MORGAN STANLEY
Form 10-Q
November 04, 2014
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2014

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

Commission File Number 1-11758

(Exact Name of Registrant as specified in its charter)

Delaware	**1585 Broadway**	**36-3145972**	**(212) 761-4000**
(State or other jurisdiction of incorporation or organization)	**New York, NY 10036** (Address of principal executive offices, including zip code)	(I.R.S. Employer Identification No.)	(Registrant s telephone number, including area code)

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨

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

Large Accelerated Filer x	Accelerated Filer ¨
Non-Accelerated Filer ¨	Smaller reporting company ¨
(Do not check if a smaller reporting company)	

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of October 31, 2014, there were 1,957,403,208 shares of the Registrant s Common Stock, par value $0.01 per share, outstanding.

Table of Contents

QUARTERLY REPORT ON FORM 10-Q

For the quarter ended September 30, 2014

Table of Contents

AVAILABLE INFORMATION

Morgan Stanley files annual, quarterly and current reports, proxy statements and other information with the U.S. Securities and Exchange Commission (the SEC). You may read and copy any document we file with the SEC at the SEC s public reference room at 100 F Street, NE, Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for information on the public reference room. The SEC maintains an internet site that contains annual, quarterly and current reports, proxy and information statements and other information that issuers (including Morgan Stanley) file electronically with the SEC. Morgan Stanley s electronic SEC filings are available to the public at the SEC s internet site, *www.sec.gov*.

Morgan Stanley s internet site is *www.morganstanley.com*. You can access Morgan Stanley s Investor Relations webpage at *www.morganstanley.com/about/ir*. Morgan Stanley makes available free of charge, on or through its Investor Relations webpage, its proxy statements, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and any amendments to those reports filed or furnished pursuant to the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practicable after such material is electronically filed with, or furnished to, the SEC. Morgan Stanley also makes available, through its Investor Relations webpage, via a link to the SEC s internet site, statements of beneficial ownership of Morgan Stanley s equity securities filed by its directors, officers, 10% or greater shareholders and others under Section 16 of the Exchange Act.

Morgan Stanley has a Corporate Governance webpage. You can access information about Morgan Stanley s corporate governance at *www.morganstanley.com/about/company/governance*. Morgan Stanley posts the following on its Corporate Governance webpage:

- Amended and Restated Certificate of Incorporation;
- Amended and Restated Bylaws;
- Charters for its Audit Committee; Operations and Technology Committee; Compensation, Management Development and Succession Committee; Nominating and Governance Committee; and Risk Committee;
- Corporate Governance Policies;
- Policy Regarding Communication with the Board of Directors;
- Policy Regarding Director Candidates Recommended by Shareholders;
- Policy Regarding Corporate Political Activities;
- Policy Regarding Shareholder Rights Plan;
- Code of Ethics and Business Conduct;
- Code of Conduct; and

Integrity Hotline information.

Morgan Stanley s Code of Ethics and Business Conduct applies to all directors, officers and employees, including its Chief Executive Officer, Chief Financial Officer and Deputy Chief Financial Officer. Morgan Stanley will post any amendments to the Code of Ethics and Business Conduct and any waivers that are required to be disclosed by the rules of either the SEC or the New York Stock Exchange LLC (NYSE) on its internet site. You can request a copy of these documents, excluding exhibits, at no cost, by contacting Investor Relations, 1585 Broadway, New York, NY 10036 (212-761-4000). The information on Morgan Stanley s internet site is not incorporated by reference into this report.

Table of Contents

Part I Financial Information.

Item 1. Financial Statements.

MORGAN STANLEY

Condensed Consolidated Statements of Financial Condition

(dollars in millions, except share data)

(unaudited)

	September 30, 2014	December 31, 2013
Assets		
Cash and due from banks ($49 and $544 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	$ 20,242	$ 16,602
Interest bearing deposits with banks	35,584	43,281
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements ($149 and $117 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	45,106	39,203
Trading assets, at fair value ($126,689 and $151,078 were pledged to various parties at September 30, 2014 and December 31, 2013, respectively) ($1,122 and $2,825 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	252,482	280,744
Available for sale securities, at fair value	63,547	53,430
Securities received as collateral, at fair value	16,694	20,508
Federal funds sold and securities purchased under agreements to resell (includes $863 and $866 at fair value at September 30, 2014 and December 31, 2013, respectively)	98,994	118,130
Securities borrowed	140,303	129,707
Customer and other receivables	54,839	57,104
Loans:		
Held for investment (net of allowances of $141 and $156 at September 30, 2014 and December 31, 2013, respectively)	51,465	36,545
Held for sale	6,744	6,329
Other investments ($488 and $561 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	4,515	5,086
Premises, equipment and software costs (net of accumulated depreciation of $6,128 and $6,420 at September 30, 2014 and December 31, 2013, respectively) ($194 and $201 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	5,642	6,019
Goodwill	6,589	6,595
Intangible assets (net of accumulated amortization of $1,924 and $1,703 at September 30, 2014 and December 31, 2013, respectively) (includes $6 and $8 at fair value at September 30, 2014 and December 31, 2013, respectively)	3,054	3,286
Other assets ($15 and $11 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally not available to the Company)	8,711	10,133
Total assets	$ 814,511	$ 832,702
Liabilities		
Deposits (includes $0 and $185 at fair value at September 30, 2014 and December 31, 2013, respectively).	$ 124,382	$ 112,379
Commercial paper and other short-term borrowings (includes $1,473 and $1,347 at fair value at September 30, 2014 and December 31, 2013, respectively)	1,760	2,142
Trading liabilities, at fair value ($1 and $33 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally non-recourse to the Company)	118,896	104,521
Obligation to return securities received as collateral, at fair value	22,944	24,568
Securities sold under agreements to repurchase (includes $609 and $561 at fair value at September 30, 2014 and December 31, 2013, respectively)	83,706	145,676
Securities loaned	27,657	32,799
Other secured financings (includes $4,367 and $5,206 at fair value at September 30, 2014 and December 31, 2013, respectively) ($380 and $543 at September 30, 2014 and December 31, 2013, respectively, related to consolidated	12,019	14,215

variable interest entities, generally non-recourse to the Company)		
Customer and other payables	181,899	157,125
Other liabilities and accrued expenses ($72 and $76 at September 30, 2014 and December 31, 2013, respectively, related to consolidated variable interest entities, generally non-recourse to the Company)	14,880	16,672
Long-term borrowings (includes $33,159 and $35,637 at fair value at September 30, 2014 and December 31, 2013, respectively)	152,357	153,575
Total liabilities	740,500	763,672
Commitments and contingent liabilities (see Note 11)		
Equity		
Morgan Stanley shareholders equity:		
Preferred stock (see Note 13)	6,020	3,220
Common stock, $0.01 par value:		
Shares authorized: 3,500,000,000 at September 30, 2014 and December 31, 2013;		
Shares issued: 2,038,893,979 at September 30, 2014 and December 31, 2013;		
Shares outstanding: 1,958,386,188 and 1,944,868,751 at September 30, 2014 and December 31, 2013, respectively	20	20
Additional paid-in capital	23,922	24,570
Retained earnings	46,573	42,172
Employee stock trusts	2,127	1,718
Accumulated other comprehensive loss	(1,115)	(1,093)
Common stock held in treasury, at cost, $0.01 par value:		
Shares outstanding: 80,507,791 and 94,025,228 at September 30, 2014 and December 31, 2013, respectively	(2,502)	(2,968)
Common stock issued to employee stock trusts	(2,127)	(1,718)
Total Morgan Stanley shareholders equity	72,918	65,921
Nonredeemable noncontrolling interests	1,093	3,109
Total equity	74,011	69,030
Total liabilities and equity	$ 814,511	$ 832,702

See Notes to Condensed Consolidated Financial Statements.

1

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Income

(dollars in millions, except share and per share data)

(unaudited)

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Revenues:				
Investment banking	$ 1,551	$ 1,160	$ 4,492	$ 3,687
Trading	2,448	2,259	7,926	7,847
Investments	138	728	724	1,254
Commissions and fees	1,124	1,079	3,478	3,463
Asset management, distribution and administration fees	2,716	2,389	7,886	7,139
Other	373	231	873	762
Total non-interest revenues	8,350	7,846	25,379	24,152
Interest income	1,384	1,261	3,977	3,873
Interest expense	827	1,151	2,845	3,377
Net interest	557	110	1,132	496
Net revenues	8,907	7,956	26,511	24,648
Non-interest expenses:				
Compensation and benefits	4,214	3,966	12,720	12,284
Occupancy and equipment	350	374	1,069	1,129
Brokerage, clearing and exchange fees	437	416	1,338	1,300
Information processing and communications	396	404	1,231	1,322
Marketing and business development	160	151	472	448
Professional services	522	448	1,506	1,346
Other	608	832	1,653	2,059
Total non-interest expenses	6,687	6,591	19,989	19,888
Income from continuing operations before income taxes	2,220	1,365	6,522	4,760
Provision for income taxes	463	363	1,263	1,288
Income from continuing operations	1,757	1,002	5,259	3,472
Discontinued operations:				
Income (loss) from discontinued operations before income taxes	(8)	14	(11)	(58)
Provision for (benefit from) income taxes	(3)	(2)	(5)	(26)
Income (loss) from discontinued operations	(5)	16	(6)	(32)
Net income	$ 1,752	$ 1,018	$ 5,253	$ 3,440
Net income applicable to redeemable noncontrolling interests				222
Net income applicable to nonredeemable noncontrolling interests	59	112	156	370

Net income applicable to Morgan Stanley	$ 1,693	$ 906	$ 5,097	$ 2,848
Preferred stock dividends and other	64	26	199	229
Earnings applicable to Morgan Stanley common shareholders	$ 1,629	$ 880	$ 4,898	$ 2,619
Amounts applicable to Morgan Stanley:				
Income from continuing operations	$ 1,698	$ 890	$ 5,103	$ 2,880
Income (loss) from discontinued operations	(5)	16	(6)	(32)
Net income applicable to Morgan Stanley	$ 1,693	$ 906	$ 5,097	$ 2,848
Earnings per basic common share:				
Income from continuing operations	$ 0.85	$ 0.45	$ 2.55	$ 1.39
Income (loss) from discontinued operations		0.01	(0.01)	(0.02)
Earnings per basic common share	$ 0.85	$ 0.46	$ 2.54	$ 1.37
Earnings per diluted common share:				
Income from continuing operations	$ 0.83	$ 0.44	$ 2.49	$ 1.36
Income (loss) from discontinued operations		0.01		(0.02)
Earnings per diluted common share	$ 0.83	$ 0.45	$ 2.49	$ 1.34
Dividends declared per common share	$ 0.10	$ 0.05	$ 0.25	$ 0.15
Average common shares outstanding:				
Basic	1,922,995,835	1,909,350,788	1,925,172,108	1,906,097,564
Diluted	1,970,922,473	1,964,812,610	1,970,091,170	1,952,146,477

See Notes to Condensed Consolidated Financial Statements.

2

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Comprehensive Income

(dollars in millions)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	$ 1,752	$ 1,018	$ 5,253	$ 3,440
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments(1)	$ (327)	$ 125	$ (175)	$ (321)
Amortization of cash flow hedges(2)	1	1	3	3
Change in net unrealized gains (losses) on available for sale securities(3)	(102)	33	134	(336)
Pension, postretirement and other related adjustments(4)	(16)	4	(10)	15
Total other comprehensive income (loss)	$ (444)	$ 163	$ (48)	$ (639)
Comprehensive income	$ 1,308	$ 1,181	$ 5,205	$ 2,801
Net income applicable to redeemable noncontrolling interests				222
Net income applicable to nonredeemable noncontrolling interests	59	112	156	370
Other comprehensive income (loss) applicable to nonredeemable noncontrolling interests	(62)	8	(26)	(141)
Comprehensive income applicable to Morgan Stanley	$ 1,311	$ 1,061	$ 5,075	$ 2,350

(1) Amounts are net of provision for (benefit from) income taxes of $249 million and $(124) million for the quarters ended September 30, 2014 and 2013, respectively, and $137 million and $176 million for the nine months ended September 30, 2014 and 2013, respectively.

