over the course of the next few years.

  In April 2004, Fitch Ratings revised our Rating Outlook to Positive from Stable and raised our Support Rating to “1” from “2”. In July 2004, Fitch Ratings raised our Senior Debt Rating to “A+” from “A” and raised our Senior Subordinated Debt Rating and our Preferred Stock Rating to “A” from “A-”. In December 2004, Fitch Ratings again raised our Senior Debt Rating to “AA-” from “A+” and our commercial paper rating to “F1+.” Also in December 2004, Moody’s Investor Service revised our rating outlook to A1 Positive from A1 Stable.

Restatement

HSBC Finance Corporation has restated its consolidated financial statements for the previously reported quarterly periods ended March 31, 2004, June 30, 2004 and September 30, 2004; and the period March 29, 2003 through December 31, 2003. This Form 10-K and the exhibits included herewith include all adjustments relating to the restatement for all such prior periods. Amended Forms 10-Q for the periods ended March 31, 2004, June 30, 2004 and September 30, 2004 that reflect adjustments relating to the restatement will be filed with the Securities and Exchange Commission on or before March 31, 2005.

During the fourth quarter of 2004, as part of HSBC Finance Corporation’s preparation for the implementation of International Financial Reporting Standards (“IFRS”) by HSBC from January 1, 2005, we undertook a review of our hedging activities to confirm conformity with the accounting requirements of IFRS, which differ in several respects from the hedge accounting requirements under U.S. GAAP as set out in Statement of Financial Accounting Standards No. 133, “Accounting for Derivative Instruments and Hedging Activities,” (“SFAS 133”). As a result of this review, management determined that there were some deficiencies in the documentation required to support hedge accounting under U.S. GAAP. These documentation deficiencies arose following our acquisition by HSBC. As a consequence of the acquisition, pre-existing hedging relationships, including hedging relationships that had previously qualified under the “shortcut” method of accounting pursuant to SFAS 133, were required to be reestablished. At that time there was some debate in the accounting profession regarding the detailed technical requirements resulting from a business combination. We consulted with our independent accountants, KPMG LLP, in reaching a determination of what was required in order to comply with SFAS 133. Following this, we took the actions we believed were necessary to maintain hedge accounting for all of our historical hedging relationships in our consolidated financial statements for the period ended December 31, 2003 and those consolidated financial statements received an unqualified audit opinion.

Management, having determined during the fourth quarter of 2004 that there were certain documentation deficiencies, engaged independent expert consultants to advise on the continuing effectiveness of the identified hedging relationships and again consulted with our independent accountants, KPMG LLP. As a result of this assessment, we concluded that a substantial number of our hedges met the correlation effectiveness requirement of SFAS 133 throughout the period following our acquisition by HSBC. However, we also determined in conjunction with KPMG LLP that, although a substantial number of the impacted hedges satisfied the correlation effectiveness requirement of SFAS 133, there were technical deficiencies in the

documentation that could not be corrected retroactively or disregarded notwithstanding the proven effectiveness of the hedging relationships in place and, consequently, that the requirements of SFAS 133 were not met and that hedge accounting was not appropriate during the period these documentation deficiencies existed. We have therefore determined that we should restate all the reported periods since our acquisition by HSBC to eliminate hedge accounting on all hedging relationships outstanding at March 29, 2003 and certain fair value swaps entered into after that date. During the period from acquisition through December 31, 2004, we are reporting net income of $3.3 billion. The cumulative impact of the loss of hedge accounting during this period is to increase reported net income by $113 million.

conditions, overall capital markets volatility and the effectiveness of our management of credit risks inherent in our customer base.

The merger with HSBC has improved our access to the capital markets and lowered our funding costs. In addition to providing several important sources of direct funding, our affiliation with HSBC is also expanding our access to a worldwide pool of potential investors. While these new funding synergies have reduced our reliance on traditional sources to fund our growth, we are focused on balancing our use of affiliate and third-party funding sources to minimize funding expense while maximizing liquidity. Because we are now a subsidiary of HSBC and our credit ratings have improved, our credit spreads relative to Treasuries have tightened relative to those we experienced during the months leading up to the announcement of our acquisition by HSBC. Primarily as a result of these tightened credit spreads, reduced liquidity requirements and lower costs due to shortening the maturity of our liabilities mainly through the issuance of commercial paper, we recognized cash funding expense savings of approximately $350 million in 2004 and $125 million in 2003 compared to the funding costs we would have incurred using average spreads from the first half of 2002. It is anticipated that these tightened credit spreads and other funding synergies including assets transfers will

eventually enable HSBC to realize annual cash funding expense savings, including external fee savings, in excess of $1 billion per year as our existing term debt matures over the course of the next few years.

For a detailed listing of the ratings that have been assigned to HSBC Finance Corporation and our significant subsidiaries as of December 31, 2004, see Exhibit 99.1 to this Form 10-K.

We fund our operations globally and domestically, using a combination of capital market and affiliate debt, preferred equity, securitizations and sales of consumer receivables and borrowings under secured financing facilities. We will continue to fund a large part of our operations in the global capital markets, primarily through the use of secured financings, commercial paper, medium-term notes and long-term debt. We will also continue to sell certain receivables to HSBC Bank USA. We will continue to use derivative financial instruments to hedge our currency and interest rate risk exposure. A description of our use of derivative financial instruments, including interest rate swaps and foreign exchange contracts, and other quantitative and qualitative information about our market risk is set forth in Item 7. “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (“2004 MD&A”) under the caption “Risk Management” and Note 16 of our consolidated financial statements (“2004 Financial Statements”).

Additional information on our sources and availability of funding are set forth in the “Liquidity and Capital Resources” and “Off Balance Sheet Arrangements” sections of our 2004 MD&A.

Regulation and Competition

Regulation

Consumer Lending. Our consumer finance businesses operate in a highly regulated environment. These businesses are subject to laws relating to consumer protection, discrimination in extending credit, use of credit reports, privacy matters, disclosure of credit terms and correction of billing errors. They also are subject to certain regulations and legislation that limit operations in certain jurisdictions. For example, limitations may be placed on the amount of interest or fees that a loan may bear, the amount that may be borrowed, the types of actions that may be taken to collect or foreclose upon delinquent loans or the information about a customer that may be shared. Our consumer branch lending offices are generally licensed in those jurisdictions in which they operate. Such licenses have limited terms but are renewable, and are revocable for cause. Failure to comply with these laws and regulations may limit the ability of our licensed lenders to collect or enforce loan agreements made with consumers and may cause our lending subsidiaries to be liable for damages and penalties.

There also continues to be a significant amount of legislative activity, nationally, locally and at the state level, aimed at curbing lending practices deemed to be “predatory”. In addition, states have sought to alter lending practices through consumer protection actions brought by state attorneys general and other state regulators. Legislative activity in this area is expected to continue targeting certain abusive practices such as loan “flipping” (making a loan to refinance another loan where there is no tangible benefit to the borrower), fee “packing” (addition of unnecessary, unwanted and unknown fees to a borrower), “equity stripping” (lending without regard to the borrower’s ability to repay or making it impossible for the borrower to refinance with another lender), and outright fraud. HSBC Finance Corporation does not condone or endorse any of these practices. We continue to work with regulators and consumer groups to create appropriate safeguards to avoid these abusive practices while allowing our borrowers to continue to have access to credit for personal purposes, such as the purchase of homes, automobiles and consumer goods. As part of this effort we have adopted a set of lending best practice initiatives. Increased legislative and regulatory focus is also expected on tax refund anticipation loans. It is possible that broad legislative initiatives will be passed which will impose additional costs and rules on our businesses. Although we have the ability to react quickly to new laws and regulations, it is too early to estimate the effect, if any, these activities will have on us in a particular locality or nationally.

Banking Institutions. Our credit card banking subsidiary, Household Bank (SB), N.A. ("Household Bank"), is a nationally-chartered 'credit card bank' which is also a member of the federal reserve system. Household

Bank is subject to regulation, supervision and examination by the Office of the Comptroller of the Currency ("OCC"). The deposits of Household Bank are insured by the FDIC, which renders it subject to relevant FDIC regulation.

As a result of our acquisition by HSBC, HSBC Finance Corporation and its subsidiaries became subject to supervision, regulation and examination by the Board of Governors of the Federal Reserve Board (the "Federal Reserve Board"). HSBC is a bank holding company under the U.S. Bank Holding Company Act of 1956 (the "BHCA") as a result of its ownership of HSBC Bank USA. On January 1, 2004, HSBC formed a new company to hold all of its North American operations, including HSBC Finance Corporation and its subsidiaries. This company, HSBC North American Holdings Inc. ("HNAH") is also a "bank holding company" under the BHCA, by virtue of its ownership and control of HSBC Bank USA. HSBC and HNAH are registered as financial holding companies ("FHC") under the Gramm-Leach-Bliley Act amendments to the BHCA, enabling them to offer a more complete line of financial products and services.

The United States is a party to the 1988 Basel Capital Accord and U.S. banking regulatory authorities have adopted risk-based capital requirements for United States banks and bank holding companies that are generally consistent with the Accord. In addition, U.S. bank regulatory authorities have adopted 'leverage' capital requirements that generally require United States banks and bank holding companies to maintain a minimum amount of capital in relation to their balance sheet assets (measured on a non-risk-weighted basis). Household Bank is subject to these capital requirements.

Household Bank, like other FDIC-insured banks, may be required to pay assessments to the FDIC for deposit insurance under the FDIC's Bank Insurance Fund. Under the FDIC's risk-based system for setting deposit insurance assessments, an institution's assessments vary according to the level of capital an institution holds, its deposit levels and other factors.

The Federal Deposit Insurance Corporation Improvement Act of 1991 provides for extensive regulation of depository institutions such as Household Bank, including requiring federal banking regulators to take 'prompt corrective action' with respect to FDIC-insured banks that do not meet minimum capital requirements. At December 31, 2004, Household Bank was well-capitalized under applicable OCC and FDIC regulations.

Our principal United Kingdom subsidiary (HFC Bank Limited, formerly known as HFC Bank plc) is subject to oversight and regulation by the U.K. Financial Services Authority ("FSA") and the Central Bank Financial Services Authority of Ireland. We have indicated our intent to the FSA to maintain the regulatory capital of this institution at specified levels. We do not anticipate that any capital contribution will be required for our United Kingdom bank in the near term. In the Republic of Ireland we are regulated by the Irish Financial Services Regulatory Authority. In May 2005, new consumer protection laws will be effective in the U.K. that may impact profitability and operations. These changes will not have a material impact on our results.

We also maintain a trust company in Canada, which is subject to regulatory supervision by the Office of the Superintendent of Financial Institutions.

Insurance. Our credit insurance business is subject to regulatory supervision under the laws of the states and provinces in which it operates. Regulations vary from state to state, and province to province, but generally cover licensing of insurance companies, premium and loss rates, dividend restrictions, types of insurance that may be sold, permissible investments, policy reserve requirements, and insurance marketing practices.

Our insurance operations in the United Kingdom are subject to regulatory supervision by the FSA.