(2) Amounts are net of provision for income taxes of $1 million and $1 million for the quarters ended September 30, 2014 and 2013, respectively, and $2 million and $2 million for the nine months ended September 30, 2014 and 2013, respectively.

(3) Amounts are net of provision for (benefit from) income taxes of $(70) million and $23 million for the quarters ended September 30, 2014 and 2013, respectively, and $92 million and $(230) million for the nine months ended September 30, 2014 and 2013, respectively.

(4) Amounts are net of provision for (benefit from) income taxes of $(8) million and $2 million for the quarters ended September 30, 2014 and 2013, respectively, and $(6) million and $13 million for the nine months ended September 30, 2014 and 2013, respectively.

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Cash Flows

(dollars in millions)

(unaudited)

	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 5,253	$ 3,440
Adjustments to reconcile net income to net cash provided by operating activities:		
Income from equity method investments	(108)	(400)
Compensation payable in common stock and options	933	850
Depreciation and amortization	748	1,084
Net gain on sale of available for sale securities	(36)	(43)
Impairment charges	85	182
Provision for credit losses on lending activities	1	116
Other operating activities	(167)	58
Changes in assets and liabilities:		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	(5,903)	(6,422)
Trading assets, net of Trading liabilities	39,205	(5,944)
Securities borrowed	(10,596)	(17,468)
Securities loaned	(5,142)	(4,042)
Customer and other receivables and other assets	2,931	6,761
Customer and other payables and other liabilities	23,335	21,500
Federal funds sold and securities purchased under agreements to resell	19,136	424
Securities sold under agreements to repurchase	(61,935)	16,724
Net cash provided by operating activities	7,740	16,820
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from (payments for):		
Premises, equipment and software	(533)	(944)
Business dispositions, net of cash disposed	962	569
Loans	(13,974)	(6,046)
Purchases of available for sale securities	(24,581)	(20,497)
Sales of available for sale securities	11,212	9,052
Maturities and redemptions of available for sale securities	3,415	3,760
Other investing activities	(264)	117
Net cash used for investing activities	(23,763)	(13,989)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net proceeds from (payments for):		
Commercial paper and other short-term borrowings	(382)	195
Noncontrolling interests	(189)	(549)
Other secured financings	(1,725)	(1,395)
Deposits	12,003	21,541
Proceeds from:		
Excess tax benefits associated with stock-based awards	91	8
Derivatives financing activities	784	244
Issuance of preferred stock, net of issuance costs	2,782	854
Issuance of long-term borrowings	26,529	24,766
Payments for:		
Long-term borrowings	(24,731)	(31,084)
Derivatives financing activities	(384)	(237)

Repurchases of common stock and related employee tax withholdings	(1,172)	(451)
Purchase of additional stake in Wealth Management JV		(4,725)
Cash dividends	(652)	(358)
Net cash provided by financing activities	12,954	8,809
Effect of exchange rate changes on cash and cash equivalents	(939)	(298)
Effect of cash and cash equivalents related to variable interest entities	(49)	(465)
Net increase (decrease) in cash and cash equivalents	(4,057)	10,877
Cash and cash equivalents, at beginning of period	59,883	46,904
Cash and cash equivalents, at end of period	$ 55,826	$ 57,781
Cash and cash equivalents include:		
Cash and due from banks	$ 20,242	$ 14,333
Interest bearing deposits with banks	35,584	43,448
Cash and cash equivalents, at end of period	$ 55,826	$ 57,781

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Cash payments for interest were $2,116 million and $3,372 million for the nine months ended September 30, 2014 and 2013, respectively.

Cash payments for income taxes were $620 million and $598 million for the nine months ended September 30, 2014 and 2013, respectively.

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Changes in Total Equity

Nine Months Ended September 30, 2014

(dollars in millions)

(unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Employee Stock Trusts	Accumulated Other Comprehensive Income (Loss)	Common Stock Held in Treasury at Cost	Common Stock Issued to Employee Stock Trusts	Non-redeemable Non-controlling Interests	Total Equity
BALANCE AT DECEMBER 31, 2013	$ 3,220	$ 20	$ 24,570	$ 42,172	$ 1,718	$ (1,093)	$ (2,968)	$ (1,718)	$ 3,109	$ 69,030
Net income applicable to Morgan Stanley				5,097						5,097
Net income applicable to nonredeemable noncontrolling interests									156	156
Dividends				(696)						(696)
Shares issued under employee plans and related tax effects			(627)		409		1,638	(409)		1,011
Repurchases of common stock and related employee tax withholdings							(1,172)			(1,172)
Net change in Accumulated other comprehensive income						(22)			(26)	(48)
Issuance of preferred stock	2,800		(18)							2,782
Deconsolidation of certain legal entities associated with a real estate fund									(1,606)	(1,606)
Other net decreases			(3)						(540)	(543)
BALANCE AT SEPTEMBER 30, 2014	$ 6,020	$ 20	$ 23,922	$ 46,573	$ 2,127	$ (1,115)	$ (2,502)	$ (2,127)	$ 1,093	$ 74,011

See Notes to Condensed Consolidated Financial Statements.

5

Table of Contents

MORGAN STANLEY

Condensed Consolidated Statements of Changes in Total Equity (Continued)

Nine Months Ended September 30, 2013

(dollars in millions)

(unaudited)

	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Employee Stock Trusts	Accumulated Other Comprehensive Income (Loss)	Common Stock Held in Treasury at Cost	Common Stock Issued to Employee Stock Trusts	Non-Redeemable Non-controlling Interests	Total Equity
BALANCE AT DECEMBER 31, 2012	$ 1,508	$ 20	$ 23,426	$ 39,912	$ 2,932	$ (516)	$ (2,241)	$ (2,932)	$ 3,319	$ 65,428
Net income applicable to Morgan Stanley				2,848						2,848
Net income applicable to nonredeemable noncontrolling interests									370	370
Dividends				(372)						(372)
Shares issued under employee plans and related tax effects			817		(1,179)		(28)	1,179		789
Repurchases of common stock and related employee tax withholdings							(451)			(451)
Net change in Accumulated other comprehensive income						(498)			(141)	(639)
Issuance of preferred stock	862		(8)							854
Wealth Management JV redemption value adjustment				(151)						(151)
Other net decreases									(435)	(435)
BALANCE AT SEPTEMBER 30, 2013	$ 2,370	$ 20	$ 24,235	$ 42,237	$ 1,753	$ (1,014)	$ (2,720)	$ (1,753)	$ 3,113	$ 68,241

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Introduction and Basis of Presentation.

The Company. Morgan Stanley, a financial holding company, is a global financial services firm that maintains significant market positions in each of its business segments Institutional Securities, Wealth Management and Investment Management. The Company, through its subsidiaries and affiliates, provides a wide variety of products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals. Unless the context otherwise requires, the terms Morgan Stanley or the Company mean Morgan Stanley (the Parent) together with its consolidated subsidiaries.

A summary of the activities of each of the Company s business segments is as follows:

Institutional Securities provides financial advisory and capital raising services, including: advice on mergers and acquisitions, restructurings, real estate and project finance; corporate lending; sales, trading, financing and market-making activities in equity and fixed income securities and related products, including foreign exchange and commodities; and investment activities.

Wealth Management provides brokerage and investment advisory services to individual investors and small-to-medium sized businesses and institutions covering various investment alternatives; financial and wealth planning services; annuity and other insurance products; credit and other lending products; cash management services; retirement services; and engages in fixed income trading, which primarily facilitates clients trading or investments in such securities.

Investment Management provides a broad array of investment strategies that span the risk/return spectrum across geographies, asset classes and public and private markets to a diverse group of clients across the institutional and intermediary channels as well as high net worth clients.

Global Oil Merchanting Business, CanTerm and TransMontaigne.

On December 20, 2013, the Company and a subsidiary of Rosneft Oil Company (Rosneft) entered into a Purchase Agreement pursuant to which the Company would sell the global oil merchanting unit of its commodities division (the global oil merchanting business) to Rosneft. In the current environment there can be no assurance that the transaction will close, particularly in light of the existing contractual requirement that all necessary approvals be received by December 20, 2014, when the Purchase Agreement will expire. The Company continues to operate the global oil merchanting business in the ordinary course, and should the transaction not close, the Company would consider a variety of options that take into account the interests of the Company s shareholders, clients and employees. For the foregoing reasons, the global oil merchanting business is no longer classified as held for sale.

On March 27, 2014, the Company completed the sale of Canterm Canadian Terminals Inc. (CanTerm), a public storage terminal operator for refined products with two distribution terminals in Canada. Due to a change in the Company s expected level of continuing involvement with CanTerm, it is no longer considered to be a discontinued operation, and as such, the results of CanTerm are reported as a component of continuing operations within the Institutional Securities business segment for all periods presented. As a result of this change, previously disclosed earnings per diluted common share (diluted EPS) from discontinued operations of $0.02 per share are included in diluted EPS from continuing operations for the nine months ended September 30, 2014.

On July 1, 2014, the Company completed the sale of its ownership stake in TransMontaigne Inc., a U.S.-based oil storage, marketing and transportation company, as well as related physical inventory and the assumption of the Company s obligations under certain terminal storage contracts, to NGL Energy Partners LP. The gain on sale, which was included in continuing operations, was approximately $101 million for the quarter and nine months ended September 30, 2014.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Discontinued Operations. Pre-tax gain (loss) amounts for the quarter and nine months ended September 30, 2014 were not significant. Pre-tax gain (loss) amounts for the quarter and nine months ended September 30, 2013 were $14 million and $(58) million, respectively, included in discontinued operations, primarily related to the prior sale of Saxon and a principal investment.

Prior-period amounts have been recast for discontinued operations.

Basis of Financial Information. The condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP), which require the Company to make estimates and assumptions regarding the valuations of certain financial instruments, the valuation of goodwill and intangible assets, compensation, deferred tax assets, the outcome of litigation and tax matters, allowance for credit losses and other matters that affect the condensed consolidated financial statements and related disclosures. The Company believes that the estimates utilized in the preparation of the condensed consolidated financial statements are prudent and reasonable. Actual results could differ materially from these estimates. Intercompany balances and transactions have been eliminated.

The condensed consolidated financial statements should be read in conjunction with the Company s consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2013 (2013 Form 10-K). The condensed consolidated financial statements reflect all adjustments of a normal recurring nature that are, in the opinion of management, necessary for the fair presentation of the results for the interim period. The results of operations for interim periods are not necessarily indicative of results for the entire year.

Consolidation. The condensed consolidated financial statements include the accounts of the Company, its wholly owned subsidiaries and other entities in which the Company has a controlling financial interest, including certain variable interest entities (VIE) (see Note 7). For consolidated subsidiaries that are less than wholly owned, the third-party holdings of equity interests are referred to as noncontrolling interests. The portion of net income attributable to noncontrolling interests for such subsidiaries is presented as either Net income (loss) applicable to redeemable noncontrolling interests or Net income (loss) applicable to nonredeemable noncontrolling interests in the condensed consolidated statements of income. The portion of shareholders equity of such subsidiaries that is redeemable would be presented as Redeemable noncontrolling interests outside of the equity section in the condensed consolidated statements of financial condition. The portion of shareholders equity of such subsidiaries that is nonredeemable is presented as Nonredeemable noncontrolling interests, a component of total equity, in the condensed consolidated statements of financial condition.

For entities where (1) the total equity investment at risk is sufficient to enable the entity to finance its activities without additional subordinated financial support and (2) the equity holders bear the economic residual risks and returns of the entity and have the power to direct the activities of the entity that most significantly affect its economic performance, the Company consolidates those entities it controls either through a majority voting interest or otherwise. For VIEs (*i.e*., entities that do not meet these criteria), the Company consolidates those entities where the Company has the power to make the decisions that most significantly affect the economic performance of the VIE and has the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE, except for certain VIEs that are money market funds, are investment companies or are entities qualifying for accounting purposes as investment companies. Generally, the Company consolidates those entities when it absorbs a majority of the expected losses or a majority of the expected residual returns, or both, of the entities.

For investments in entities in which the Company does not have a controlling financial interest but has significant influence over operating and financial decisions, the Company generally applies the equity method of accounting with net gains and losses recorded within Other revenues. Where the Company has elected to measure certain eligible investments at fair value in accordance with the fair value option, net gains and losses are recorded within Investments revenues (see Note 4).

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Equity and partnership interests held by entities qualifying for accounting purposes as investment companies are carried at fair value.

The Company s significant regulated U.S. and international subsidiaries include Morgan Stanley & Co. LLC (MS&Co.), Morgan Stanley Smith Barney LLC (MSSB LLC), Morgan Stanley & Co. International plc (MSIP), Morgan Stanley MUFG Securities Co., Ltd. (MSMS), Morgan Stanley Bank, N.A. (MSBNA) and Morgan Stanley Private Bank, National Association (MSPBNA).

Income Statement Presentation. The Company, through its subsidiaries and affiliates, provides a wide variety of products and services to a large and diversified group of clients and customers, including corporations, governments, financial institutions and individuals. In connection with the delivery of the various products and services to clients, the Company manages its revenues and related expenses in the aggregate. As such, when assessing the performance of its businesses, primarily in its Institutional Securities business segment, the Company considers its trading, investment banking, commissions and fees, and interest income, along with the associated interest expense, as one integrated activity.

2. Significant Accounting Policies.

For a detailed discussion about the Company s significant accounting policies, see Note 2 to the consolidated financial statements in the 2013 Form 10-K.

During the quarter and nine months ended September 30, 2014, other than the following, no updates were made to the Company s significant accounting policies.

Condensed Consolidated Statements of Cash Flows.

For purposes of the condensed consolidated statements of cash flows, cash and cash equivalents consist of Cash and due from banks and Interest bearing deposits with banks, which are highly liquid investments with original maturities of three months or less, held for investment purposes, and readily convertible to known amounts of cash.

On April 1, 2014, the Company deconsolidated approximately $1.6 billion in total assets that were related to certain legal entities associated with a real estate fund sponsored by the Company. The deconsolidation resulted in a non-cash reduction of assets of $1.3 billion. The Company had no significant non-cash activities in the nine months ended September 30, 2013.

Goodwill.

The Company completed its annual goodwill impairment testing at July 1, 2014. The Company s impairment testing did not indicate any goodwill impairment, as each of the Company s reporting units with goodwill had a fair value that was substantially in excess of its carrying value. Adverse market or economic events could result in impairment charges in future periods.

Accounting Standards Adopted.

Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date. In February 2013, the Financial Accounting Standards Board (the FASB) issued an accounting update that requires an entity to measure obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed at the reporting date, as the sum of the amount the reporting entity agreed to pay and any additional amount the reporting entity expects to

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

pay on behalf of its co-obligors. This update also requires additional disclosures about those obligations. This guidance became effective for the Company retrospectively beginning on January 1, 2014. The adoption of this accounting guidance did not have a material impact on the Company s condensed consolidated financial statements.

Parent s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity. In March 2013, the FASB issued an accounting update requiring the parent entity to release any related cumulative translation adjustment into net income when the parent ceases to have a controlling financial interest in a subsidiary that is a foreign entity. When the parent ceases to have a controlling financial interest in a subsidiary or group of assets that is a business within a foreign entity, the related cumulative translation adjustment would be released into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. This guidance became effective for the Company prospectively beginning on January 1, 2014. The adoption of this accounting guidance did not have a material impact on the Company s condensed consolidated financial statements.

Amendments to the Scope, Measurement, and Disclosure Requirements of an Investment Company. In June 2013, the FASB issued an accounting update that modifies the criteria used in defining an investment company under U.S. GAAP and sets forth certain measurement and disclosure requirements. This update requires an investment company to measure noncontrolling interests in another investment company at fair value and requires an entity to disclose the fact that it is an investment company, and provide information about changes, if any, in its status as an investment company. An entity will also need to include disclosures around financial support that has been provided or is contractually required to be provided to any of its investees. This guidance became effective for the Company prospectively beginning January 1, 2014. The adoption of this accounting guidance did not have a material impact on the Company s condensed consolidated financial statements.

Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. In July 2013, the FASB issued an accounting update providing guidance on the financial statement presentation of an unrecognized tax benefit when a deferred tax asset from a net operating loss carryforward, similar tax loss, or tax credit carryforward exists. This guidance requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to such deferred tax asset if a settlement in such manner is expected in the event the uncertain tax position is disallowed. This guidance became effective for the Company beginning January 1, 2014. This guidance was applied prospectively to unrecognized tax benefits that existed at the effective date. The adoption of this accounting guidance did not have a material impact on the Company s condensed consolidated financial statements.

Accounting for Investments in Qualified Affordable Housing Projects. In January 2014, the FASB issued an accounting update providing guidance on accounting for investments in flow-through limited liability entities that manage or invest in affordable housing projects that qualify for the low-income housing tax credit. The Company adopted this guidance on April 1, 2014, as early adoption is permitted. The adoption of this guidance did not have a material impact on the Company s condensed consolidated financial statements. For further information on the adoption of this guidance, see Note 17.

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. In April 2014, the FASB issued an accounting update that changes the requirements and disclosure for reporting discontinued operations. The new guidance defines a discontinued operation as a disposal of a component or group of components that is disposed of or is classified as held for sale and represents a strategic shift that has (or will have) a major effect on an entity s operations and financial results. Individually significant components that have been disposed of or are held for sale that do not meet the definition of a discontinued operation require new disclosures. The Company adopted this guidance on April 1, 2014, as early adoption is permitted. The adoption of this guidance did not have a material impact on the Company s condensed consolidated financial statements.

3. Wealth Management JV.

In 2009, the Company and Citigroup Inc. (Citi) consummated the combination of each institution s respective wealth management business. The combined businesses operated as the Wealth Management JV . Prior to September 2012, the Company owned 51% and Citi owned 49% of the Wealth Management JV. In September 2012, the Company purchased an additional 14% stake in the Wealth Management JV from Citi for $1.89 billion, increasing the Company s interest from 51% to 65%. In June 2013, the Company purchased the remaining 35% stake in the Wealth Management JV for $4.725 billion, increasing the Company s interest from 65% to 100%.

For the quarters ended September 30, 2014 and 2013 and the nine months ended September 30, 2014, no results were attributed to Citi since the Company owned 100% of the Wealth Management JV. For the nine months ended September 30, 2013, Citi s 35% interest was reported on the balance sheet as redeemable noncontrolling interest and the results related to its 35% interest were reported in net income (loss) applicable to redeemable noncontrolling interests in the condensed consolidated statement of income.

Concurrent with the acquisition of the remaining 35% stake in the Wealth Management JV, the deposit sweep agreement between Citi and the Company was terminated. During the quarter and nine months ended September 30, 2014, $5 billion and $14 billion, respectively, of deposits held by Citi relating to the Company s customer accounts were transferred to the Company s depository institutions. At September 30, 2014, approximately $13 billion of additional deposits are scheduled to be transferred to the Company s depository institutions on an agreed-upon basis through June 2015.

4. Fair Value Disclosures.

Fair Value Measurements.

For a description of the valuation techniques applied to the Company s major categories of assets and liabilities measured at fair value on a recurring basis, see Note 4 to the consolidated financial statements in the 2013 Form 10-K.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following fair value hierarchy tables present information about the Company s assets and liabilities measured at fair value on a recurring basis at September 30, 2014 and December 31, 2013.

Assets and Liabilities Measured at Fair Value on a Recurring Basis at September 30, 2014.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at September 30, 2014
			(dollars in millions)		
Assets at Fair Value					
Trading assets:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 19,259	$	$	$	$ 19,259
U.S. agency securities	976	13,788			14,764
Total U.S. government and agency securities	20,235	13,788			34,023
Other sovereign government obligations	22,746	7,982	13		30,741
Corporate and other debt:					
State and municipal securities		1,656			1,656
Residential mortgage-backed securities		1,486	81		1,567
Commercial mortgage-backed securities		1,428	57		1,485
Asset-backed securities		773	111		884
Corporate bonds		17,007	506		17,513
Collateralized debt and loan obligations		627	1,271		1,898
Loans and lending commitments		6,436	7,507		13,943
Other debt		1,420	155		1,575
Total corporate and other debt		30,833	9,688		40,521
Corporate equities(1)	102,539	1,011	241		103,791
Derivative and other contracts:					
Interest rate contracts	665	438,182	2,685		441,532
Credit contracts		30,381	1,597		31,978
Foreign exchange contracts	71	70,609	265		70,945
Equity contracts	1,209	54,189	1,353		56,751
Commodity contracts	3,133	10,101	2,177		15,411
Other		251			251
Netting(2)	(4,017)	(511,875)	(4,130)	(61,831)	(581,853)
Total derivative and other contracts	1,061	91,838	3,947	(61,831)	35,015
Investments:					
Private equity funds			2,493		2,493
Real estate funds		6	1,811		1,817
Hedge funds		351	364		715
Principal investments	66	5	913		984
Other	202	70	393		665
Total investments	268	432	5,974		6,674

Physical commodities		1,717			1,717
Total trading assets	146,849	147,601	19,863	(61,831)	252,482
Available for sale securities	33,367	30,180			63,547
Securities received as collateral	16,652	42			16,694
Federal funds sold and securities purchased under agreements to resell		863			863
Intangible assets(3)			6		6
Total assets measured at fair value	$ 196,868	$ 178,686	$ 19,869	$ (61,831)	$ 333,592

12

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Counterparty and Cash Collateral Netting	Balance at September 30, 2014
			(dollars in millions)		
Liabilities at Fair Value					
Commercial paper and other short-term borrowings	$	$ 1,473	$	$	$ 1,473
Trading liabilities:					
U.S. government and agency securities:					
U.S. Treasury securities	16,718				16,718
U.S. agency securities	1,157	83			1,240
Total U.S. government and agency securities	17,875	83			17,958
Other sovereign government obligations	16,974	2,486	2		19,462
Corporate and other debt:					
State and municipal securities		4			4
Corporate bonds		6,057	48		6,105
Collateralized debt and loan obligations		1			1
Unfunded lending commitments		3			3
Other debt		251	35		286
Total corporate and other debt		6,316	83		6,399
Corporate equities(1)	34,487	1,531	3		36,021
Derivative and other contracts:					
Interest rate contracts	492	417,021	2,672		420,185
Credit contracts		29,330	2,279		31,609
Foreign exchange contracts	2	70,012	111		70,125
Equity contracts	920	59,026	2,541		62,487
Commodity contracts	3,023	10,887	1,010		14,920
Other		43			43
Netting(2)	(4,017)	(511,875)	(4,130)	(40,291)	(560,313)
Total derivative and other contracts	420	74,444	4,483	(40,291)	39,056
Total trading liabilities	69,756	84,860	4,571	(40,291)	118,896
Obligation to return securities received as collateral	22,880	64			22,944
Securities sold under agreements to repurchase		456	153		609
Other secured financings		4,205	162		4,367
Long-term borrowings		31,238	1,921		33,159
Total liabilities measured at fair value	$ 92,636	$ 122,296	$ 6,807	$ (40,291)	$ 181,448

(1) The Company holds or sells short for trading purposes equity securities issued by entities in diverse industries and of varying size.
(2) For positions with the same counterparty that cross over the levels of the fair value hierarchy, both counterparty netting and cash collateral netting are included in the column titled Counterparty and Cash Collateral Netting. For contracts with the same counterparty, counterparty netting among positions classified within the same level is included within that level. For further information on derivative instruments and hedging activities, see Note 10.