Competition

Total domestic	**$ 94,512**	$ 82,496	$ 75,303	$ 73,905	$ 60,837
Foreign:					
Real estate secured	**$ 2,874**	$ 2,195	$ 1,679	$ 1,383	$ 1,260
Auto finance	**54**	-	-	-	-
MasterCard/ Visa	**2,264**	1,605	1,319	1,174	2,207
Private label	**3,070**	2,872	1,974	1,811	1,675
Personal non-credit card	**4,079**	3,208	2,285	1,600	1,378
Commercial and other	**2**	2	2	2	2
Total foreign	**$ 12,343**	$ 9,882	$ 7,259	$ 5,970	$ 6,522
Total owned receivables:					
Real estate secured	**$ 64,820**	$ 51,221	$ 45,819	$ 43,857	$ 35,180
Auto finance	**7,544**	4,138	2,024	2,369	1,851
MasterCard/ Visa	**14,635**	11,182	8,947	8,141	8,054
Private label	**3,411**	12,604	11,339	11,664	10,347
Personal non-credit card	**16,128**	12,832	13,970	13,337	11,328
Commercial and other	**317**	401	463	507	599
Total owned receivables	**$ 106,855**	$ 92,378	$ 82,562	$ 79,875	$ 67,359
Deposits	**$ 47**	$ 232	$ 821	$ 6,562	$ 8,677
Commercial paper, bank and other borrowings	**9,013**	9,122	6,128	12,024	10,788
Due to affiliates(4)	**13,789**	7,589	-	-	-
Long term debt	**85,378**	79,632	75,751	57,799	45,728
Preferred stock(5)	**1,100**	1,100	1,193	456	164
Common shareholder's(s') equity(6)	**15,841**	16,391	9,222	7,843	7,667
Owned Basis Selected Financial Ratios					
Common and preferred equity to owned assets	**13.01%**	14.69%	10.64%	9.33%	10.26%
Consumer two-month-and-over contractual delinquency	**4.07**	5.36	5.34	4.43	4.19
Reserves as a percent of receivables	**3.39**	4.11	4.04	3.33	3.14
Reserves as a percent of nonperforming loans	**103.0**	93.7	94.5	92.7	91.1
Managed Basis Balance Sheet Data and Selected Financial Ratios(2)					
Total assets	**$ 144,415**	$ 145,253	$ 122,794	$ 109,859	$ 96,558
Managed receivables:(3)					
Real estate secured	**$ 64,901**	$ 51,415	$ 46,275	$ 44,719	$ 36,638
Auto finance	**10,223**	8,813	7,442	6,395	4,563
MasterCard/ Visa	**22,218**	21,149	18,953	17,395	17,584
Private label	**3,411**	17,865	14,917	13,814	11,997
Personal non-credit card	**20,010**	18,936	19,446	17,993	16,227
Commercial and other	**317**	401	463	507	599
Total managed receivables	**$ 121,080**	$ 118,579	$ 107,496	$ 100,823	$ 87,608
Tangible shareholder's(s') equity to tangible managed assets ("TETMA")(7)	**6.68%**	7.03%	9.08%	7.57%	7.13%
Tangible shareholder's(s') equity plus owned loss reserves to tangible managed assets ("TETMA + Owned Reserves")(7)	**9.45**	9.89	11.87	10.03	9.36
Tangible common equity to tangible managed assets(7)	**4.67**	5.04	6.83	6.24	6.25
Excluding purchase accounting adjustments:					
TETMA	**8.34**	8.90	8.90	7.57	7.13
TETMA + Owned Reserves	**11.12**	11.77	11.87	10.03	9.36
Tangible common equity to tangible managed assets	**6.35**	6.94	6.83	6.24	6.25
Risk adjusted revenue	**7.30**	7.18	7.18	7.64	7.40
Consumer two-month-and-over contractual delinquency	**4.24**	5.39	5.24	4.46	4.20
Reserves as a percent of receivables	**3.73**	5.20	4.74	3.78	3.65
Reserves as a percent of nonperforming loans	**108.4**	118.0	112.6	105.0	107.0

(1) The following table, which contains non-GAAP financial information is provided for comparison of our operating trends only and should be read in conjunction with our owned basis GAAP financial information. For 2004, the operating trends, percentages and ratios presented below exclude the $121 million decrease in net income relating to the adoption of Federal Financial Institutions Examination Council ("FFIEC") charge-off policies for our domestic private label and MasterCard/ Visa receivables and the $423 million (after-tax) gain on the bulk sale of domestic private label receivables to an affiliate, HSBC Bank USA, National Association ("HSBC

Bank USA”). For 2003, the operating results, percentages and ratios exclude $167 million (after-tax) of HSBC acquisition related costs and other merger related items and for 2002, exclude the $333 million (after-tax) settlement charge and related expenses and the $240 million (after-tax) loss on disposition of Thrift assets and deposits. See “Basis of Reporting” and “Reconciliations to GAAP Financial Measures” in Management’s Discussion and Analysis for additional discussion and quantitative reconciliations to the equivalent GAAP basis financial measure.

Year ended December 31,	2004 (Successor)	2003 (Combined) (Restated)	2002 (Predecessor)	2001 (Predecessor)	2000 (Predecessor)
			(dollars are in millions)		
Operating net income	**$ 1,638**	$ 1,770	$ 2,131	$ 1,848	$ 1,631
Return on average owned assets	**1.32%**	1.61%	2.21%	2.26%	2.35%
Return on average common shareholder’s(s’) equity	**9.2**	11.9	23.9	24.1	23.2
Owned basis consumer net charge-off ratio	**3.84**	4.06	3.81	3.32	3.18
Managed basis consumer net charge-off ratio	**4.44**	4.67	4.28	3.73	3.64
Owned basis efficiency ratio	**43.4**	41.0	36.3	38.4	39.6
Return on average managed assets	**1.12**	1.32	1.80	1.82	1.85
Managed basis efficiency ratio	**42.9**	34.1	30.8	34.3	34.5

(2) We monitor our operations and evaluate trends on both an owned basis as shown in our financial statements and on a managed basis. Managed basis reporting (a non-GAAP financial measure) assumes that securitized receivables have not been sold and are still on our balance sheet. Managed basis information is intended to supplement, and should not be considered a substitute for, owned basis reporting and should be read in conjunction with reported owned basis results. See “Basis of Reporting” and “Reconciliations to GAAP Financial Measures” for additional discussion and quantitative reconciliations to the equivalent GAAP basis financial measure.

(3) In 2004, we sold $.9 billion of higher quality non-conforming real estate secured receivables and sold our domestic private label receivable portfolio of $12.2 billion ($15.6 billion on a managed basis) to HSBC Bank USA. In 2003, we sold $2.8 billion of higher quality non-conforming real estate secured receivables to HSBC Bank USA and acquired owned basis private label portfolios totaling $1.2 billion ($1.6 billion on a managed basis) and MasterCard and Visa portfolios totaling $.9 billion. In 2002, we sold $6.3 billion of real estate secured whole loans from our consumer lending and mortgage services businesses and purchased a $.5 billion private label portfolio. In 2001, we sold approximately $1 billion of MasterCard and Visa receivables as a result of discontinuing our participation in the Goldfish credit card program and purchased a $.7 billion private label portfolio. In 2000, we acquired real estate secured portfolios totaling $3.7 billion.

(4) As of December 31, 2004, we had received $35.7 billion in HSBC related funding. As of December 31, 2003, we had received $14.7 billion in HSBC related funding. See Liquidity and Capital Resources for the components of this funding.

(5) In conjunction with the acquisition by HSBC, our 7.625%, 7.60%, 7.50% and 8.25% preferred stock was converted into the right to receive cash which totaled approximately $1.1 billion. In consideration of HSBC transferring sufficient funds to make these payments, we issued Series A preferred stock to HSBC on March 28, 2003. Also on March 28, 2003, we called for redemption our $4.30, $4.50 and 5.00% preferred stock. In September 2004, HSBC North America Holdings Inc. (“HNAH”) issued a new series of preferred stock to HSBC in exchange for our Series A preferred stock. In October 2004, HSBC Investments (North America) Inc. (“HINO”) issued a new series of preferred stock to HNAH in exchange for our Series A preferred stock.

(6) Common shareholder’s equity at December 31, 2004 and 2003 reflects push-down accounting adjustments resulting from the HSBC merger.

(7) TETMA, TETMA + Owned Reserves and tangible common equity to tangible managed assets are non-GAAP financial ratios that are used by HSBC Finance Corporation management or certain rating agencies as a measure to evaluate capital adequacy and may differ from similarly named measures presented by other companies. See “Basis of Reporting” for additional discussion on the use of non-GAAP financial measures and “Reconciliations to GAAP Financial Measures” for quantitative reconciliations to the equivalent GAAP basis financial measure.

(8) In December 2004, we adopted charge-off and account management policies in accordance with the Uniform Retail Credit Classification and Account Management Policy issued by the FFIEC for our domestic private label and MasterCard and Visa portfolios. The adoption of the FFIEC charge-off policies resulted in a reduction to net income of $121 million. See “Credit Quality” in Management’s Discussion and Analysis and Note 5, “Sale of Domestic Private Label Receivable Portfolio and Adoption of FFIEC Policies,” in the accompanying consolidated financial statements for further discussion of these policy changes.

(9) The adoption of FFIEC charge-off policies for our domestic private label and MasterCard and Visa portfolios and subsequent sale of the domestic private label portfolio in December 2004 have negatively impacted these ratios. Reserves as a percentage of net charge-offs excluding domestic private label charge-offs in 2004 and the impact of adopting FFIEC charge-off policies for these portfolios was 109.2 percent on an owned basis and 96.0 percent on a managed basis.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Restatement

HSBC Finance Corporation has restated its consolidated financial statements for the previously reported quarterly periods ended March 31, 2004, June 30, 2004 and September 30, 2004; and the period March 29, 2003 through December 31, 2003. This Form 10-K and the exhibits included herewith include all adjustments relating to the restatement for all such prior periods. Amended Forms 10-Q for the periods ended March 31, 2004, June 30, 2004 and September 30, 2004 that reflect adjustments relating to the restatement will be filed with the Securities and Exchange

America Holdings Inc. ("HNAH") which is a wholly owned subsidiary of HSBC Holdings plc ("HSBC"). HSBC Finance Corporation may also be referred to in Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") as "we", "us", or "our".

On September 30, 2004, Household International, Inc. ("Household") commenced the rebranding of the majority of its U.S. and Canadian businesses to the HSBC brand. Businesses previously operating under the Household name are now called HSBC. Our branch-based consumer lending business has retained the HFC and Beneficial brands, accompanied by the HSBC Group's endorsement signature, "Member HSBC Group." The single brand allows HSBC in North America to better align its businesses, providing a stronger platform to service customers and advance growth. The HSBC brand also positions us to expand the products and services offered to our customers. As part of this initiative, we merged with our subsidiary, Household Finance Corporation, and changed our name to HSBC Finance Corporation in December 2004.

HSBC Finance Corporation provides middle-market consumers with real estate secured loans, auto finance loans, MasterCard* and Visa* credit card loans, private label credit card loans and personal non-credit card loans in the United States, the United Kingdom, Canada, the Republic of Ireland, the Czech Republic and Hungary. We also initiate tax refund anticipation loans in the United States and offer credit and specialty insurance products in the United States, the United Kingdom and Canada. We generate cash to fund our businesses primarily by collecting receivable balances; issuing commercial paper, medium and long term debt; borrowing from HSBC subsidiaries and customers; securitizing and selling consumer receivables and borrowing under secured financing facilities. We use the cash generated to invest in and support receivable growth, to service our debt obligations and to pay dividends to our parent.

* MasterCard is a registered trademark of MasterCard International, Incorporated and Visa is a registered trademark of Visa USA, Inc.

The acquisition by HSBC on March 28, 2003 resulted in a new basis of accounting reflecting the fair market value of our assets and liabilities for the "successor" periods beginning March 29, 2003. Information for all "predecessor" periods prior to the merger is presented using our historical basis of accounting, which impacts comparability to our "successor" periods beginning March 29, 2003. During 2003, the "predecessor" period contributed $246 million of net income and the "successor" period contributed $1.4 billion of net income. To assist in the comparability of our financial results and to make it easier to discuss and understand our results of operations, Management's Discussion and Analysis combines the "predecessor period" (January 1 to March 28, 2003) with the "successor period" (March 29 to December 31, 2003) to present "combined" results for the year ended December 31, 2003.

In addition to owned basis reporting, we also monitor our operations and evaluate trends on a managed basis (a non-GAAP financial measure), which assumes that securitized receivables have not been sold and are still on our balance sheet. See "Basis of Reporting" for further discussion of the reasons we use this non-GAAP financial measure.

Performance, Developments and Trends

Our net income was $1.9 billion in 2004, $1.6 billion in 2003 and $1.6 billion in 2002. In measuring our results, management's primary focus is on managed receivable growth and operating net income (a non-GAAP financial measure which excludes certain nonrecurring items). See "Basis of Reporting" for further discussion of operating net income. Operating net income was $1.6 billion in 2004 compared to $1.8 billion in 2003 and $2.1 billion in 2002. Operating net income declined in 2004 primarily due to higher operating expenses and higher provision for credit losses due to receivables growth, partially offset by higher net interest income and higher other revenues. Operating expenses increased due to receivables growth, increases in marketing expenses and higher amortization of intangibles which were established in connection with our acquisition by HSBC. Other revenues increased due to higher derivative income and higher fee and other income, partially offset by lower securitization revenue due to reduced securitization activity. The increase in net interest income was due to higher average receivable balances partially offset by lower yields on our receivables, particularly in real estate secured, auto finance and personal non-credit card receivables, and by higher interest expense. Interest expense was higher in 2004 resulting from a larger balance sheet, partially offset by a lower cost of funds. Amortization of purchase accounting fair value adjustments increased net income by $128 million in 2004 compared to $92 million in 2003.

Operating net income declined in 2003 compared to 2002 due to higher operating expenses to support receivable growth; increased legal and compliance costs; higher amortization of intangibles; lower initial securitization activity as a result of the use of alternative funding sources and higher provision for credit losses as a result of higher charge-offs partially offset by higher net interest margin and fee income due to receivable growth, higher derivative income and lower funding costs.

Owned receivables increased to $106.9 billion at December 31, 2004, a 16 percent increase from December 31, 2003. Excluding the impact of the sale of our domestic private label portfolio, owned receivables grew 29 percent in 2004 as we experienced growth in all our receivable products with real estate secured receivables being the primary contributor of the growth. Real estate secured receivable levels reflect sales to HSBC Bank USA in 2004 and 2003 and purchases of correspondent receivables directly by HSBC Bank USA of $2.8 billion during 2004, a portion of which we otherwise would have purchased. Lower securitization levels also contributed to the increase in owned receivables in 2004.

Because HSBC reports results on a U.K. GAAP basis, management also separately monitors earnings excluding goodwill amortization and net income under U.K. GAAP (non-GAAP financial measures). The following table summarizes U.K. GAAP results:

	Year ended December 31, 2004	March 29 through December 31, 2003
	(in millions)	
Earnings excluding goodwill amortization – U.K. GAAP basis	**$ 3,105**	$ 1,768
Net income – U.K. GAAP basis	**2,584**	1,387

Credit Quality

Our owned basis two-months-and-over contractual delinquency ratio in 2004 decreased from 5.36 percent to 4.07 percent compared to 2003. The decrease is consistent with the improvements in early delinquency trends we began to experience in the fourth quarter of 2003 as a result of improvements in the economy, better underwriting standards and improved credit quality of originations. Dollars of delinquency in 2004 decreased compared to 2003 due to the adoption of FFIEC charge-off policies for our domestic private label and MasterCard and Visa portfolios and the subsequent bulk sale of the domestic private label receivable portfolio in December 2004, partially offset by higher levels of receivables in 2004. Excluding these factors, dollars of delinquency would have increased only modestly despite significant growth in our owned portfolios as improvements in credit quality were more than offset by growth as securitized levels declined and our interest in the receivables of certain securitization trusts increased.

Net charge-offs as a percentage of average consumer receivables for 2004 decreased 6 basis points over 2003 despite being negatively impacted by a charge-off of $158 million related to the adoption of FFIEC Policies in the fourth quarter of 2004 as discussed above. Excluding the charge-off associated with the adoption of FFIEC Policies, net charge-offs as a percentage of average consumer receivables would have decreased 22 basis points in 2004. The lower delinquency levels we have been experiencing as a result of an improving economy as well as the impact of improved collection activities and higher levels of average receivables are having a positive impact on net charge-offs.

During 2004, our credit loss reserves decreased as a result of the bulk sale of our domestic private label receivables to HSBC Bank USA. Excluding this sale, owned credit loss reserves would have increased in 2004 reflecting growth in our loan portfolio, including lower securitization levels which result in our interest in the receivables of certain securitization trusts to increase, partially offset by improved credit quality.

Funding and Capital

During 2004, we were less reliant on third party debt and securitization funding as we used proceeds from the sales of real estate secured and private label receivables to HSBC Bank USA and debt issued to affiliates to assist in the funding of our businesses. Because we are now a subsidiary of HSBC, our credit ratings have improved and our credit spreads relative to Treasuries have tightened compared to those we experienced during the months leading up to the announcement of our acquisition by HSBC. Primarily as a result of these tightened credit spreads, reduced liquidity requirements and lower costs due to shortening the maturity of our liabilities, principally through increased issuance of commercial paper, we recognized cash funding expense savings in excess of approximately $350 million in 2004 and $125 million in 2003 compared to the funding costs we would have incurred using average spreads from the first half of 2002. It is anticipated that these tightened credit spreads and other funding synergies including asset transfers will eventually enable HSBC to realize annual cash funding expense savings, including external fee savings, in excess of $1 billion per year as our existing term debt matures over the course of the next few years.

Securitization of consumer receivables has been a source of funding and liquidity for us. Under U.K. GAAP as currently reported by HSBC, our securitizations are treated as secured financings. In order to align our accounting treatment with that of HSBC under U.K. GAAP (and beginning in 2005 International Financial

Reporting Standards), we began to structure all new collateralized funding transactions as secured financings in the third quarter of 2004. However, because existing public MasterCard and Visa credit card transactions were structured as sales to revolving trusts that require replenishments of receivables to support previously issued securities, receivables will continue to be sold to these trusts until the revolving periods end, the last of which is expected to occur in early 2008 based on current projections. Private label trusts that publicly issued securities will now be replenished by HSBC Bank USA as a result of the daily sale of new domestic private label credit card originations to HSBC Bank USA. We will continue to replenish at reduced levels, certain non-public personal non-credit card and MasterCard and Visa securities issued to conduits and record the resulting replenishment gains for a period of time in order to manage liquidity. Since our securitized receivables have varying lives, it will take several years for these receivables to pay-off and the related interest-only strip receivables to be reduced to zero. The termination of sale treatment on new collateralized funding activity reduced our reported net income under U.S. GAAP. In 2004, our net interest-only strip receivables, See "Credit Quality Statistics" for further information regarding owned basis and managed basis delinquency, charge-offs and nonperforming loans.

The amount of domestic and foreign managed receivables in forbearance, modification, credit card services approved consumer credit counseling accommodations, rewrites or other customer account management techniques for which we have reset delinquency and that is not included in the restructured or delinquency statistics was approximately $.4 billion or .4 percent of managed receivables at December 31, 2004 compared with $1.0 billion or .9 percent of managed receivables at December 31, 2003. For periods prior to June 30, 2004, all credit card approved consumer credit counseling accommodations are included in the reported statistics in this paragraph. As a result of our system enhancements, we are now able to segregate which credit card approved consumer credit counseling accommodations included resetting the contractual delinquency status to current after January 1, 2003. Such accounts are included in the December 31, 2004 restructure statistics in the table above. Credit card credit counseling accommodations that did not include resetting contractual delinquency status are not reported in the table above or the December 31, 2004 statistics in this paragraph.

Geographic Concentrations The state of California accounts for 12 percent of our domestic owned portfolio. No other state accounts for more than 10 percent of either our domestic owned or managed portfolio. Because of our centralized underwriting, collections and processing functions, we can quickly change our credit standards and intensify collection efforts in specific locations. We believe this lowers risks resulting from such geographic concentrations.

Our foreign consumer operations located in the United Kingdom and the rest of Europe accounted for 9 percent of owned consumer receivables and Canada accounted for 2 percent of owned consumer receivables at December 31, 2004.

Liquidity and Capital Resources

While the funding synergies resulting from our acquisition by HSBC have allowed us to reduce our reliance on traditional sources to fund our growth, our continued success and prospects for growth are dependent upon access to the global capital markets. Numerous factors, internal and external, may impact our access to and the costs associated with issuing debt in these markets. These factors may include our debt ratings, overall capital markets volatility and the impact of overall economic conditions on our business. We continue to focus on balancing our use of affiliate and third-party funding sources to minimize funding expense while maximizing liquidity. As discussed below, we decreased our reliance on third-party debt and initial securitization funding during 2004 as we used proceeds from the sales of real estate secured receivables and our domestic private label receivable portfolio to HSBC Bank USA, debt issued to affiliates and additional secured financings to assist in the funding of our businesses.

Because we are now a subsidiary of HSBC, our credit spreads relative to Treasuries have tightened compared to those we experienced during the months leading up to the announcement of our acquisition by HSBC. Primarily as a result of these tightened credit spreads, reduced liquidity requirements and lower costs due to shortening the maturity of our liabilities, principally through increased issuance of commercial paper, we recognized cash funding expense savings of approximately $350 million in 2004 and $125 million in 2003 compared to the funding costs we would have incurred using average spreads from the first half of 2002. It is anticipated that these tightened credit spreads and other funding synergies including asset transfers will eventually enable HSBC to realize annual cash funding expense savings, including external fee savings, in excess of $1 billion per year as our existing term debt matures over the course of the next few years. The portion of these savings to be realized by HSBC Finance Corporation will depend in large part upon the amount and timing of various initiatives between HSBC Finance Corporation and HSBC subsidiaries. Amortization of purchase accounting fair value adjustments to our external debt obligations as a result of the HSBC merger, reduced interest expense by $901 million in 2004 and $773 million in 2003.

Debt due to affiliates and other HSBC related funding are summarized in the following table:

December 31,	2004	2003
	(in billions	
Debt outstanding to HSBC subsidiaries:		
Domestic short-term borrowings	$ -	$ 2.6

Drawings on bank lines in the U.K. and Europe	**7.5**	3.4
Term debt	**6.0**	1.3
Preferred securities issued by Household Capital Trust VIII to HSBC	**.3**	.3
Total debt outstanding to HSBC subsidiaries	**13.8**	7.6
Debt outstanding to HSBC clients:		
Euro commercial paper	**2.6**	2.8
Term debt	**.8**	.4
Total debt outstanding to HSBC clients	**3.4**	3.2
Preferred stock held by HINO (held by HSBC at December 31, 2003)	**1.1**	1.1
Cash received on sale of domestic private label credit card portfolio to HSBC Bank USA	**12.4**	-
Real estate secured receivable activity with HSBC Bank USA:		
Cash received on sales (cumulative)	**3.7**	2.8
Direct purchases from correspondents (cumulative)	**2.8**	-
Reductions in real estate secured receivables sold to HSBC Bank USA	**(1.5)**	-
Total real estate secured receivable activity with HSBC Bank USA	**5.0**	2.8
Total HSBC related funding	**$ 35.7**	$ 14.7

At December 31, 2004, funding from HSBC, including debt issuances to HSBC subsidiaries and clients and preferred stock held by HINO, represented fifteen percent of our total managed debt and preferred stock funding. At December 31, 2003, funding from HSBC, including debt issuances to HSBC subsidiaries and clients and preferred stock held by HSBC, represented ten percent of our total managed debt and preferred stock funding.