(3) Amount represents mortgage servicing rights (MSR) accounted for at fair value.

Transfers Between Level 1 and Level 2 During the Quarter and Nine Months Ended September 30, 2014.

For assets and liabilities that were transferred between Level 1 and Level 2 during the period, fair values are ascribed as if the assets or liabilities had been transferred as of the beginning of the period.

In the quarter and nine months ended September 30, 2014, there were no material transfers between Level 1 and Level 2.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Assets and Liabilities Measured at Fair Value on a Recurring Basis at December 31, 2013.

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3) (dollars in millions)	Counterparty and Cash Collateral Netting	Balance at December 31, 2013
Assets at Fair Value					
Trading assets:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 32,083	$	$	$	$ 32,083
U.S. agency securities	1,216	17,720			18,936
Total U.S. government and agency securities	33,299	17,720			51,019
Other sovereign government obligations	25,363	6,610	27		32,000
Corporate and other debt:					
State and municipal securities		1,615			1,615
Residential mortgage-backed securities		2,029	47		2,076
Commercial mortgage-backed securities		1,534	108		1,642
Asset-backed securities		878	103		981
Corporate bonds		16,592	522		17,114
Collateralized debt and loan obligations		802	1,468		2,270
Loans and lending commitments		7,483	5,129		12,612
Other debt		6,365	27		6,392
Total corporate and other debt		37,298	7,404		44,702
Corporate equities(1)	107,818	1,206	190		109,214
Derivative and other contracts:					
Interest rate contracts	750	526,127	2,475		529,352
Credit contracts		42,258	2,088		44,346
Foreign exchange contracts	52	61,570	179		61,801
Equity contracts	1,215	51,656	1,234		54,105
Commodity contracts	2,396	8,595	2,380		13,371
Other		43			43
Netting(2)	(3,836)	(606,878)	(4,931)	(54,906)	(670,551)
Total derivative and other contracts	577	83,371	3,425	(54,906)	32,467
Investments:					
Private equity funds			2,531		2,531
Real estate funds		6	1,637		1,643
Hedge funds		377	432		809
Principal investments	43	42	2,160		2,245
Other	202	45	538		785
Total investments	245	470	7,298		8,013
Physical commodities		3,329			3,329
Total trading assets	167,302	150,004	18,344	(54,906)	280,744
Available for sale securities	24,412	29,018			53,430

Securities received as collateral	20,497	11			20,508
Federal funds sold and securities purchased under agreements to resell		866			866
Intangible assets(3)			8		8
Total assets measured at fair value	$ 212,211	$ 179,899	$ 18,352	$ (54,906)	$ 355,556

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3) (dollars in millions)	Counterparty and Cash Collateral Netting	Balance at December 31, 2013
Liabilities at Fair Value					
Deposits	$	$ 185	$	$	$ 185
Commercial paper and other short-term borrowings		1,346	1		1,347
Trading liabilities:					
U.S. government and agency securities:					
U.S. Treasury securities	15,963				15,963
U.S. agency securities	2,593	116			2,709
Total U.S. government and agency securities	18,556	116			18,672
Other sovereign government obligations	14,717	2,473			17,190
Corporate and other debt:					
State and municipal securities		15			15
Corporate bonds		5,033	22		5,055
Collateralized debt and loan obligations		3			3
Unfunded lending commitments		127	2		129
Other debt		1,144	48		1,192
Total corporate and other debt		6,322	72		6,394
Corporate equities(1)	27,983	513	8		28,504
Derivative and other contracts:					
Interest rate contracts	675	504,292	2,362		507,329
Credit contracts		40,391	2,235		42,626
Foreign exchange contracts	23	61,925	111		62,059
Equity contracts	1,033	57,797	2,065		60,895
Commodity contracts	2,637	8,749	1,500		12,886
Other		72	4		76
Netting(2)	(3,836)	(606,878)	(4,931)	(36,465)	(652,110)
Total derivative and other contracts	532	66,348	3,346	(36,465)	33,761
Total trading liabilities	61,788	75,772	3,426	(36,465)	104,521
Obligation to return securities received as collateral	24,549	19			24,568
Securities sold under agreements to repurchase		407	154		561
Other secured financings		4,928	278		5,206
Long-term borrowings		33,750	1,887		35,637
Total liabilities measured at fair value	$ 86,337	$ 116,407	$ 5,746	$ (36,465)	$ 172,025

(1) The Company holds or sells short for trading purposes equity securities issued by entities in diverse industries and of varying size.

(2) For positions with the same counterparty that cross over the levels of the fair value hierarchy, both counterparty netting and cash collateral netting are included in the column titled Counterparty and Cash Collateral Netting. For contracts with the same counterparty, counterparty netting among positions classified within the same level is included within that level. For further information on derivative instruments and hedging activities, see Note 10.

(3) Amount represents MSRs accounted for at fair value.

Transfers Between Level 1 and Level 2 During the Quarter and Nine Months Ended September 30, 2013.

For assets and liabilities that were transferred between Level 1 and Level 2 during the period, fair values are ascribed as if the assets or liabilities had been transferred as of the beginning of the period.

In the quarter and nine months ended September 30, 2013, there were no material transfers between Level 1 and Level 2.

Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis.

The following tables present additional information about Level 3 assets and liabilities measured at fair value on a recurring basis for the quarters and nine months ended September 30, 2014 and 2013, respectively. Level 3 instruments

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

may be hedged with instruments classified in Level 1 and Level 2. As a result, the realized and unrealized gains (losses) for assets and liabilities within the Level 3 category presented in the tables below do not reflect the related realized and unrealized gains (losses) on hedging instruments that have been classified by the Company within the Level 1 and/or Level 2 categories.

Additionally, both observable and unobservable inputs may be used to determine the fair value of positions that the Company has classified within the Level 3 category. As a result, the unrealized gains (losses) during the period for assets and liabilities within the Level 3 category presented in the tables below may include changes in fair value during the period that were attributable to both observable (*e.g.*, changes in market interest rates) and unobservable (*e.g.*, changes in unobservable long-dated volatilities) inputs.

For assets and liabilities that were transferred into Level 3 during the period, gains (losses) are presented as if the assets or liabilities had been transferred into Level 3 at the beginning of the period; similarly, for assets and liabilities that were transferred out of Level 3 during the period, gains (losses) are presented as if the assets or liabilities had been transferred out at the beginning of the period.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Quarter Ended September 30, 2014.

	Beginning Balance at June 30, 2014	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2014	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2014(2)
				(dollars in millions)					
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 14	$ (1)	$	$ (1)	$	$	$ 1	$ 13	$ (1)
Corporate and other debt:									
State and municipal securities	4						(4)		
Residential mortgage-backed securities	55	11	33	(7)		(11)		81	11
Commercial mortgage-backed securities	47	(1)	1	(3)			13	57	(2)
Asset-backed securities	65	5	27	(8)			22	111	5
Corporate bonds	510	36	99	(148)			9	506	38
Collateralized debt and loan obligations	1,332	8	299	(362)		(6)		1,271	6
Loans and lending commitments	5,829	(20)	2,138	(676)		(721)	957	7,507	(24)
Other debt	22		135	(3)			1	155	
Total corporate and other debt	7,864	39	2,732	(1,207)		(738)	998	9,688	34
Corporate equities	243	(2)	30	(41)			11	241	7
Net derivative and other contracts(3):									
Interest rate contracts	(109)	(15)	7		(3)	(17)	150	13	(22)
Credit contracts	(710)	209	7		(64)	(108)	(16)	(682)	140
Foreign exchange contracts	109	(27)	6	(3)		70	(1)	154	(25)
Equity contracts	(1,097)	(6)	56		(59)	(105)	23	(1,188)	(9)
Commodity contracts	1,132	73	36			(62)	(12)	1,167	12
Other	(3)	(1)				4			
Total net derivative and other contracts	(678)	233	112	(3)	(126)	(218)	144	(536)	96
Investments:									
Private equity funds	2,555	60	31	(153)				2,493	11
Real estate funds	1,813	67	8	(77)				1,811	86
Hedge funds	371	(1)	1	(23)			16	364	(1)
Principal investments	883	(1)	22	(23)			32	913	(1)
Other	380	(3)	14				2	393	(3)
Total investments	6,002	122	76	(276)			50	5,974	92
Intangible assets	6							6	
Liabilities at Fair Value									
Trading liabilities:									
Other sovereign government obligations	$	$	$	$	$	$	$ 2	$ 2	$
Corporate and other debt:									
Corporate bonds	14	1	(8)	46			(3)	48	1
Unfunded lending commitments	12	12							

Other debt	42	5				(2)		35	5
Total corporate and other debt	68	18	(8)	46		(2)	(3)	83	6
Corporate equities	6	(5)	(12)	2			2	3	(4)
Securities sold under agreements to repurchase	155	2						153	2
Other secured financings	135				4	(3)	26	162	
Long-term borrowings	1,779	72			136	(108)	186	1,921	72

(1) Total realized and unrealized gains (losses) are primarily included in Trading revenues in the condensed consolidated statements of income except for $122 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the quarter ended September 30, 2014 related to assets and liabilities still outstanding at September 30, 2014.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 10.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In the quarter ended September 30, 2014, there were no material transfers into or out of Level 3.

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Nine Months Ended September 30, 2014.

	Beginning Balance at December 31, 2013	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2014	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2014(2)
					(dollars in millions)				
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 27	$ (1)	$ 7	$ (21)	$	$	$ 1	$ 13	$ (1)
Corporate and other debt:									
Residential mortgage-backed securities	47	34	30	(9)		(20)	(1)	81	29
Commercial mortgage-backed securities	108	11	22	(97)			13	57	(3)
Asset-backed securities	103	(3)	58	(93)			46	111	(3)
Corporate bonds	522	107	185	(302)			(6)	506	84
Collateralized debt and loan obligations	1,468	137	716	(940)		(109)	(1)	1,271	45
Loans and lending commitments	5,129	(202)	3,962	(327)		(1,299)	244	7,507	(181)
Other debt	27	4	128	(6)		(2)	4	155	3
Total corporate and other debt	7,404	88	5,101	(1,774)		(1,430)	299	9,688	(26)
Corporate equities	190	17	83	(47)			(2)	241	10
Net derivative and other contracts(3):									
Interest rate contracts	113	(4)	8		(3)	(61)	(40)	13	4
Credit contracts	(147)	(434)	52		(118)	10	(45)	(682)	(475)
Foreign exchange contracts	68	(6)	6	(1)		106	(19)	154	(2)
Equity contracts	(831)	(19)	223	(1)	(273)	(370)	83	(1,188)	(66)
Commodity contracts	880	177	200			(90)		1,167	99
Other	(4)	(1)				5			
Total net derivative and other contracts	79	(287)	489	(2)	(394)	(400)	(21)	(536)	(440)
Investments:									
Private equity funds	2,531	357	141	(537)			1	2,493	130
Real estate funds	1,637	212	142	(180)				1,811	263
Hedge funds	432	17	36	(44)			(77)	364	17
Principal investments	2,160	49	36	(124)		(1,234)	26	913	129
Other	538	(13)	17	(11)			(138)	393	(6)
Total investments	7,298	622	372	(896)		(1,234)	(188)	5,974	533
Intangible assets	8					(2)		6	(1)

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at December 31, 2013	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2014	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2014(2)
	(dollars in millions)								
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 1	$	$	$	$	$ (1)	$	$	$
Trading liabilities:									
Other sovereign government obligations							2	2	
Corporate and other debt:									
Corporate bonds	22	2	(46)	85			(11)	48	3
Unfunded lending commitments	2	2							
Other debt	48	15				1	1	35	5
Total corporate and other debt	72	19	(46)	85		1	(10)	83	8
Corporate equities	8	(6)	(16)	2			3	3	(6)
Securities sold under agreements to repurchase	154	1						153	1
Other secured financings	278	(9)			21	(188)	42	162	(6)
Long-term borrowings	1,887	17			372	(289)	(32)	1,921	15

(1) Total realized and unrealized gains (losses) are primarily included in Trading revenues in the condensed consolidated statements of income except for $622 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the nine months ended September 30, 2014 related to assets and liabilities still outstanding at September 30, 2014.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 10.