Proceeds from the December 2004 domestic private label bulk receivable sale to HSBC Bank USA of $12.4 billion were used to pay down short-term domestic borrowings, including outstanding commercial paper balances, and to fund operations. Excess liquidity from the sale was used to temporarily fund available for sale investments. Proceeds from the December 2003 sale of $2.8 billion of real estate secured loans to HSBC Bank USA, which at year-end 2003 had been temporarily held as securities available for sale, were used to pay-down domestic short-term borrowings in the first quarter of 2004. Proceeds from the March 2004 real estate secured receivable sale were used to pay-down commercial paper balances which had been used as temporary funding in the first quarter of 2004 and to fund various debt maturities.

As of December 31, 2004, we had revolving credit facilities of $2.5 billion from HSBC domestically and $7.5 billion from HSBC subsidiaries in the U.K. which was increased to $8.0 billion in early 2005. A $4.0 billion revolving credit facility with HSBC Private Bank (Suisse) SA, which was new in 2004, expired on December 30, 2004. At December 31, 2004, $7.4 billion was outstanding under the U.K. lines and no balances were outstanding under the domestic lines. As of December 31, 2003, $3.4 billion was outstanding on the U.K. lines and no balances were outstanding on the domestic lines. We had derivative contracts with a notional value of $62.6 billion, or approximately 87 percent of total derivative contracts, outstanding with HSBC affiliates at December 31, 2004. At December 31, 2003, we had derivative contracts with a notional value of $39.7 billion, or approximately 58 percent of total derivative contracts, outstanding with HSBC affiliates.

Securities totaled $4.3 billion at December 31, 2004 and $11.1 billion at December 31, 2003. Additionally at December 31, 2004, we had $2.7 billion of securities purchased under agreements to resell. Included in the December 31, 2003 balance was $2.4 billion dedicated to our credit card bank. In 2004, the investment levels dedicated to our credit card bank were eliminated as a result of the funding and capital synergies resulting from our acquisition by HSBC. Our securities balance at the end of 2003 was also unusually high as a result of the cash received from the sale of $2.8 billion in real estate secured loans to HSBC Bank USA on December 31, 2003. Given the timing of the bulk sale of the domestic private label receivables to HSBC Bank USA on December 29, 2004, there was excess funding at December 31, 2004 even after paying down certain debt obligations prior to year end. These remaining excess funds will be used to fund future asset growth.

Commercial paper, bank and other borrowings totaled $9.0 billion at December 31, 2004 and $9.1 billion at December 31, 2003. Included in this total was outstanding Euro commercial paper sold to customers of HSBC of $2.6 billion at December 31, 2004 and $2.8 billion at December 31, 2003. Commercial paper, bank and other borrowings decreased significantly during the fourth quarter of 2004 as the proceeds from the sale of the domestic private label loan portfolio to HSBC Bank USA were used to reduce the outstanding balances.

Long term debt (with original maturities over one year) increased to $85.4 billion at December 31, 2004 from $79.6 billion at December 31, 2003. Significant issuances during 2004 included the following:

- $7.2 billion of domestic and foreign medium-term notes
- $1.8 billion of foreign currency-denominated bonds (including $243 million which was issued to customers of HSBC)

- $1.4 billion of InterNotesSM (retail-oriented medium-term notes)
- $4.5 billion of global debt
- $5.1 billion of securities backed by home equity and auto finance loans. For accounting purposes, these transactions were structured as secured financings.

Selected capital ratios – In managing capital, we develop targets for tangible shareholder's(s') equity to tangible managed assets ("TETMA"), tangible shareholder's(s') equity plus owned loss reserves to tangible managed assets ("TETMA + Owned Reserves") and tangible common equity to tangible managed assets. These ratio targets are based on discussions with HSBC and rating agencies, risks inherent in the portfolio, the projected operating environment and related risks, and any acquisition objectives. Our targets may change from time to time to accommodate changes in the operating environment or other considerations such as those listed above. We are committed to maintaining at least a mid-single "A" rating and as part of that effort will continue to review appropriate capital levels with our rating agencies.

In April 2004, Fitch Ratings revised our Rating Outlook to Positive from Stable and raised our Support Rating to "1" from "2". In July 2004, Fitch Ratings raised our Senior Debt Rating to "A+" from "A" and raised our Senior Subordinated Debt Rating and our Preferred Stock Rating to "A" from "A-". In December 2004, Fitch Ratings again raised our Senior Debt Rating to "AA-" from "A+" and our commercial paper rating to "F1+." Also in December 2004, Moody's Investor Service revised our rating outlook to A1 Positive from A1 Stable.

Selected capital ratios are summarized in the following table:

December 31,	2004	2003 (Restated)
TETMA(1)	**6.68%**	7.03%
TETMA + Owned Reserves(1)	**9.45**	9.89
Tangible common equity to tangible managed assets(1)	**4.67**	5.04
Common and preferred equity to owned assets	**13.01**	14.69
Excluding purchase accounting adjustments:		
TETMA(1)	**8.34%**	8.90%
TETMA + Owned Reserves(1)	**11.12**	11.77
Tangible common equity to tangible managed assets(1)	**6.35**	6.94

(1) TETMA, TETMA + Owned Reserves and tangible common equity to tangible managed assets represent non-GAAP financial ratios that are used by HSBC Finance Corporation management and certain rating agencies to evaluate capital adequacy and may differ from similarly named measures presented by other companies. See "Basis of Reporting" for additional discussion on the use of non-GAAP financial measures and "Reconciliations to GAAP Financial Measures" for quantitative reconciliations to the equivalent GAAP basis financial measure.

HSBC Finance Corporation. HSBC Finance Corporation is an indirect wholly owned subsidiary of HSBC Holdings plc. On March 28, 2003, HSBC acquired Household International, Inc. by way of merger in a purchase business combination. Effective January 1, 2004, HSBC transferred its ownership interest in Household to a wholly owned subsidiary, HSBC North America Holdings Inc., which subsequently contributed Household to its wholly owned subsidiary, HSBC Investments (North America) Inc. ("HINO"). On December 15, 2004, Household merged with its wholly owned subsidiary, Household Finance Corporation, with Household as the surviving entity. At the time of the merger, Household changed its name to "HSBC Finance Corporation."

HSBC Finance Corporation is the parent company that owns the outstanding common stock of its subsidiaries. Our main source of funds is cash received from operations and subsidiaries in the form of dividends and intercompany borrowings. In addition, we may receive cash from third parties or affiliates by issuing preferred stock and debt.

HSBC Finance Corporation received dividends from its subsidiaries of $120 million in 2004 and $159 million in 2003.

During the first quarter of 2003, in conjunction with the acquisition by HSBC, we redeemed outstanding shares of its 4.30, 4.50 and 5.00 percent cumulative preferred stock pursuant to their respective terms. Additionally, outstanding shares of its 7.625, 7.60, 7.50 and 8.25 percent preferred stock were converted into the right to receive cash from HSBC in an amount equal to their liquidation value, plus accrued and unpaid dividends up to but not including the effective date of the merger which was an aggregate amount of $1.1 billion. In consideration of HSBC transferring sufficient funds to make the payments described above with respect to the 7.625, 7.60, 7.50, and 8.25 percent preferred stock, we issued a new series of 6.50 percent cumulative preferred stock in the amount of $1.1 billion to HSBC on March 28, 2003. In September 2004, HNAH issued a new series of preferred stock totaling $1.1 billion to HSBC in exchange for our outstanding 6.5 percent cumulative preferred stock. In October 2004, we paid an accrued dividend of $108 million on our preferred stock to HNAH. Also in October 2004, our immediate parent, HINO, issued a new series of preferred stock to HNAH in exchange for our 6.5 percent cumulative preferred stock.

In August 2003, we redeemed Household Capital Trusts I and IV. The preferred securities issued by these Trusts totaled $275 million and were replaced with $275 million of 6.375% preferred securities of Household Capital Trust VIII, which were issued to HSBC.

HSBC Finance Corporation has a number of obligations to meet with its available cash. It must be able to service its debt and meet the capital needs of its subsidiaries. It also must pay dividends on its preferred stock and may pay dividends on its common stock. Dividends of $2.6 billion were paid to HINO, our immediate

parent company, on our common stock in 2004. No dividends were paid in 2003. HSBC Finance Corporation paid $434 million in common and preferred dividends prior to the merger in 2003. We anticipate paying future dividends to HINO, but will maintain our capital at levels necessary to maintain at least a mid-single "A" rating either by limiting the dividends to or through capital contributions from our parent.

At various times, we will make capital contributions to our subsidiaries to comply with regulatory guidance, support receivable growth, maintain acceptable investment grade ratings at the subsidiary level, or provide funding for long-term facilities and technology improvements. No capital contributions to subsidiaries were made by HSBC Finance Corporation in 2004 or 2003.

Subsidiaries Prior to December 15, 2004, we had two major subsidiaries: Household Finance Corporation ("HFC") and Household Global Funding ("Global"). As previously discussed, on December 15, 2004, HFC merged with and into Household International which changed its name to HSBC Finance Corporation. At December 31, 2004, HSBC Finance had one major subsidiary, Global, and manages all domestic operations held by HFC prior to the merger.

Domestic Operations HSBC Finance Corporation's domestic operations are funded through the collection of receivable balances; issuing commercial paper, medium-term debt and long-term debt; securitizing and borrowing under secured financing facilities and selling consumer receivables. Domestically, HSBC Finance Corporation markets its commercial paper primarily through an in-house sales force. The vast majority of our domestic medium-term notes and long-term debt is now marketed through subsidiaries of HSBC. Domestic medium-term notes may also be marketed through our in-house sales force and investment banks. Long-term debt may also be marketed through investment banks.

At December 31, 2004, advances from subsidiaries of HSBC for our domestic operations totaled $6.0 billion. At December 31, 2003, advances from subsidiaries of HSBC to the domestic operations totaled $3.9 billion. The interest rates on funding from HSBC subsidiaries are market-based and comparable to those available from unaffiliated parties.

Outstanding commercial paper related to our domestic operations totaled $6.0 billion at December 31, 2004 and $7.9 billion at December 31, 2003. The outstanding domestic commercial paper balance decreased significantly in the fourth quarter of 2004 as the proceeds from the bulk sale of the domestic private label portfolio to HSBC Bank USA were used to reduce the outstanding balances. In 2003, following the HSBC merger we established a new Euro commercial paper program, largely targeted towards HSBC clients, which expanded our European base. Under the Euro commercial paper program, commercial paper denominated in Euros, British pounds and U.S. dollars is sold to foreign investors. Outstanding Euro commercial paper sold to customers of HSBC totaled $2.6 billion at December 31, 2004 and $2.8 billion at December 31, 2003. We actively manage the level of commercial paper outstanding to ensure availability to core investors while maintaining excess capacity within our internally-established targets as communicated with the rating agencies.

The following table shows various domestic debt issuances during 2004 and 2003.

	2004	2003
	(in billions)	
Domestic medium term notes, excluding issuances to HSBC customers and subsidiaries of HSBC	**$ 6.4**	$ 3.8
Domestic medium term notes issued to HSBC customers	**.3**	.2
Domestic medium term notes issued to subsidiaries of HSBC	**4.6**	.5
Foreign currency-denominated bonds, excluding issuances to HSBC customers and subsidiaries of HSBC	**1.0**	4.7
Foreign currency-denominated bonds issued to HSBC customers	**.2**	.2
Foreign currency-denominated bonds issued to subsidiaries of HSBC	**.6**	.8

Global debt	**4.5**	5.1
InterNotesSM (retail-oriented medium-term notes)	**1.4**	2.1
Securities backed by home equity and auto finance loans structured as secured financings	**5.1**	3.3

In order to eliminate future foreign exchange risk, currency swaps were used at the time of issuance to fix in U.S. dollars substantially all foreign-denominated notes in 2004 and 2003.

HSBC Finance Corporation issued securities backed by dedicated receivables of $5.1 billion in 2004 and $3.3 billion in 2003. For accounting purposes, these transactions were structured as secured financings, therefore, the receivables and the related debt remain on our balance sheet. At December 31, 2004, closed-end real estate secured and auto finance receivables totaling $10.3 billion secured $7.3 billion of outstanding debt. At December 31, 2003, closed-end real estate secured receivables totaling $8.0 billion secured $6.7 billion of outstanding debt.

HSBC Finance Corporation had committed back-up lines of credit totaling $9.9 billion at December 31, 2004 for its domestic operations. Included in the December 31, 2004 total are $2.5 billion of revolving credit facilities with HSBC. A $4.0 billion revolving credit facility with HSBC Private Bank (Suisse) SA, which was new in 2004 to allow temporary increases in commercial paper issuances in anticipation of the sale of the private label receivables to HSBC Bank USA, expired on December 30, 2004. None of these back-up lines were drawn upon in 2004. The back-up lines expire on various dates through 2007. The most restrictive financial covenant contained in the back-up line agreements that could restrict availability is an obligation to maintain minimum shareholder's equity of $6.9 billion which is substantially below our December 31, 2004 common and preferred shareholder's equity balance of $16.9 billion.

At December 31, 2004, we had facilities with commercial and investment banks under which our domestic operations may securitize up to $14.1 billion of receivables, including up to $12.2 billion of auto finance, MasterCard, Visa, and personal non-credit card receivables and $1.9 billion of real estate secured receivables. As a result of additional liquidity capacity now available from HSBC and its subsidiaries, we have reduced our total conduit capacity by $2.0 billion in 2004. Conduit capacity for real estate secured receivables was increased $.2 billion and capacity for other products was decreased $2.2 billion. The facilities are renewable at the banks' option. At December 31, 2004, $8.2 billion of auto finance, MasterCard and Visa, and personal non-credit card receivables and $1.7 billion of real estate secured receivables were used in collateralized funding transactions structured either as securitizations or secured financings under these funding programs. In addition, we have available a $4 billion single seller mortgage facility (none of which was outstanding at December 31, 2004) structured as a secured financing. The amount available under the facilities will vary based on the timing and volume of public securitization transactions. Through existing term bank financing and new debt issuances, we believe we should continue to have adequate sources of funds.

Global Global includes our foreign subsidiaries in the United Kingdom, the rest of Europe and Canada. Global's assets were $14.3 billion at year-end 2004 and $11.7 billion at year-end 2003. Consolidated

shareholder's(s') equity includes the effect of translating our foreign subsidiaries' assets, liabilities and operating results from their local currency into U.S. dollars.

Each foreign subsidiary conducts its operations using its local currency. While each foreign subsidiary usually borrows funds in its local currency, both our United Kingdom and Canadian subsidiaries have historically borrowed funds in foreign currencies. This allowed the subsidiaries to achieve a lower cost of funds than that available at that time in their local markets. These borrowings were converted from foreign currencies to their local currencies using currency swaps at the time of issuance.

United Kingdom Our United Kingdom operation is funded with HSBC subsidiary debt, long-term debt and securitizations of receivables. Prior to 2004, we also utilized wholesale deposits, commercial paper and short-term and intermediate term bank lines of credit to fund our U.K. operations. The following table summarizes the funding of our United Kingdom operation:

	2004	**2003**
	(in billions)	
Deposits	$ -	$ .2
Commercial paper, bank and other borrowings	-	.8
Due to HSBC affiliates	7.4	3.4
Long term debt	1.0	2.4

At December 31, 2004, the $1.0 billion of long term debt was guaranteed by HSBC Finance Corporation. HSBC Finance Corporation receives a fee for providing the guarantee. Committed back-up lines of credit, which totaled approximately $5.3 billion at December 31, 2003, were eliminated in 2004 as our United Kingdom subsidiary received its 2004 funding directly from HSBC. At December 31, 2004, the U.K. had securitized receivables totaling $922 million.

Canada Our Canadian operation is funded with commercial paper, intermediate debt and long-term debt. Outstanding commercial paper totaled $248 million at December 31, 2004 compared to $307 million a year ago. Intermediate and long-term debt totaled $1.9 billion at year-end 2004 compared to $1.5 billion a year ago. At December 31, 2004, $2.2 billion of the Canadian subsidiary's debt was guaranteed by HSBC Finance Corporation for which it receives a fee for providing the guarantee. Committed back-up lines of credit for Canada were approximately $416 million at December 31, 2004. All of these back-up lines are guaranteed by HSBC Finance Corporation and none were used in 2004.

2005 Funding Strategy As discussed previously, the acquisition by HSBC has improved our access to the capital markets as well as expanded our access to a worldwide pool of potential investors. Our current estimated domestic funding needs and sources for 2005 are summarized in the table that follows.

		(in billions)
Funding needs:		
Net asset growth	$	14 - 18
Commercial paper, term debt and securitization maturities		30 - 34
Other		2 - 4
Total funding needs, including growth	$	46 - 56
Funding sources:		
External funding, including HSBC clients	$	42 - 50
HSBC and HSBC subsidiaries		4 - 6
Total funding sources	$	46 - 56

Commercial paper outstanding in 2005 is expected to be slightly higher than the December 31, 2004 balances, especially during the first three months of 2005 when commercial paper balances will be temporarily high due

to the seasonal activity of our TFS business. Approximately two-thirds of outstanding commercial paper is expected to be domestic commercial paper sold both directly and through dealer programs. Euro commercial paper, introduced in 2003, is expected to account for approximately one-third of outstanding commercial paper and will be marketed predominately to HSBC clients.

Term debt issuances are expected to utilize several ongoing programs to achieve the desired funding. Approximately one-half of term debt funding is expected to be achieved through transactions including U.S. dollar global and Euro transactions and large medium-term note ("MTN") offerings. Domestic and foreign retail note programs are expected to account for approximately 20 percent of term debt issuances. The remaining term debt issuances are expected to consist of smaller domestic and foreign currency MTN offerings.

As a result of our decision in 2004 to fund all new collateralized funding transactions as secured financings, we anticipate securitization levels to continue to decline in 2005. Because existing public MasterCard and Visa credit card transactions were structured as sales to revolving trusts that require replenishments of receivables to support previously issued securities, receivables will continue to be sold to these trusts until the revolving periods end, the last of which is expected to occur in early 2008 based on current projections. In addition, we will continue to replenish at reduced levels, certain non-public personal non-credit card and MasterCard/ Visa securities issued to conduits for a period of time in order to manage liquidity. Since our securitized receivables have varying lives, it will take several years for these receivables to pay-off and the related interest-only strip receivables to be reduced to zero. The termination of sale treatment on new collateralized funding activity reduced our reported net income under U.S. GAAP. There was no impact, however, on cash received from operations or on U.K. GAAP reported results. Because we believe the market for securities backed by receivables is a reliable, efficient and cost-effective source of funds, we will continue to use secured financings of consumer receivables as a source of our funding and liquidity.

HSBC received regulatory approval in 2003 to provide the direct funding required by our United Kingdom operations of up to $10.0 billion. Accordingly, in 2004 we eliminated all back-up lines of credit which had previously supported our United Kingdom subsidiary. All new funding for our United Kingdom subsidiary is now provided directly by HSBC. Our Canadian operation will continue to fund itself independently through traditional third-party funding sources such as commercial paper and medium term-notes. Funding needs in 2005 are not expected to be significant for Canada.

Capital Expenditures We made capital expenditures of $96 million in 2004 and $115 million in 2003. The decrease in 2004 is due to certain technology costs that are now incurred by HTSU.

Commitments We also enter into commitments to meet the financing needs of our customers. In most cases, we have the ability to reduce or eliminate these open lines of credit. As a result, the amounts below do not necessarily represent future cash requirements at December 31, 2004:

(in billions)

Private label, MasterCard and Visa credit cards	**$ 169.4**
Other consumer lines of credit	**12.0**
Open lines of credit(1)	**$ 181.4**

(1) Includes an estimate for acceptance of credit offers mailed to potential customers prior to December 31, 2004.

At December 31, 2004, our mortgage services business had commitments with numerous correspondents to purchase up to $285 million of real estate secured receivables at fair market value, subject to availability based on underwriting guidelines specified by our mortgage services business and at prices indexed to general market rates. These commitments have terms of up to one year and can be renewed upon mutual agreement.

Contractual Cash Obligations The following table summarizes our long-term contractual cash obligations at December 31, 2004 by period due:

	2005	2006	2007	2008	2009	Thereafter	Total
				(in millions)			
Principal balance of debt:							
Time certificates of deposit	$ 2	$ -	$ 10	$ -	$ -	$ -	$ 12
Due to affiliates	7,485	1,241	624	-	2,030	2,409	13,789
Long term debt (including secured financings)	17,114	11,278	9,689	9,570	10,008	21,386	79,045
Total debt	24,601	12,519	10,323	9,570	12,038	23,795	92,846
Operating leases:							
Minimum rental payments	187	141	125	104	76	182	815
Minimum sublease income	77	42	39	35	23	11	227
Total operating leases	110	99	86	69	53	171	588
Obligations under merchant and affinity programs	126	127	127	124	117	597	1,218
Non-qualified pension and postretirement benefit liabilities(1)	26	25	26	31	27	1,063	1,198
Total contractual cash obligations	$ 24,863	$ 12,770	$ 10,562	$ 9,794	$ 12,235	$ 25,626	$ 95,850

(1) Expected benefit payments calculated include future service component.

These cash obligations could be funded primarily through cash collections on receivables, from the issuance of new unsecured debt or through secured financings of receivables. Our receivables and other liquid assets generally have shorter lives than the liabilities used to fund them.

Our purchase obligations for goods and services at December 31, 2004 were not significant.

Off Balance Sheet Arrangements and Secured Financings

Securitizations and Secured Financings Securitizations (collateralized funding transactions structured to receive sale treatment under Statement of Financial Accounting Standards No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a Replacement of FASB Statement No. 125," ("SFAS No. 140")) and secured financings (collateralized funding transactions which do not receive sale treatment under SFAS No. 140) of consumer receivables have been a significant source of funding and liquidity for us. Securitizations and secured financings have been used to limit our reliance on the unsecured debt markets and often are more cost-effective than alternative funding sources.

In a securitization, a designated pool of non-real estate consumer receivables is removed from the balance sheet and transferred through a limited purpose financing subsidiary to an unaffiliated trust. This unaffiliated trust is a qualifying special purpose entity ("QSPE") as defined by SFAS No. 140 and, therefore, is not consolidated. The QSPE funds its receivable purchase through the issuance of securities to investors, entitling them to receive specified cash flows during the life of the securities. The receivables transferred to the QSPE serve as collateral for the securities. At the time of sale, an interest-only strip receivable is recorded, representing the present value of the cash flows we expect to receive over the life of the securitized receivables, net of estimated credit losses and debt service. Under the terms of the securitizations, we receive annual servicing fees on the outstanding balance of the securitized receivables and the rights to future residual cash flows on the sold receivables after the investors receive their contractual return. Cash flows related to the interest-only strip receivables and servicing the receivables are collected over the life of the underlying securitized receivables.

(1) These non-GAAP financial measures are provided for comparison of our operating trends and should be read in conjunction with our owned basis GAAP financial information. Refer to "Reconciliations to GAAP Financial Measures" for a discussion of non-GAAP financial information and for quantitative reconciliations to the equivalent GAAP basis financial measure.

(2) Includes $5 million of MasterCard and Visa and $197 million of private label charge-off relating to the adoption of FFIEC charge-off policies in December 2004.

(3) As previously discussed, the adoption of FFIEC charge-off policies for our domestic private label and MasterCard/ Visa portfolios and subsequent sale of the domestic private label receivable portfolio in December 2004 had a significant impact on this ratio. Reserves as a percentage of net charge-offs excluding domestic private label net charge-offs and charge-off relating to the adoption of FFIEC was 96.0% at December 31, 2004.