In the nine months ended September 30, 2014, there were no material transfers into or out of Level 3.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Quarter Ended September 30, 2013.

	Beginning Balance at June 30, 2013	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2013(2)
					(dollars in millions)				
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 4	$	$ 2	$ (4)	$	$	$	$ 2	$
Corporate and other debt:									
Residential mortgage-backed securities	19	(2)	72	(3)			4	90	(3)
Commercial mortgage-backed securities	181	(2)	39	(61)			(7)	150	5
Asset-backed securities	108		13	(23)			1	99	
Corporate bonds	509	43	76	(79)			(12)	537	36
Collateralized debt obligations	1,333	60	269	(206)		(55)	(21)	1,380	28
Loans and lending commitments	5,243	(72)	530	(112)		(1,279)	(212)	4,098	(111)
Other debt	12		14	(5)				21	
Total corporate and other debt	7,405	27	1,013	(489)		(1,334)	(247)	6,375	(45)
Corporate equities	256	(25)	38	(20)			(6)	243	(3)
Net derivative and other contracts(3):									
Interest rate contracts	16	262	4		(72)	11	89	310	111
Credit contracts	685	(259)	41		(46)	(146)	435	710	(448)
Foreign exchange contracts	(96)	6				61	(6)	(35)	6
Equity contracts	(1,284)	(309)	102		(190)	39	11	(1,631)	(429)
Commodity contracts	781	45	4		(1)	23	3	855	73
Other	(6)					5		(1)	(2)
Total net derivative and other contracts	96	(255)	151		(309)	(7)	532	208	(689)
Investments:									
Private equity funds	2,286	213	24	(74)				2,449	163
Real estate funds	1,422	159	18	(76)				1,523	196
Hedge funds	407	5	7	(17)			29	431	5
Principal investments	2,822	84	10	(125)			(453)	2,338	71
Other	385	16	3				90	494	16
Total investments	7,322	477	62	(292)			(334)	7,235	451
Intangible assets	9					(1)		8	

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at June 30, 2013	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2013(2)
	(dollars in millions)								
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$	$	$	$	$	$	$ 3	$ 3	$
Trading liabilities:									
Corporate and other debt:									
Residential mortgage-backed securities	4							4	
Corporate bonds	42	(15)	(64)	26			(14)	5	(17)
Unfunded lending commitments	8	4						4	4
Other debt	11	1	(1)					9	
Total corporate and other debt	65	(10)	(65)	26			(14)	22	(13)
Corporate equities	16	(5)	(19)	8				10	(9)
Securities sold under agreements to repurchase	148	(2)						150	(2)
Other secured financings	256	(5)				(1)		260	(5)
Long-term borrowings	2,705	(98)			188	(344)	(334)	2,313	(89)

(1) Total realized and unrealized gains (losses) are primarily included in Trading revenues in the condensed consolidated statements of income except for $477 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for the quarter ended September 30, 2013 related to assets and liabilities still outstanding at September 30, 2013.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 10.

21

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Changes in Level 3 Assets and Liabilities Measured at Fair Value on a Recurring Basis for the Nine Months Ended September 30, 2013.

	Beginning Balance at December 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2013(2)
	(dollars in millions)								
Assets at Fair Value									
Trading assets:									
Other sovereign government obligations	$ 6	$	$ 3	$ (8)	$	$	$ 1	$ 2	$
Corporate and other debt:									
Residential mortgage-backed securities	45	29	85	(45)			(24)	90	8
Commercial mortgage-backed securities	232	6	78	(166)				150	7
Asset-backed securities	109	1	4	(15)				99	
Corporate bonds	660	64	327	(462)		(12)	(40)	537	15
Collateralized debt and loan obligations	1,951	276	612	(1,405)		(53)	(1)	1,380	118
Loans and lending commitments	4,694	(308)	1,607	(316)		(1,838)	259	4,098	(306)
Other debt	45	(3)	15	(36)				21	1
Total corporate and other debt	7,736	65	2,728	(2,445)		(1,903)	194	6,375	(157)
Corporate equities	288	(36)	142	(164)			13	243	(4)
Net derivative and other contracts(3):									
Interest rate contracts	(82)	237	10		(86)	185	46	310	157
Credit contracts	1,822	(1,133)	184		(278)	(369)	484	710	(1,187)
Foreign exchange contracts	(359)	117				215	(8)	(35)	106
Equity contracts	(1,144)	(293)	123	(1)	(232)	(156)	72	(1,631)	(369)
Commodity contracts	709	90	40		(19)	36	(1)	855	124
Other	(7)	(4)				10		(1)	(6)
Total net derivative and other contracts	939	(986)	357	(1)	(615)	(79)	593	208	(1,175)
Investments:									
Private equity funds	2,179	432	96	(258)				2,449	409
Real estate funds	1,370	287	61	(195)				1,523	402
Hedge funds	552	5	46	(154)			(18)	431	6
Principal investments	2,833	96	106	(286)			(411)	2,338	63
Other	486	36	3	(30)			(1)	494	37
Total investments	7,420	856	312	(923)			(430)	7,235	917
Intangible assets	7	7				(6)		8	3

22

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Beginning Balance at December 31, 2012	Total Realized and Unrealized Gains (Losses)(1)	Purchases	Sales	Issuances	Settlements	Net Transfers	Ending Balance at September 30, 2013	Unrealized Gains (Losses) for Level 3 Assets/ Liabilities Outstanding at September 30, 2013(2)
					(dollars in millions)				
Liabilities at Fair Value									
Commercial paper and other short-term borrowings	$ 19	$	$	$	$	$ (1)	$ (15)	$ 3	$
Trading liabilities:									
Corporate and other debt:									
Residential mortgage-backed securities	4							4	
Corporate bonds	177	(5)	(154)	76			(99)	5	(5)
Unfunded lending commitments	46	42						4	42
Other debt	49	13	(31)	2			2	9	6
Total corporate and other debt	276	50	(185)	78			(97)	22	43
Corporate equities	5	(1)	(19)	24			(1)	10	(10)
Securities sold under agreements to repurchase	151	1						150	1
Other secured financings	406	23			13	(136)		260	16
Long-term borrowings	2,789	(87)			875	(468)	(970)	2,313	(89)

(1) Total realized and unrealized gains (losses) are primarily included in Trading revenues in the condensed consolidated statements of income except for $856 million related to Trading assets Investments, which is included in Investments revenues.

(2) Amounts represent unrealized gains (losses) for nine months ended September 30, 2013 related to assets and liabilities still outstanding at September 30, 2013.

(3) Net derivative and other contracts represent Trading assets Derivative and other contracts, net of Trading liabilities Derivative and other contracts. For further information on derivative instruments and hedging activities, see Note 10.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Quantitative Information about and Sensitivity of Significant Unobservable Inputs Used in Recurring Level 3 Fair Value Measurements at September 30, 2014 and December 31, 2013.

The disclosures below provide information on the valuation techniques, significant unobservable inputs and their ranges and averages for each major category of assets and liabilities measured at fair value on a recurring basis with a significant Level 3 balance. The level of aggregation and breadth of products cause the range of inputs to be wide and not evenly distributed across the inventory. Further, the range of unobservable inputs may differ across firms in the financial services industry because of diversity in the types of products included in each firm s inventory. The following disclosures also include qualitative information on the sensitivity of the fair value measurements to changes in the significant unobservable inputs.

At September 30, 2014.

	Balance at September 30, 2014 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Assets					
Trading assets:					
Corporate and other debt:					
Residential mortgage-backed securities	$ 81	Comparable pricing	Comparable bond price / (A)	3 to 9 points	5 points
Commercial mortgage-backed securities	57	Comparable pricing	Comparable bond price / (A)	0 to 19 points	7 points
Asset-backed securities	111	Comparable pricing	Comparable bond price / (A)	4 to 80 points	31 points
Corporate bonds	506	Comparable pricing	Comparable bond price / (A)	1 to 160 points	77 points
Collateralized debt and loan obligations	1,271	Comparable pricing(6)	Comparable bond price / (A)	20 to 105 points	78 points
		Correlation model	Credit correlation / (B)	53 to 58 %	53%
Loans and lending commitments	7,507	Corporate loan model	Credit spread / (C)	30 to 528 basis points	266 basis points
		Margin loan model	Credit spread / (C)(D)	150 to 300 basis points	181 basis points
			Volatility skew / (C)(D)	4 to 24 %	19%
			Discount rate / (C)(D)	2 to 3 %	3%
		Option model	Volatility skew / (C)	-1 to 0 %	0%
		Comparable pricing(6)	Comparable loan price / (A)	5 to 105 points	92 points
Other debt	155	Comparable pricing	Comparable bond price / (A)	15 to 21 points	18 points
		Option model(6)	At the money volatility / (A)	15 to 54 %	16%
Corporate equities(3)	241	Net asset value	Discount to net asset value / (C)	0 to 79 %	39%
		Comparable pricing(6)	Comparable equity price / (A)	100 %	100%
		Market approach	EBITDA multiple / (A)(D)	6 to 10 times	7 times
			Price/Book ratio / (A)(D)	0 times	0 times
Net derivative and other contracts:					
Interest rate contracts	13	Option model	Interest rate volatility concentration liquidity multiple / (C)(D)	0 to 3 times	2 times