HSBC FINANCE CORPORATION AND SUBSIDIARIES

NET INTEREST MARGIN – 2004 COMPARED TO 2003 (OWNED BASIS)

	Average Outstanding(1)		Average Rate		Finance and Interest Income/ Interest Expense		Increase/ (Decrease) Due to:		
	2004	2003 (Restated)	2004	2003 (Restated)	2004	2003 (Restated)	Variance	Volume Variance(2)	Rate Variance(2)
					(dollars are in millions)				
Receivables:									
Real estate secured	**$ 56,303**	$ 49,852	**8.8%**	9.7%	**$ 4,974**	$ 4,852	$ 122	$ 594	$ (472)
Auto finance	**5,785**	2,920	**12.2**	12.9	**706**	378	328	351	(23)
MasterCard/ Visa	**11,575**	9,517	**14.8**	14.8	**1,712**	1,406	306	304	2
Private label	**13,029**	11,942	**10.8**	11.6	**1,407**	1,379	28	121	(93)
Personal non-credit card	**14,194**	14,009	**15.7**	16.5	**2,234**	2,314	(80)	30	(110)
Commercial and other	**354**	430	**2.5**	2.2(6)	**9**	10	(1)	(2)	1
Purchase accounting adjustments	**319**	397	**-**	-	**(201)**	(200)	(1)	(1)	-
Total receivables	**101,559**	89,067	**10.7**	11.4	**10,841**	10,139	702	1,401	(699)
Noninsurance investments	**4,853**	5,280	**2.1**	2.0	**104**	103	1	(6)	7
Total interest-earning assets (excluding insurance investments)	**$ 106,412**	$ 94,347	**10.3%**	10.9%	**$ 10,945**	$ 10,242	$ 703	$ 1,261	$ (558)
Insurance investments	**3,165**	3,160							
Other assets	**14,344**	12,590							
Total Assets	**$ 123,921**	$ 110,097							
Debt:									
Deposits	**$ 88**	$ 992	**1.9%**	3.6%	**$ 2**	$ 36	$ (34)	$ (24)	$ (10)
Commercial paper	**11,403**	6,357	**1.8**	1.6	**210**	103	107	91	16
Bank and other borrowings	**38**	1,187	**1.9(6)**	3.9	**1**	46	(45)	(29)	(16)
Due to affiliates	**8,752**	3,014	**3.9**	2.4	**343**	73	270	204	66
Long term debt (with original maturities over one year)	**79,834**	73,383	**3.3**	3.6	**2,587**	2,670	(83)	223	(306)
Total debt	**$ 100,115**	$ 84,933	**3.1%**	3.4%	**$ 3,143**	$ 2,928	$ 215	$ 492	$ (277)
Other liabilities	**5,703**	9,836							
Total liabilities	**105,818**	94,769							
Preferred securities	**1,100**	1,119							
Common shareholder's(s') equity	**17,003**	14,209							
Total Liabilities and Shareholder's(s') Equity	**$ 123,921**	$ 110,097							
Net Interest Margin – Owned Basis(3)(5)			7.3%	7.8%	**$ 7,802**	$ 7,314	$ 488	$ 769	$ (281)
Interest Spread – Owned Basis(4)			7.2%	7.5%					

(1) Nonaccrual loans are included in average outstanding balances.

(2) Rate/volume variance is allocated based on the percentage relationship of changes in volume and changes in rate to the total interest variance. For total receivables, total interest-earning assets and total debt, the rate and volume variances are calculated based on the relative weighting of the individual components comprising these totals. These totals do not represent an arithmetic sum of the individual components.

(3) Represents net interest income as a percent of average interest-earning assets

(4) Represents the difference between the yield earned on interest-earning assets and the cost of the debt used to fund the assets

(5) The net interest margin analysis includes the following for foreign businesses:

	2004	2003
Average interest-earning assets	**$ 10,728**	$ 8,779
Average interest-bearing liabilities	**9,127**	7,957
Net interest income	**712**	660
Net interest margin	**6.6%**	7.5%

(6) Average rate does not recompute from the dollar figures presented due to rounding.

HSBC FINANCE CORPORATION AND SUBSIDIARIES

NET INTEREST MARGIN – 2003 COMPARED TO 2002 (OWNED BASIS)

	Average Outstanding(1)		Average Rate		Finance and Interest Income/ Interest Expense		Increase/ (Decrease) Due to:		
	2003 (Restated)	2002	2003 (Restated)	2002	2003 (Restated)	2002	Variance	Volume Variance(2)	Rate Variance(2)
	(dollars are in millions)								
Receivables:									
Real estate secured	$ 49,852	$47,258	9.7%	10.7%	$ 4,852	$ 5,051	$ (199)	$ 268	$ (467)
Auto finance	2,920	2,529	12.9	14.7	378	373	5	54	(49)
MasterCard/ Visa	9,517	7,569	14.8	14.8	1,406	1,119	287	288	(1)
Private label	11,942	10,775	11.6	12.2	1,379	1,314	65	137	(72)
Personal non-credit card	14,009	13,968	16.5	18.1	2,314	2,526	(212)	7	(219)
Commercial and other	430	483	2.2(6)	2.1	10	10	-	(1)	1
Purchase accounting adjustments	397	-	-	-	(200)	-	(200)	(200)	-
Total receivables	89,067	82,582	11.4	12.6	10,139	10,393	(254)	781	(1,035)
Noninsurance investments	5,280	5,302	2.0	2.5	103	132	(29)	(1)	(28)
Total interest-earning assets (excluding insurance investments)	$ 94,347	$87,884	10.9%	12.0%	$ 10,242	$10,525	$ (283)	$ 735	$ (1,018)
Insurance investments	3,160	3,191							
Other assets	12,590	5,229							
Total Assets	$ 110,097	$96,304							
Debt:									
Deposits	$ 992	$ 5,839	3.6%	6.5%	$ 36	$ 380	$ (344)	$ (224)	$ (120)
Commercial paper	6,357	6,830	1.6	1.9	103	130	(27)	(9)	(18)
Bank and other borrowings	1,187	1,473	3.9	3.4	46	51	(5)	(11)	6
Due to affiliates	3,014	-	2.4	-	73	-	73	73	-
Long term debt (with original maturities over one year)	73,383	69,406	3.6	4.8	2,670	3,310	(640)	181	(821)
Total debt	$ 84,933	$83,548	3.4%	4.6%	$ 2,928	$ 3,871	$ (943)	$ 63	$ (1,006)
Other liabilities	9,836	3,251							
Total liabilities	94,769	86,799							
Preferred securities	1,119	865							
Common shareholder’s(s’) equity	14,209	8,640							
Total Liabilities and Shareholder’s(s’) Equity	$ 110,097	$96,304							

Net Interest Margin – Owned Basis(3)(5)	7.8%	7.6%	$ 7,314	$ 6,654	$ 660	$ 672	$ (12)
Interest Spread – Owned Basis (4)	7.5%	7.4%					

(1) Nonaccrual loans are included in average outstanding balances.

(2) Rate/volume variance is allocated based on the percentage relationship of changes in volume and changes in rate to the total interest variance. For total receivables, total interest-earning assets and total debt, the rate and volume variances are calculated based on the relative weighting of the individual components comprising these totals. These totals do not represent an arithmetic sum of the individual components

(3) Represents net interest income as a percent of average interest-earning assets

(4) Represents the difference between the yield earned on interest-earning assets and the cost of the debt used to fund the assets

(5) The net interest income analysis includes the following for foreign businesses:

	2003	2002
Average interest-earning assets	$ 8,779	$ 6,616
Average interest-bearing liabilities	7,957	6,076
Net interest income	660	483
Net interest margin	7.5%	7.3%

(6) Average rate does not recompute from dollar figures presented due to rounding.

HSBC FINANCE CORPORATION AND SUBSIDIARIES

NET INTEREST MARGIN – 2004 COMPARED TO 2003 AND 2002 (MANAGED BASIS)

Net Interest Margin on a Managed Basis As receivables are securitized rather than held in our portfolio, net interest margin is reclassified to securitization revenue. We retain a substantial portion of the profit inherent in the receivables while increasing liquidity. The comparability of net interest margin between periods may be impacted by the level and type of receivables securitized. Net interest margin on a managed basis includes finance income earned on our owned receivables as well on our securitized receivables. This finance income is offset by interest expense on the debt recorded on our balance sheet as well as the contractual rate of return on the instruments issued to investors when the receivables were securitized.

	Average Outstanding(1)			Average Rate			Finance and Interest Income/Interest Expense			Increase/(Decrease) Due to: 2004 Compared to 2003			2003 Compared to 2002		
	2004	**2003 (Restated)**	**2002**	**2004**	**2003 (Restated)**	**2002**	**2004**	**2003 (Restated) (dollars are in millions)**	**2002**	**Variance**	**Volume Variance(2)**	**Rate Variance(2)**	**Variance**	**Volume Variance(2)**	**Rate Variance(2)**
Receivables:															
Real estate secured	**$ 56,462**	$ 50,124	$ 47,830	**8.8%**	9.7%	10.7%	**$ 4,984**	$ 4,874	$ 5,114	$ 110	$ 583	$ (473)	$ (240)	$ 238	$ (478)
Auto finance	**9,432**	7,918	6,942	**13.3**	14.9	16.7	**1,250**	1,180	1,156	70	210	(140)	24	153	(129)
MasterCard/ Visa	**20,674**	19,272	17,246	**12.7**	12.9	13.4	**2,627**	2,484	2,304	143	179	(36)	180	263	(83)
Private label	**17,579**	16,016	13,615	**10.8**	11.5	12.2	**1,895**	1,843	1,663	52	173	(121)	180	281	(101)
Personal non-credit card	**18,986**	19,041	18,837	**17.2**	17.8	18.6	**3,260**	3,388	3,505	(128)	(10)	(118)	(117)	38	(155)
Commercial and other	**354**	430	483	**2.5**	2.2(5)	2.1	**9**	10	10	(1)	(2)	1	-	-	-
Purchase accounting adjustment	**319**	397	-	**-**	-	-	**(201)**	(200)	-	(1)	(1)	-	(170)	(170)	-
Total receivables	**123,806**	113,198	104,953	**11.2**	12.0	13.1	**13,824**	13,579	13,752	245	1,253	(1,008)	(143)	1,036	(1,179)
Noninsurance investments	**4,853**	5,280	5,302	**2.1**	2.0	2.5	**104**	103	131	1	(6)	7	(58)	(1)	(57)
Total interest-earning assets (excluding insurance investments)	**$ 128,659**	$ 118,478	$ 110,255	**10.8%**	11.5%	12.6%	**$ 13,928**	$ 13,682	$ 13,883	$ 246	$ 1,133	$ (887)	$ (201)	$ 1,025	$ (1,226)
Total debt	**$ 122,362**	$ 109,064	$ 105,919	**3.0%**	3.2%	4.3%	**$ 3,671**	$ 3,494	$ 4,546	$ 177	$ 408	$ (231)	$ (1,052)	$ 133	$ (1,185)
Net Interest Margin – Managed Basis(3)				8.0%	8.6%	8.5%	**$ 10,257**	$ 10,188	$ 9,337	$ 69	$ 725	$ (656)	$ 851	$ 892	$ (41)
Interest Spread –															

Total other revenues	**5,073**	3,107	1,212	4,146
Costs and expenses:				
Salaries and employee benefits	**1,886**	1,507	491	1,817
Sales incentives	**363**	226	37	256
Occupancy and equipment expenses	**323**	302	98	371
Other marketing expenses	**636**	409	139	531
Other servicing and administrative expenses	**868**	835	314	889
Support services from HSBC affiliates	**750**	-	-	-
Amortization of intangibles	**363**	246	12	58
Policyholders' benefits	**412**	286	91	368
Settlement charge and related expenses	**-**	-	-	525
HSBC acquisition related costs incurred by HSBC Finance Corporation	**-**	-	198	-
Total costs and expenses	**5,601**	3,811	1,380	4,815
Income before income tax expense	**2,940**	2,047	428	2,253
Income tax expense	**1,000**	690	182	695
Net income	**$ 1,940**	$ 1,357	$ 246	$ 1,558

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

CONSOLIDATED BALANCE SHEET

Year ended December 31,	2004 (Successor)	2003 (Successor) (Restated)
	(in millions, except share data)	
Assets		
Cash	**$ 392**	$ 463
Securities purchased under agreements to resell	**2,651**	-
Securities	**4,327**	11,073
Receivables, net	**104,815**	91,027
Intangible assets, net	**2,705**	2,856
Goodwill	**6,856**	6,697
Properties and equipment, net	**487**	527
Real estate owned	**587**	631
Derivative financial assets	**4,049**	3,016
Other assets	**3,321**	2,762
Total assets	**$ 130,190**	$ 119,052
Liabilities		
Debt:		
Deposits	**$ 47**	$ 232
Commercial paper, bank and other borrowings	**9,013**	9,122
Due to affiliates	**13,789**	7,589
Long term debt (with original maturities over one year)	**85,378**	79,632
Total debt	**108,227**	96,575
Insurance policy and claim reserves	**1,303**	1,258
Derivative related liabilities	**432**	597
Other liabilities	**3,287**	3,131
Total liabilities	**113,249**	101,561
Shareholder's equity		
Redeemable preferred stock held by HINO (held by HSBC at December 31, 2003)	**1,100**	1,100

Common shareholder’s equity:		
Common stock, $0.01 par value, 100 shares authorized, 50 shares issued	**-**	-
Additional paid-in capital	**14,627**	14,645
Retained earnings	**571**	1,303
Accumulated other comprehensive income	**643**	443
Total common shareholder’s equity	**15,841**	16,391
Total liabilities and shareholder’s equity	**$ 130,190**	$ 119,052

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

HSBC Finance Corporation

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDER’S(S’) EQUITY

	Year ended December 31, 2004 (Successor)	March 29 through December 31, 2003 (Successor)	January 1 through March 28, 2003 (Predecessor)	Year ended December 31, 2002 (Predecessor)
		(Restated) (in millions)		
Preferred stock				
Balance at beginning of period	**$ 1,100**	$ 1,100	$ 1,193	$ 456
Reclassification of preferred stock issuance costs	**-**	-	21	-
Issuance of preferred stock	**-**	-	-	737
Redemption of preferred stock	**-**	-	(114)	-
Balance at end of period	**$ 1,100**	$ 1,100	$ 1,100	$ 1,193
Common shareholder’s(s’) equity				
Common stock				
Balance at beginning of period	**$ -**	$ -	$ 552	$ 552
Effect of push-down accounting of HSBC’s purchase price on net assets	**-**	-	(552)	-
Balance at end of period	**$ -**	$ -	$ -	$ 552
Additional paid-in capital				
Balance at beginning of period	**$ 14,645**	$ 14,661	$ 1,911	$ 2,030
Return of capital to HSBC	**(31)**	(41)	-	-
Employee benefit plans and other	**13**	25	10	50
Reclassification of preferred stock issuance costs	**-**	-	(21)	-
Issuance of preferred stock	**-**	-	-	(11)
Exercise of stock options		-	-	5
Common stock offering	**-**	-	-	(194)
Issuance of adjustable conversion rate equity security units	**-**	-	-	31
Effect of push-down accounting of HSBC’s purchase price on net assets	**-**	-	12,761	-
Balance at end of period	**$ 14,627**	$ 14,645	$ 14,661	$ 1,911
Retained earnings				
Balance at beginning of period	**1,303**	$ -	$ 9,885	$ 8,838
Net income	**1,940**	1,357	246	1,558
Dividends:				
Preferred stock	**(72)**	(54)	(22)	(63)
Common stock	**(2,600)**	-	(412)	(448)
Effect of push-down accounting of HSBC’s purchase price on net assets	**-**	-	(9,697)	-
Balance at end of period	**$ 571**	$ 1,303	$ -	$ 9,885
Accumulated other comprehensive income				
Balance at beginning of period	**$ 443**	$ -	$ (695)	$ (732)
Net change in unrealized gains (losses) on:				
Derivatives classified as cash flow hedges	**130**	(11)	101	(37)
Securities available for sale and interest-only strip receivables	**(114)**	168	(25)	96
Minimum pension liability	**(4)**	-	-	(31)

Contractual maturities of time certificates within each interest rate range at December 31, 2004 were as follows:

Interest Rate	2005	2006	2007	2008	2009	Thereafter	Total
4.00% - 5.99%	$ 2	$ -	$ 10	$ -	$ -	$ -	$ 12

14. *Commercial Paper, Bank and Other Borrowings*

	Commercial Paper	Bank and Other Borrowings	Total
2004			
Balance	**$ 8,969**	**$ 44**	**$ 9,013**
Highest aggregate month-end balance			**16,179**
Average borrowings	**11,403**	**38**	**11,441**
Weighted-average interest rate:			
At year-end	**2.2%**	**2.6%**	**2.2%**
Paid during year	**1.8**	**1.9**	**1.8**
2003			
Balance	$ 8,256	$ 866	$ 9,122
Highest aggregate month-end balance			9,856
Average borrowings	6,357	1,187	7,544
Weighted-average interest rate:			
At year-end	1.2%	3.6%	1.4%
Paid during year	1.6	3.9	2.0
2002			
Balance	$ 4,605	$ 1,523	$ 6,128
Highest aggregate month-end balance			13,270
Average borrowings	6,830	1,473	8,303
Weighted-average interest rate:			
At year-end	1.8%	3.9%	2.4%
Paid during year	1.9	3.4	2.2

Commercial paper included obligations of foreign subsidiaries of $248 million at December 31, 2004, $307 million at December 31, 2003 and $497 million at December 31, 2002. Bank and other borrowings included obligations of foreign subsidiaries of $44 million at December 31, 2004, $832 million at December 31, 2003 and $1.5 billion at December 31, 2002.

Interest expense for commercial paper, bank and other borrowings totaled $211 million in 2004, $130 million in the period March 29 through December 31, 2003, $19 million in the period January 1 through March 28, 2003 and $181 million in 2002.

We maintain various bank credit agreements primarily to support commercial paper borrowings and also to provide funding in the U.K. We had committed back-up lines and other bank lines of $18.0 billion at December 31, 2004, including $10.1 billion with HSBC and subsidiaries and $15.8 billion at December 31, 2003, including $7.0 billion with HSBC and subsidiaries. Our U.K. subsidiary had drawn $7.4 billion on its bank lines of credit (all with HSBC), at December 31, 2004 and had $4.1 billion drawn on its bank lines of credit including $3.4 billion drawn on HSBC lines, at December 31, 2003. A $4.0 billion revolving credit facility with HSBC Private Bank (Suisse) SA, which was new in 2004 to allow temporary increases in commercial paper issuances in anticipation of the sale of the private label receivables to HSBC Bank USA, expired on December 30, 2004. Formal credit lines are reviewed annually and expire at various dates through 2007. Borrowings under these lines generally are available at a surcharge over LIBOR. The most restrictive financial covenant contained in the back-up line agreements that could restrict availability is an obligation to maintain minimum shareholder’s equity of $6.9 billion which is substantially below our December 31, 2004 common and preferred shareholder’s(s’) equity balance of $16.9 billion. Because our U.K. subsidiary receives its funding directly from HSBC, we eliminated all third-party back-up lines at our U.K. subsidiary in 2004. Annual commitment fee requirements to support availability of these lines at December 31, 2004 totaled $7 million and included $2 million for the HSBC lines.

15. Long Term Debt (With Original Maturities Over One Year)

	At December 31, 2004	2003
	(in millions)	(Restated)
Senior Debt		
Fixed rate:		
8.875% Adjustable Conversion-Rate Equity Security Units	**$ 529**	$ 519
Secured financings:		
1.50% to 2.99%; due 2005 to 2006	**239**	-
3.00% to 3.99%; due 2006 to 2008	**346**	-
7.00% to 7.49%; due 2005	**51**	79
7.50% to 7.99%; due 2005	**10**	16
8.00% to 8.99%; due 2005	**11**	17
Other fixed rate senior debt:		
2.15% to 3.99%; due 2005 to 2010	**6,310**	3,549
4.00% to 4.99%; due 2005 to 2023	**10,878**	8,176
5.00% to 5.49%; due 2005 to 2023	**5,082**	5,045
5.50% to 5.99%; due 2005 to 2024	**6,922**	6,222
6.00% to 6.49%; due 2005 to 2033	**8,380**	9,616
6.50% to 6.99%; due 2005 to 2033	**9,247**	9,211
7.00% to 7.49%; due 2005 to 2032	**6,333**	6,748
7.50% to 7.99%; due 2005 to 2032	**7,450**	7,775
8.00% to 9.25%; due 2005 to 2012	**3,497**	3,547
Variable interest rate:		
Secured financings – 2.63% to 3.35%; due 2005 to 2010	**6,668**	6,611
Other variable interest rate senior debt – 2.16% to 6.07%; due 2005 to 2018	**10,555**	8,504
Senior Subordinated Debt – 4.56%, due 2005	**170**	170
Junior Subordinated Notes Issued to Capital Trusts	**722**	722
Unamortized Discount	**(296)**	(84)
Purchase Accounting Fair Value Adjustments	**2,274**	3,189
Total long term debt	**$ 85,378**	$ 79,632

Purchase accounting fair value adjustments represent adjustments which have been “pushed down” to record our long term debt at fair value at the merger date.

Secured financings of $7.3 billion at December 31, 2004 are secured by $10.3 billion of real estate secured and auto finance receivables. Secured financings of $6.7 billion at December 31, 2003 are secured by $8.0 billion of real estate secured receivables.

At December 31, 2004, long term debt included carrying value adjustments relating to derivative financial instruments which decreased the debt balance by $121 million and a foreign currency translation adjustment relating to our foreign denominated debt which increased the debt balance by $4 billion. At December 31, 2003, long term debt included carrying value adjustments relating to derivative financial instruments which increased the debt balance by $37 million and a foreign currency translation adjustment relating to our foreign denominated debt which increased the debt balance by $3.3 billion.

Weighted-average interest rates were 5.1 percent at December 31, 2004 and 5.1 percent at December 31, 2003 (excluding purchase accounting adjustments). Interest expense for long term debt was $2.6 billion in 2004,

$1.8 billion in the period March 29 through December 31, 2003, $870 million in the period January 1 through March 28, 2003 and $3.3 billion in 2002. The most restrictive financial covenants contained in the terms of our debt agreements are the maintenance of a minimum shareholder’s equity of $6.9 billion which is substantially lower than our common and preferred shareholder’s equity balance of $16.9 billion at December 31, 2004. Debt denominated in a foreign currency is included in the applicable rate category based on the effective U.S. dollar equivalent rate as summarized in Note 16, “Derivative Financial Instruments.”

In 2002, we issued $542 million of 8.875 percent Adjustable Conversion-Rate Equity Security Units. The Adjustable Conversion-Rate Equity Security Units each consist of a senior unsecured note of HSBC Finance Corporation (as successor by merger to Household Finance Corporation)

(1) Represent contracts terminated as the market execution technique of closing the transaction either (a) just prior to maturity to avoid delivery of the underlying instrument or (b) at the maturity of the underlying items being hedged.