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Balance at September 30, 2014 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
			Interest rate - Foreign exchange correlation / (A)(D)	27 to 62 %	42% / 40%(4)
			Interest rate volatility skew / (A)(D)	27 to 82 %	39% / 32%(4)
			Interest rate quanto correlation / (A)(D)	-13 to 35 %	3% / -8%(4)
			Interest rate curve correlation / (A)(D)	46 to 86 %	69% / 64%(4)
			Inflation volatility / (A)(D)	79 %	79% / 79%(4)
			Interest rate - Inflation correlation / (A)(D)	-39 to -41 %	-41% / -41%(4)
Credit contracts	(682)	Comparable pricing	Cash synthetic basis / (C)(D)	5 to 13 points	10 points
			Comparable bond price / (C)(D)	0 to 55 points	18 points
		Correlation model(6)	Credit correlation / (B)	49 to 78 %	61%
Foreign exchange contracts(5)	154	Option model	Comparable bond price / (A)(D)	1 to 11 points	8 points / 9 points(4)
			Interest rate quanto correlation / (A)(D)	-13 to 35 %	3% / -8%(4)
			Interest rate - Credit spread correlation / (A)(D)	-26 to 34 %	-6% / -8%(4)
			Interest rate curve correlation / (A)(D)	46 to 86 %	69% / 64%(4)
			Interest rate - Foreign exchange correlation / (A)(D)	27 to 62 %	42% / 40%(4)
			Interest rate volatility skew / (A)(D)	27 to 82 %	39% / 32%(4)
			Interest rate curve / (A)(D)	0 to 1 %	0% / 0%(4)
Equity contracts(5)	(1,188)	Option model	At the money volatility / (A)(D)	14 to 64 %	35%
			Volatility skew / (A)(D)	-4 to 1 %	-1%
			Equity - Equity correlation / (C)(D)	30 to 99 %	67%
			Equity - Foreign exchange correlation / (C)(D)	-60 to 10 %	-19%
			Equity - Interest rate correlation / (C)(D)	-17 to 71 %	27% / 12%(4)
Commodity contracts	1,167	Option model	Forward power price / (C)(D)	$10 to $100 per Megawatt hour	$37 per Megawatt hour
			Commodity volatility / (A)(D)	10 to 69 %	18%
			Cross commodity correlation / (C)(D)	28 to 100 %	88%
Investments(3):					
Principal investments	913	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	12%	12%
			Exit multiple / (A)(D)	10 times	10 times
		Discounted cash flow	Equity discount rate / (C)	25 %	25%
		Market approach	EBITDA multiple / (A)(D)	4 to 18 times	7 times
			Price / Earnings ratio / (A)(D)	21 to 24 times	22 times
			Forward capacity price / (A)(D)	$5 to $7	$7
		Comparable pricing(6)	Comparable equity price / (A)	86% to 100%	93%
Other	393	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	11 to 13 %	11%
			Exit multiple / (A)(D)	5 to 8 times	8 times
		Market approach(6)	EBITDA multiple / (A)(D)	9 to 12 times	10 times
			Price / Earnings ratio / (A)(D)	20 times	20 times
		Comparable pricing	Comparable equity price / (A)	100%	100%
Liabilities					
Securities sold under agreements to repurchase	$ 153	Discounted cash flow	Funding spread / (A)	75 to 90 basis points	86 basis points

Other secured financings	162	Comparable pricing	Comparable bond price / (A)	99 to 101 points	100 points
		Discounted cash flow	Discount rate / (C)	19 %	19%
		Discounted cash flow(6)	Funding spread / (A)	84 to 104 basis points	99 basis points

25

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Balance at September 30, 2014 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s) / Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Long-term borrowings	1,921	Option model	At the money volatility / (C)(D)	22 to 44 %	34%
			Volatility skew / (A)(D)	-2 to 0 %	0%
			Equity - Equity correlation / (A)(D)	32 to 90 %	67%
			Equity - Foreign exchange correlation / (C)(D)	-85 to 30 %	-30%
		Option model	Equity alpha / (A)	5 to 90 %	47%
		Correlation model	Credit correlation / (B)	50 to 57 %	51%

EBITDA Earnings before interest, taxes, depreciation and amortization

(1) The ranges of significant unobservable inputs are represented in points, percentages, basis points, times or megawatt hours. Points are a percentage of par; for example, 9 points would be 9% of par. A basis point equals 1/100th of 1%; for example, 528 basis points would equal 5.28%.
(2) Amounts represent weighted averages except where simple averages and the median of the inputs are provided (see footnote 4 below). Weighted averages are calculated by weighting each input by the fair value of the respective financial instruments except for collateralized debt and loan obligations, principal investments, other debt, long-term borrowings and derivative instruments where some or all inputs are weighted by risk.
(3) Investments in funds measured using an unadjusted net assets value (NAV) are excluded.
(4) The data structure of the significant unobservable inputs used in valuing Interest rate contracts, Foreign exchange contracts and certain Equity contracts may be in a multi-dimensional form, such as a curve or surface, with risk distributed across the structure. Therefore, a simple average and median, together with the range of data inputs, may be more appropriate measurements than a single point weighted average.
(5) Includes derivative contracts with multiple risks (*i.e.,* hybrid products).
(6) This is the predominant valuation technique for this major asset or liability class.

Sensitivity of the fair value to changes in the unobservable inputs:

(A) Significant increase (decrease) in the unobservable input in isolation would result in a significantly higher (lower) fair value measurement.
(B) Significant changes in credit correlation may result in a significantly higher or lower fair value measurement. Increasing (decreasing) correlation drives a redistribution of risk within the capital structure such that junior tranches become less (more) risky and senior tranches become more (less) risky.
(C) Significant increase (decrease) in the unobservable input in isolation would result in a significantly lower (higher) fair value measurement.
(D) There are no predictable relationships between the significant unobservable inputs.

At December 31, 2013.

	Balance at December 31, 2013 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s)/ Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Assets					
Trading assets:					
Corporate and other debt:					
Commercial mortgage-backed securities	$ 108	Comparable pricing	Comparable bond price / (A)	40 to 93 points	78 points
Asset-backed securities	103	Discounted cash flow	Discount rate / (C)	18%	18%
Corporate bonds	522	Comparable pricing	Comparable bond price / (A)	1 to 159 points	85 points
	1,468	Comparable pricing(6)	Comparable bond price / (A)	18 to 99 points	73 points

Collateralized debt and loan obligations					
		Correlation model	Credit correlation / (B)	29 to 59 %	43%
Loans and lending commitments	5,129	Corporate loan model	Credit spread / (C)	28 to 487 basis points	249 basis points
		Margin loan model	Credit spread / (C)(D)	10 to 265 basis points	135 basis points
			Volatility skew / (C)(D)	3 to 40 %	14%
			Comparable bond price / (A)(D)	80 to 120 points	100 points
		Option model	Volatility skew / (C)	-1 to 0 %	0%
		Comparable pricing(6)	Comparable loan price / (A)	10 to 100 points	76 points

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Balance at December 31, 2013 (dollars in millions)	Valuation Technique(s)	Significant Unobservable Input(s)/ Sensitivity of the Fair Value to Changes in the Unobservable Inputs	Range(1)	Averages(2)
Corporate equities(3)	190	Net asset value(6)	Discount to net asset value / (C)	0 to 85 %	43%
		Comparable pricing	Comparable equity price / (A)	100 %	100%
		Comparable pricing	Comparable price / (A)	100 %	100%
		Market approach	EBITDA multiple / (A)(D)	5 to 9 times	6 times
			Price/Book ratio / (A)(D)	0 to 1 times	1 times
Net derivative and other contracts:					
Interest rate contracts	113	Option model	Interest rate volatility concentration liquidity multiple / (C)(D)	0 to 6 times	2 times
			Comparable bond price / (A)(D)	5 to 100 points	58 points / 65 points(4)
			Interest rate - Foreign exchange correlation / (A)(D)	3 to 63 %	43% / 48%(4)
			Interest rate volatility skew / (A)(D)	24 to 50 %	33% / 28%(4)
			Interest rate quanto correlation / (A)(D)	-11 to 34 %	8% / 5%(4)
			Interest rate curve correlation / (A)(D)	46 to 92 %	74% / 80%(4)
			Inflation volatility / (A)(D)	77 to 86 %	81% / 80%(4)
Credit contracts	(147)	Comparable pricing	Cash synthetic basis / (C)(D)	2 to 5 points	4 points
			Comparable bond price / (C)(D)	0 to 75 points	27 points
		Correlation model(6)	Credit correlation / (B)	19 to 96 %	56%
Foreign exchange contracts(5)	68	Option model	Comparable bond price / (A)(D)	5 to 100 points	58 points / 65 points(4)
			Interest rate quanto correlation / (A)(D)	-11 to 34 %	8% / 5%(4)
			Interest rate curve correlation / (A)(D)	46 to 92 %	74% / 80%(4)
			Interest rate - Foreign exchange correlation / (A)(D)	3 to 63 %	43% / 48%(4)
			Interest rate volatility skew / (A)(D)	24 to 50 %	33% / 28%(4)
			Interest rate curve / (A)(D)	0 to 1 %	1% / 0%(4)
Equity contracts(5)	(831)	Option model	At the money volatility / (A)(D)	20 to 53 %	31%
			Volatility skew / (A)(D)	-3 to 0 %	-1%
			Equity - Equity correlation / (C)(D)	40 to 99 %	69%
			Equity - Foreign exchange correlation / (C)(D)	-50 to 9 %	-20%
			Equity - Interest rate correlation / (C)(D)	-4 to 70 %	39% / 40%(4)
Commodity contracts	880	Option model	Forward power price / (C)(D)	$14 to $91 per Megawatt hour	$40 per Megawatt hour
			Commodity volatility / (A)(D)	11 to 30 %	14%
			Cross commodity correlation / (C)(D)	34 to 99 %	93%
Investments(3):					
Principal investments	2,160	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	12 %	12%
			Exit multiple / (A)(D)	9 times	9 times
		Discounted cash flow(6)	Capitalization rate / (C)(D)	5 to 13 %	7%
			Equity discount rate / (C)(D)	10 to 30 %	21%
		Market approach	EBITDA multiple / (A)	5 to 6 times	5 times
Other	538	Discounted cash flow	Implied weighted average cost of capital / (C)(D)	7 to 10 %	8%
			Exit multiple / (A)(D)	7 to 9 times	9 times
		Market approach(6)	EBITDA multiple / (A)	8 to 14 times	10 times
Liabilities					

Securities sold under agreements to repurchase	$ 154	Discounted cash flow	Funding spread / (A)	92 to 97 basis points	95 basis points
Other secured financings	278	Comparable pricing(6)	Comparable bond price / (A)	99 to 102 points	101 points
		Discounted cash flow	Funding spread / (A)	97 basis points	97 basis points
Long-term borrowings	1,887	Option model	At the money volatility / (C)(D)	20 to 33 %	26%
			Volatility skew / (A)(D)	-2 to 0 %	0%
			Equity - Equity correlation / (A)(D)	50 to 70 %	69%
			Equity - Foreign exchange correlation / (C)(D)	-60 to 0 %	-23%

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) The ranges of significant unobservable inputs are represented in points, percentages, basis points, times or megawatt hours. Points are a percentage of par; for example, 93 points would be 93% of par. A basis point equals 1/100th of 1%; for example, 487 basis points would equal 4.87%.
(2) Amounts represent weighted averages except where simple averages and the median of the inputs are provided (see footnote 4 below). Weighted averages are calculated by weighting each input by the fair value of the respective financial instruments except for long-term borrowings and derivative instruments where inputs are weighted by risk.
(3) Investments in funds measured using an unadjusted NAV are excluded.
(4) The data structure of the significant unobservable inputs used in valuing Interest rate contracts, Foreign exchange contracts and certain Equity contracts may be in a multi-dimensional form, such as a curve or surface, with risk distributed across the structure. Therefore, a simple average and median, together with the range of data inputs, may be more appropriate measurements than a single point weighted average.
(5) Includes derivative contracts with multiple risks (*i.e.,* hybrid products).
(6) This is the predominant valuation technique for this major asset or liability class.

Sensitivity of the fair value to changes in the unobservable inputs:

(A) Significant increase (decrease) in the unobservable input in isolation would result in a significantly higher (lower) fair value measurement.
(B) Significant changes in credit correlation may result in a significantly higher or lower fair value measurement. Increasing (decreasing) correlation drives a redistribution of risk within the capital structure such that junior tranches become less (more) risky and senior tranches become more (less) risky.
(C) Significant increase (decrease) in the unobservable input in isolation would result in a significantly lower (higher) fair value measurement.
(D) There are no predictable relationships between the significant unobservable inputs.

The following provides a description of significant unobservable inputs included in the September 30, 2014 and December 31, 2013 tables above for all major categories of assets and liabilities:

Comparable bond price a pricing input used when prices for the identical instrument are not available. Significant subjectivity may be involved when fair value is determined using pricing data available for comparable instruments. Valuation using comparable instruments can be done by calculating an implied yield (or spread over a liquid benchmark) from the price of a comparable bond, then adjusting that yield (or spread) to derive a value for the bond. The adjustment to yield (or spread) should account for relevant differences in the bonds such as maturity or credit quality. Alternatively, a price-to-price basis can be assumed between the comparable instrument and bond being valued in order to establish the value of the bond. Additionally, as the probability of default increases for a given bond (*i.e.*, as the bond becomes more distressed), the valuation of that bond will increasingly reflect its expected recovery level assuming default. The decision to use price-to-price or yield/spread comparisons largely reflects trading market convention for the financial instruments in question. Price-to-price comparisons are primarily employed for residential mortgage-backed securities, commercial mortgage-backed securities (CMBS), collateralized debt obligations (CDOs), collateralized loan obligations (CLOs), Other debt, interest rate contracts, foreign exchange contracts, Other secured financings, mortgage loans and distressed corporate bonds. Implied yield (or spread over a liquid benchmark) is utilized predominately for non-distressed corporate bonds, loans and credit contracts.

Correlation a pricing input where the payoff is driven by more than one underlying risk. Correlation is a measure of the relationship between the movements of two variables (*i.e*., how the change in one variable influences a change in the other variable). Credit correlation, for example, is the factor that describes the relationship between the probability of individual entities to default on obligations and the joint probability of multiple entities to default on obligations.

Credit spread the difference in yield between different securities due to differences in credit quality. The credit spread reflects the additional net yield an investor can earn from a security with more credit risk relative to one with less credit risk. The credit spread of a particular security is often quoted in relation to the yield on a credit risk-free benchmark security or reference rate, typically either U.S. Treasury or London Interbank Offered Rate (LIBOR).

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Volatility skew the measure of the difference in implied volatility for options with identical underliers and expiry dates but with different strikes. The implied volatility for an option with a strike price that is above or below the current price of an underlying asset will typically deviate from the implied volatility for an option with a strike price equal to the current price of that same underlying asset.

Volatility the measure of the variability in possible returns for an instrument given how much that instrument changes in value over time. Volatility is a pricing input for options and, generally, the lower the volatility, the less risky the option. The level of volatility used in the valuation of a particular option depends on a number of factors, including the nature of the risk underlying that option (*e.g.*, the volatility of a particular underlying equity security may be significantly different from that of a particular underlying commodity index), the tenor and the strike price of the option.

Comparable equity price a price derived from equity raises, share buybacks and external bid levels, etc. A discount or premium may be included in the fair value estimate.

EBITDA multiple / Exit multiple is the Enterprise Value to EBITDA ratio, where the Enterprise Value is the aggregate value of equity and debt minus cash and cash equivalents. The EBITDA multiple reflects the value of the company in terms of its full-year EBITDA, whereas the exit multiple reflects the value of the company in terms of its full-year expected EBITDA at exit. Either multiple allows comparison between companies from an operational perspective as the effect of capital structure, taxation and depreciation/amortization is excluded.

Price / Book ratio the ratio used to compare a stock s market value to its book value. It is calculated by dividing the current closing price of the stock by the latest book value per share. This multiple allows comparison between companies from an operational perspective.

Cash synthetic basis the measure of the price differential between cash financial instruments (cash instruments) and their synthetic derivative-based equivalents (synthetic instruments). The range disclosed in the table above signifies the number of points by which the synthetic bond equivalent price is higher than the quoted price of the underlying cash bonds.

Interest rate curve the term structure of interest rates (relationship between interest rates and the time to maturity) and a market s measure of future interest rates at the time of observation. An interest rate curve is used to set interest rate and foreign exchange derivative cash flows and is a pricing input used in the discounting of any over-the-counter (OTC) derivative cash flow.

Implied weighted average cost of capital (WACC) the WACC implied by the current value of equity in a discounted cash flow model. The model assumes that the cash flow assumptions, including projections, are fully reflected in the current equity value while the debt to equity ratio is held constant. The WACC theoretically represents the required rate of return to debt and equity investors, respectively.

Capitalization rate the ratio between net operating income produced by an asset and its market value at the projected disposition date.

Price / Earnings ratio the ratio used to measure a company s equity value in relation to its earnings. It is calculated by dividing the equity value per share by the latest historical or forward-looking earnings per share. The ratio results in a standardized metric that allows comparison between companies, after also considering the effects of different leverage ratios and taxations.

Funding spread the difference between the general collateral rate (which refers to the rate applicable to a broad class of U.S. Treasury issuances) and the specific collateral rate (which refers to the rate applicable to a specific type of security pledged as collateral, such as a municipal bond). Repurchase agreements and certain other secured financings are discounted based on collateral curves. The curves are

29

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

constructed as spreads over the corresponding overnight indexed swap (OIS) or LIBOR curves, with the short end of the curve representing spreads over the corresponding OIS curves and the long end of the curve representing spreads over LIBOR.

Equity alpha a parameter used in modeling of equity hybrid prices.

Fair Value of Investments That Calculate Net Asset Value.

The Company s Investments measured at fair value were $6,674 million and $8,013 million at September 30, 2014 and December 31, 2013, respectively. The following table presents information solely about the Company s investments in private equity funds, real estate funds and hedge funds measured at fair value based on NAV at September 30, 2014 and December 31, 2013, respectively:

	At September 30, 2014		At December 31, 2013	
	Fair Value	Unfunded Commitment	Fair Value	Unfunded Commitment
	(dollars in millions)			
Private equity funds	$ 2,493	$ 614	$ 2,531	$ 559
Real estate funds	1,817	111	1,643	124
Hedge funds(1):				
Long-short equity hedge funds	444		469	
Fixed income/credit-related hedge funds	74		82	
Event-driven hedge funds	40		38	
Multi-strategy hedge funds	157	3	220	3
Total	$ 5,025	$ 728	$ 4,983	$ 686

(1) Fixed income/credit-related hedge funds, event-driven hedge funds, and multi-strategy hedge funds are redeemable at least on a three-month period basis primarily with a notice period of 90 days or less. At September 30, 2014, approximately 38% of the fair value amount of long-short equity hedge funds is redeemable at least quarterly, 46% is redeemable every six months and 16% of these funds have a redemption frequency of greater than six months. The notice period for long-short equity hedge funds at September 30, 2014 is primarily greater than six months. At December 31, 2013, approximately 42% of the fair value amount of long-short equity hedge funds is redeemable at least quarterly, 42% is redeemable every six months and 16% of these funds have a redemption frequency of greater than six months. The notice period for long-short equity hedge funds at December 31, 2013 is primarily greater than six months.

Private Equity Funds. Amount includes several private equity funds that pursue multiple strategies including leveraged buyouts, venture capital, infrastructure growth capital, distressed investments, and mezzanine capital. In addition, the funds may be structured with a focus on specific domestic or foreign geographic regions. These investments are generally not redeemable with the funds. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the fund. At September 30, 2014, it was estimated that 6% of the fair value of the funds will be liquidated in the next five years, another 59% of the fair value of the funds will be liquidated between five to 10 years and the remaining 35% of the fair value of the funds have a remaining life of greater than 10 years.

Real Estate Funds. Amount includes several real estate funds that invest in real estate assets such as commercial office buildings, retail properties, multi-family residential properties, developments or hotels. In addition, the funds may be structured with a focus on specific geographic domestic or foreign regions. These investments are generally not redeemable with the funds. Distributions from each fund will be received as the underlying investments of the funds are liquidated. At September 30, 2014, it was estimated that 4% of the fair value of the funds will be liquidated within the next five years, another 59% of the fair value of the funds will be liquidated between five to 10 years and the remaining 37% of the fair value of the funds have a remaining life of greater than 10 years.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Hedge Funds. Investments in hedge funds may be subject to initial period lock-up restrictions or gates. A hedge fund lock-up provision is a provision that provides that, during a certain initial period, an investor may not make a withdrawal from the fund. The purpose of a gate is to restrict the level of redemptions that an investor in a particular hedge fund can demand on any redemption date.

Long-Short Equity Hedge Funds. Amount includes investments in hedge funds that invest, long or short, in equities. Equity value and growth hedge funds purchase stocks perceived to be undervalued and sell stocks perceived to be overvalued. Investments representing approximately 11% of the fair value of the investments in this category cannot be redeemed currently because the investments include certain initial period lock-up restrictions. The remaining restriction period for these investments subject to lock-up restrictions was primarily less than one year at September 30, 2014. Investments representing approximately 21% of the fair value of the investments in long-short equity hedge funds cannot be redeemed currently because an exit restriction has been imposed by the hedge fund manager. The restriction period for these investments subject to an exit restriction was primarily indefinite at September 30, 2014.

Fixed Income/Credit-Related Hedge Funds. Amount includes investments in hedge funds that employ long-short, distressed or relative value strategies in order to benefit from investments in undervalued or overvalued securities that are primarily debt or credit related. Investments representing approximately 10% of the fair value of the investments in this category cannot be redeemed currently because the investments include certain initial period lock-up restrictions. The remaining restriction period for these investments subject to lock-up restrictions was primarily over three years at September 30, 2014.

Event-Driven Hedge Funds. Amount includes investments in hedge funds that invest in event-driven situations such as mergers, hostile takeovers, reorganizations, or leveraged buyouts. This may involve the simultaneous purchase of stock in companies being acquired and the sale of stock in its acquirer, with the expectation to profit from the spread between the current market price and the ultimate purchase price of the target company. At September 30, 2014, there were no restrictions on redemptions.

Multi-strategy Hedge Funds. Amount includes investments in hedge funds that pursue multiple strategies to realize short- and long-term gains. Management of the hedge funds has the ability to overweight or underweight different strategies to best capitalize on current investment opportunities. At September 30, 2014, investments representing approximately 27% of the fair value of the investments in this category cannot be redeemed currently because the investments include certain initial period lock-up restrictions. The remaining restriction period for these investments subject to lock-up restrictions was primarily over three years at September 30, 2014. Investments representing approximately 25% of the fair value of the investments in multi-strategy hedge funds cannot be redeemed currently because an exit restriction has been imposed by the hedge fund manager. The restriction period for these investments subject to an exit restriction was indefinite at September 30, 2014.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fair Value Option.

The Company elected the fair value option for certain eligible instruments that are risk managed on a fair value basis to mitigate income statement volatility caused by measurement basis differences between the elected instruments and their associated risk management transactions or to eliminate complexities of applying certain accounting models. The following table presents net gains (losses) due to changes in fair value for items measured at fair value pursuant to the fair value option election for the quarters and nine months ended September 30, 2014 and 2013, respectively:

	Trading Revenues	Interest Income (Expense)	Gains (Losses) Included in Net Revenues
		(dollars in millions)	
Three Months Ended September 30, 2014			
Federal funds sold and securities purchased under agreements to resell	$ (2)	$ 2	$
Commercial paper and other short-term borrowings(1)	5	2	7
Securities sold under agreements to repurchase	3	(2)	1
Long-term borrowings(1)	1,579	(174)	1,405
Nine Months Ended September 30, 2014			
Federal funds sold and securities purchased under agreements to resell	$ (4)	$ 6	$ 2
Commercial paper and other short-term borrowings(1)	(32)	2	(30)
Securities sold under agreements to repurchase	(2)	(4)	(6)
Long-term borrowings(1)	631	(520)	111
Three Months Ended September 30, 2013			
Federal funds sold and securities purchased under agreements to resell	$ 1	$ 3	$ 4
Deposits	14	(17)	(3)
Commercial paper and other short-term borrowings(2)	(62)	(3)	(65)
Securities sold under agreements to repurchase	(3)	(2)	(5)
Long-term borrowings(2)	(154)	(224)	(378)
Nine Months Ended September 30, 2013			
Federal funds sold and securities purchased under agreements to resell	$	$ 6	$ 6
Deposits	44	(50)	(6)
Commercial paper and other short-term borrowings(2)	118	(5)	113
Securities sold under agreements to repurchase	2	(5)	(3)
Long-term borrowings(2)	1,053	(752)	301

(1) Of the total gains (losses) recorded in Trading revenues for short-term and long-term borrowings for the quarter and nine months ended September 30, 2014, $215 million and $428 million, respectively, are attributable to changes in the credit quality of the Company and other credit factors, and the respective remainder is attributable to changes in foreign currency rates or interest rates or movements in the reference price or index for structured notes before the impact of related hedges.