(2) Under the Financial Accounting Standards Board's interpretations of SFAS 133, the shortcut method of accounting was no longer allowed for interest rate swaps which were outstanding at the time of the merger. During 2003, we restructured our interest rate swap portfolio to regain use of the shortcut method for a substantial number of our fair value hedges and to reduce the potential volatility of future earnings.

(3) (Bracketed) unbracketed amounts represent amounts to be (paid) received by us had these positions been closed out at the respective balance sheet date. Bracketed amounts do not necessarily represent risk of loss as the fair value of the derivative financial instrument and the items being hedged must be evaluated together. See Note 25, "Fair Value of Financial Instruments," for further discussion of the relationship between the fair value of our assets and liabilities.

We operate in three functional currencies, the U.S. dollar, the British pound and the Canadian dollar. The U.S. dollar is the functional currency for exchange-traded interest rate futures contracts and options. Non-exchange traded instruments are restated in U.S. dollars by country as follows:

	Interest Rate Swaps	Currency Swaps	Foreign Exchange Rate Contracts Purchased	Foreign Exchange Rate Contracts Sold	Interest Rate Forward Contracts Purchased	Other Risk Management Instruments
			(in millions)			
2004						
United States	**$ 42,365**	**$ 17,543**	**$ 1,146**	**$ (599)**	**$ -**	**$ 4,345**
Canada	**582**	**-**	**-**	**(15)**	**374**	**-**
United Kingdom	**2,306**	**607**	**-**	**-**	**-**	**35**
	$ 45,253	**$ 18,150**	**$ 1,146**	**$ (614)**	**$ 374**	**$ 4,380**
2003						
United States	$ 39,653	$ 14,995	$ 1,223	$ (593)	$ -	$ 6,595
Canada	405	-	-	(1)	174	-
United Kingdom	1,254	1,543	-	-	-	32
	$ 41,312	$ 16,538	$ 1,223	$ (594)	$ 174	$ 6,627
2002						
United States	$ 42,682	$ 10,211	$ 351	$ (2,524)	$ -	$ 7,194
Canada	270	-	-	-	159	-
United Kingdom	1,554	1,450	26	-	-	27
	$ 44,506	$ 11,661	$ 377	$ (2,524)	$ 159	$ 7,221

The table below reflects the items hedged using derivative financial instruments which qualify for hedge accounting at December 31, 2004. The critical terms of the derivative financial instruments have been designed to match those of the related asset or liability.

	Interest Rate Swaps	Currency Swaps	Foreign Exchange Rate Contracts
		(in millions)	
Investment securities	$ -	$ -	$ -
Commercial paper, bank and other borrowings	2,306	-	1,200
Long term debt	37,625	8,415	-
Advances to foreign subsidiaries	-	-	560
Total items hedged using derivative financial instruments	$ 39,931	$ 8,415	$ 1,760

The following table summarizes the maturities and related weighted-average receive/pay rates of interest rate swaps outstanding at December 31, 2004:

	2005	2006	2007	2008	2009	2010	Thereafter	Total
				(dollars are in millions)				

characteristics used in our asset/liability management process. All assumptions are based on historical experience adjusted for future expectations. Assumptions used to determine fair values for financial instruments for which no active market exists are inherently judgmental and changes in these assumptions could significantly affect fair value calculations.

As required under generally accepted accounting principles, a number of other assets recorded on the balance sheets (such as acquired credit card relationships, the value of consumer lending relationships for originated receivables and the franchise values of our business units) are not considered financial instruments and, accordingly, are not valued for purposes of this disclosure. However, on March 29, 2003, as a result of our acquisition by HSBC, these other assets were adjusted to their fair market value based, in part, on third party valuation data, under the "push-down" method of accounting. (See Note 4, "Acquisitions and Divestitures.") We believe there continues to be substantial value associated with these assets based on current market conditions and historical experience. Accordingly, the estimated fair value of financial instruments, as disclosed, does not fully represent our entire value, nor the changes in our entire value.

The following is a summary of the carrying value and estimated fair value of our financial instruments:

	At December 31,					
	2004			2003		
	Carrying Value	Estimated Fair Value	Difference	Carrying Value	Estimated Fair Value	Difference
	(in millions)					
Assets:						
Cash	**$ 392**	**$ 392**	**$ -**	$ 463	$ 463	$ -
Securities purchased under agreements to resell	**2,651**	**2,651**	**-**	-	-	-
Securities	**4,327**	**4,327**	**-**	11,073	11,073	-
Receivables	**104,815**	**105,314**	**499**	91,027	91,597	570
Due from affiliates	**604**	**604**	**-**	-	-	-
Derivative financial assets	**4,049**	**4,049**	**-**	3,016	3,016	-
Total assets	**116,838**	**117,337**	**499**	105,579	106,149	570
Liabilities:						
Deposits	**(47)**	**(47)**	**-**	(232)	(233)	(1)
Commercial paper, bank and other borrowings	**(9,013)**	**(9,013)**	**-**	(9,122)	(9,122)	-
Due to affiliates	**(13,789)**	**(13,819)**	**(30)**	(7,589)	(7,603)	(14)
Long term debt	**(85,378)**	**(86,752)**	**(1,374)**	(79,632)	(80,566)	(924)
Insurance policy and claim reserves	**(1,303)**	**(1,370)**	**(67)**	(1,258)	(1,255)	3
Derivative financial liabilities	**(70)**	**(70)**	**-**	(149)	(149)	-
Total liabilities	**(109,600)**	**(111,071)**	**(1,471)**	(97,982)	(98,918)	(936)
Total	**$ 7,238**	**$ 6,266**	**$ (972)**	$ 7,597	$ 7,231	$ (366)

Cash: Carrying value approximates fair value due to cash's liquid nature.

Securities purchased under agreements to resell: The fair value of securities purchased under agreements to resell approximates carrying value due to their short-term maturity.

Securities: Securities are classified as available-for-sale and are carried at fair value on the balance sheets. Fair values are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Receivables: The fair value of adjustable rate receivables generally approximates carrying value because interest rates on these receivables adjust with changing market interest rates. The fair value of fixed rate consumer receivables was estimated by discounting future expected cash flows at interest rates which approximate the rates that would achieve a similar return on assets with comparable risk characteristics. Receivables also includes our interest-only strip receivables. The interest-only strip receivables are carried at fair value on our balance sheets. Fair value is based on an estimate of the present value of future cash flows associated with securitizations of certain real estate secured, auto finance, MasterCard and Visa, private label and personal non-credit card receivables.

Deposits: The fair value of our savings and demand accounts equaled the carrying amount as stipulated in SFAS No. 107. The fair value of fixed rate time certificates was estimated by discounting future expected cash flows at interest rates that we offer on such products at the respective valuation dates.

Commercial paper, bank and other borrowings: The fair value of these instruments approximates existing carrying value because interest rates on these instruments adjust with changes in market interest rates due to their short-term maturity or repricing characteristics.

Due to affiliates: The estimated fair value of our fixed rate debt instruments was determined using either quoted market prices or by discounting future expected cash flows at interest rates offered for similar types of debt instruments. Carrying value is typically used to estimate the fair value of floating rate debt.

Long term debt: The estimated fair value of our fixed rate debt instruments was determined using either quoted market prices or by discounting future expected cash flows at interest rates offered for similar types of debt instruments. Carrying value is typically used to estimate the fair value of floating rate debt.

Insurance policy and claim reserves: The fair value of insurance reserves for periodic payment annuities was estimated by discounting future expected cash flows at estimated market interest rates at December 31, 2004 and 2003. The fair value of other insurance reserves is not required to be determined in accordance with SFAS No. 107.

Derivative financial assets and liabilities: All derivative financial assets and liabilities, which exclude amounts receivable from or payable to swap counterparties, are carried at fair value on the balance sheet. Where practical, quoted market prices were used to determine fair value of these instruments. For non-exchange traded contracts, fair value was determined using accepted and established valuation methods (including input from independent third parties) which consider the terms of the contracts and market expectations on the valuation date for forward interest rates (for interest rate contracts) or forward foreign currency exchange rates (for foreign exchange contracts). We enter into foreign exchange contracts to hedge our exposure to currency risk on foreign denominated debt. We also enter into interest rate contracts to hedge our exposure to interest rate risk on assets and liabilities, including debt. As a result, decreases/increases in the fair value of derivative financial instruments which have been designated as effective hedges are offset by a corresponding increase/decrease in the fair value of the individual asset or liability being hedged. See Note 16, “Derivative Financial Instruments,” for additional discussion of the nature of these items.

26. Attorney General Settlement

On October 11, 2002, we reached a preliminary agreement with a multi-state working group of state attorneys general and regulatory agencies to effect a nationwide resolution of alleged violations of federal and/or state consumer protection, consumer financing and banking laws and regulations with respect to secured real estate lending from Household Finance Corporation and Beneficial Corporation and their subsidiaries conducting

retail branch consumer lending operations. This preliminary agreement, and related subsequent consent decrees and similar documentation entered into with each of the 50 states and the District of Columbia, are referred to collectively as the “Multi-State Settlement Agreement”, which became effective on December 16, 2002. Pursuant to the Multi-State Settlement Agreement, we funded a $484 million settlement fund that was divided among the states (and the District of Columbia), with each state receiving a proportionate share of the funds based upon the volume of the retail branch originated real estate secured loans we made in that state during the period of January 1, 1999 to September 30, 2002. No fines, penalties or punitive damages were assessed by the states pursuant to the Multi-State Settlement Agreement.

In August 2003, notices of a claims procedure were distributed to holders of approximately 591,000 accounts identified as having potential claims. Approximately 82% of customers accepted funds in settlement and had executed a release of all civil claims against us relating to the specified consumer lending practices. All checks were mailed. Each state agreed that the settlement resolves all current civil investigations and proceedings by the attorneys general and state lending regulators relating to the lending practices at issue.

We recorded a pre-tax charge of $525 million ($333 million after-tax) during the third quarter of 2002 related to the Multi-State Settlement Agreement. The charge reflects the costs of this settlement agreement and related matters and has been reflected in the statement of income in total costs and expenses.

27. Concentration of Credit Risk

A concentration of credit risk is defined as a significant credit exposure with an individual or group engaged in similar activities or affected similarly by economic conditions.

Because we primarily lend to consumers, we do not have receivables from any industry group that equal or exceed 10 percent of total owned or managed receivables at December 31, 2004 and 2003. We lend nationwide and our receivables are distributed as follows at December 31, 2004:

State/Region	Percent of Total Owned Domestic Receivables	Percent of Total Managed Domestic Receivables
California	12%	12%
Midwest (IL, IN, IA, KS, MI, MN, MO, NE, ND, OH, SD, WI)	23	23

I, the undersigned, declare:

1. That declarant is and was, at all times herein mentioned, a citizen of the United States and employed in the City and County of San Diego, State of California, over the age of 18 years, and not a party to or interested party in the within action; that declarant's business address is 655 W. Broadway, Suite 1900, San Diego, California 92101.

2. That on September 13, 2013, declarant served by electronic mail and by U.S. Mail to the parties the following documents:

DECLARATION OF BJORN I. STEINHOLT, CFA DATED SEPTEMBER 12, 2013

The parties' e-mail addresses are as follows:

Tkavaler@cahill.com	Zhudson@bancroftpllc.com
Pfarren@cahill.com	Mrakoczy@skadden.com
Dowen@cahill.com	Rstoll@skadden.com
Jhall@cahill.com	Mmiller@MillerLawLLC.com
Pclement@bancroftpllc.com	Lfanning@MillerLawLLC.com

and by U.S. Mail to:

Lawrence G. Soicher, Esq.
Law Offices of Lawrence G. Soicher
110 East 59th Street, 25th Floor
New York, NY 10022

I declare under penalty of perjury that the foregoing is true and correct. Executed this 13th day of September, 2013, at San Diego, California.

Marianne Maloney