(2) Of the total gains (losses) recorded in Trading for short-term and long-term borrowings for the quarter and nine months ended September 30, 2013, $(171) million and $(313) million, respectively, are attributable to changes in the credit quality of the Company and other credit factors, and the respective remainder is attributable to changes in foreign currency rates or interest rates or movements in the reference price or index for structured notes before the impact of related hedges.

In addition to the amounts in the above table, as discussed in Note 2 to the consolidated financial statements in the 2013 Form 10-K, all of the instruments within Trading assets or Trading liabilities are measured at fair value, either through the election of the fair value option or as required by other accounting guidance. The amounts in the above table are included within Net revenues and do not reflect gains or losses on related hedging instruments, if any.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company hedges the economics of market risk for short-term and long-term borrowings (*i.e*., risks other than that related to the credit quality of the Company) as part of its overall trading strategy and manages the market risks embedded within the issuance by the related business unit as part of the business unit s portfolio. The gains and losses on related economic hedges are recorded in Trading revenues and largely offset the gains and losses on short-term and long-term borrowings attributable to market risk.

At September 30, 2014 and December 31, 2013, a breakdown of the short-term and long-term borrowings measured at fair value on a recurring basis by business unit responsible for risk-managing each borrowing is shown in the table below:

Business Unit	Short-Term and Long-Term Borrowings At September 30, 2014	Short-Term and Long-Term Borrowings At December 31, 2013
	(dollars in millions)	
Interest rates	$ 14,457	$ 15,933
Equity	17,292	17,945
Credit and foreign exchange	2,181	2,561
Commodities	702	545
Total	$ 34,632	$ 36,984

The following tables present information on the Company s short-term and long-term borrowings (primarily structured notes), loans and unfunded lending commitments for which the fair value option was elected:

Gains (Losses) due to Changes in Instrument-Specific Credit Risk.

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(dollars in millions)			
Short-term and long-term borrowings(1)	$ 215	$ (171)	$ 428	$ (313)
Loans(2)	25	35	153	150
Unfunded lending commitments(3)	2	6	29	221

(1) The change in the fair value of short-term and long-term borrowings (primarily structured notes) includes an adjustment to reflect the change in credit quality of the Company based upon observations of the Company s secondary bond market spreads and changes in other credit factors.
(2) Instrument-specific credit gains (losses) were determined by excluding the non-credit components of gains and losses, such as those due to changes in interest rates.
(3) Gains (losses) were generally determined based on the differential between estimated expected client yields and contractual yields at each respective period-end.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net Difference between Contractual Principal Amount and Fair Value.

	Contractual Principal Amount Exceeds Fair Value	
	At September 30, 2014	At December 31, 2013
	(dollars in millions)	
Short-term and long-term borrowings(1)	$ (680)	$ (2,409)
Loans(2)	16,372	17,248
Loans 90 or more days past due and/or on nonaccrual status(2)(3)	14,419	15,113

(1) These amounts do not include structured notes where the repayment of the initial principal amount fluctuates based on changes in the reference price or index.
(2) The majority of this difference between principal and fair value amounts emanates from the Company s distressed debt trading business, which purchases distressed debt at amounts well below par.
(3) The aggregate fair value of loans that were in nonaccrual status, which includes all loans 90 or more days past due, was $1,343 million and $1,205 million at September 30, 2014 and December 31, 2013, respectively. The aggregate fair value of loans that were 90 or more days past due was $524 million and $655 million at September 30, 2014 and December 31, 2013, respectively.

The tables above exclude non-recourse debt from consolidated VIEs, liabilities related to failed sales of financial assets, pledged commodities and other liabilities that have specified assets attributable to them.

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

Certain assets were measured at fair value on a non-recurring basis and are not included in the tables above. These assets may include loans, other investments, premises, equipment and software costs, and intangible assets.

The following tables present, by caption on the condensed consolidated statements of financial condition, the fair value hierarchy for those assets measured at fair value on a non-recurring basis for which the Company recognized a non-recurring fair value adjustment for the quarters and nine months ended September 30, 2014 and 2013, respectively.

Three and Nine Months Ended September 30, 2014.

		Fair Value Measurements Using:			Total Gains (Losses) for the:	
	Carrying Value at September 30, 2014(1)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Three Months Ended September 30, 2014(2)	Nine Months Ended September 30, 2014(2)
			(dollars in millions)			
Loans(3)	$ 2,672	$	$ 1,996	$ 676	$ (45)	$ (55)
Other investments(4)	38			38	(2)	(27)
Premises, equipment and software costs(5)					(27)	(43)

Intangible assets(4)	20			20	(4)	(6)
Other assets(5)						(9)
Total	$ 2,730	$	$ 1,996	$ 734	$ (78)	$ (140)

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) Carrying values relate only to those assets that had fair value adjustments during the quarter ended September 30, 2014. These amounts do not include assets that had fair value adjustments during the nine months ended September 30, 2014, unless the assets also had a fair value adjustment during the quarter ended September 30, 2014.
(2) Fair value adjustments related to Loans and losses related to Other investments are recorded within Other revenues whereas losses related to Premises, equipment and software costs, Intangible assets and Other assets are recorded within Other expenses in the condensed consolidated statements of income.
(3) Non-recurring changes in the fair value of loans held for investment or held for sale were calculated using recently executed transactions; market price quotations; valuation models that incorporate market observable inputs where possible, such as comparable loan or debt prices and credit default swap spread levels adjusted for any basis difference between cash and derivative instruments; or default recovery analysis where such transactions and quotations are unobservable.
(4) Losses were determined primarily using discounted cash flow models and methodologies that incorporate multiples of certain comparable companies.
(5) Losses were determined primarily using a default recovery analysis.

There were no significant liabilities measured at fair value on a non-recurring basis during the quarter and nine months ended September 30, 2014.

Three and Nine Months Ended September 30, 2013.

		Fair Value Measurements Using:			Total Gains (Losses) for the:	
	Carrying Value at September 30, 2013(1)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Three Months Ended September 30, 2013(2)	Nine Months Ended September 30, 2013(2)
	(dollars in millions)					
Loans(3)	$ 1,507	$	$ 1,160	$ 347	$ (35)	$ (106)
Other investments(4)	55			55	(5)	(28)
Premises, equipment and software costs(4)					(17)	(23)
Intangible assets(4)						(9)
Total	$ 1,562	$	$ 1,160	$ 402	$ (57)	$ (166)

(1) Carrying values relate only to those assets that had fair value adjustments during the quarter ended September 30, 2013. These amounts do not include assets that had fair value adjustments during the nine months ended September 30, 2013, unless the assets also had a fair value adjustment during the quarter ended September 30, 2013.
(2) Fair value adjustments related to Loans and losses related to Other investments are recorded within Other revenues whereas losses related to Premises, equipment and software costs and Intangible assets are recorded within Other expenses in the condensed consolidated statements of income.
(3) Non-recurring changes in the fair value of loans held for investment or held for sale were calculated using recently executed transactions; market price quotations; valuation models that incorporate market observable inputs where possible, such as comparable loan or debt prices and credit default swap spread levels adjusted for any basis difference between cash and derivative instruments; or default recovery analysis where such transactions and quotations are unobservable.
(4) Losses recorded were determined primarily using discounted cash flow models.

There were no significant liabilities measured at fair value on a non-recurring basis during the quarter and nine months ended September 30, 2013.

Financial Instruments Not Measured at Fair Value.

The tables below present the carrying value, fair value and fair value hierarchy category of certain financial instruments that are not measured at fair value in the condensed consolidated statements of financial condition.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below exclude certain financial instruments such as equity method investments and all non-financial assets and liabilities such as the value of the long-term relationships with our deposit customers.

The carrying value of cash and cash equivalents, including Interest bearing deposits with banks, and other short-term financial instruments such as Federal funds sold and securities purchased under agreements to resell; Securities borrowed; Securities sold under agreements to repurchase; Securities loaned; certain Customer and other receivables and Customer and other payables arising in the ordinary course of business; certain Deposits; Commercial paper and other short-term borrowings; and Other secured financings approximate fair value because of the relatively short period of time between their origination and expected maturity.

For longer-dated Federal funds sold and securities purchased under agreements to resell, Securities borrowed, Securities sold under agreements to repurchase, Securities loaned and Other secured financings, fair value is determined using a standard cash flow discounting methodology. The inputs to the valuation include contractual cash flows and collateral funding spreads, which are estimated using various benchmarks and interest rate yield curves.

For consumer and residential real estate loans and lending commitments where position-specific external price data are not observable, the fair value is based on the credit risks of the borrower using a probability of default and loss given default method, discounted at the estimated external cost of funding level. The fair value of corporate loans and lending commitments is determined using recently executed transactions, market price quotations (where observable), implied yields from comparable debt, and market observable credit default swap spread levels along with proprietary valuation models and default recovery analysis where such transactions and quotations are unobservable.

The fair value of long-term borrowings is generally determined based on transactional data or third-party pricing for identical or comparable instruments, when available. Where position-specific external prices are not observable, fair value is determined based on current interest rates and credit spreads for debt instruments with similar terms and maturity.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Financial Instruments Not Measured at Fair Value at September 30, 2014 and December 31, 2013.

At September 30, 2014.

	At September 30, 2014		Fair Value Measurements Using:		
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
			(dollars in millions)		
Financial Assets:					
Cash and due from banks	$ 20,242	$ 20,242	$ 20,242	$	$
Interest bearing deposits with banks	35,584	35,584	35,584		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	45,106	45,106	45,106		
Federal funds sold and securities purchased under agreements to resell	98,131	98,679		98,323	356
Securities borrowed	140,303	140,302		140,152	150
Customer and other receivables(1)	50,556	50,425		45,374	5,051
Loans(2)	58,209	58,853		14,456	44,397
Financial Liabilities:					
Deposits	$ 124,382	$ 124,421	$	$ 124,421	$
Commercial paper and other short-term borrowings	287	287		287	
Securities sold under agreements to repurchase	83,097	83,025		79,403	3,622
Securities loaned	27,657	27,676		27,004	672
Other secured financings	7,652	7,693		5,576	2,117
Customer and other payables(1)	178,471	178,471		178,471	
Long-term borrowings	119,198	123,885		123,277	608

(1) Accrued interest, fees and dividend receivables and payables where carrying value approximates fair value have been excluded.
(2) Includes all loans measured at fair value on a non-recurring basis.

The fair value of the Company s unfunded lending commitments, primarily related to corporate lending in the Institutional Securities business segment, that are not carried at fair value at September 30, 2014 was $1,009 million, of which $823 million and $186 million would be categorized in Level 2 and Level 3 of the fair value hierarchy, respectively. The carrying value of these commitments, if fully funded, would be $85.0 billion.

37

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At December 31, 2013.

	At December 31, 2013		Fair Value Measurements Using:		
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
			(dollars in millions)		
Financial Assets:					
Cash and due from banks	$ 16,602	$ 16,602	$ 16,602	$	$
Interest bearing deposits with banks	43,281	43,281	43,281		
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	39,203	39,203	39,203		
Federal funds sold and securities purchased under agreements to resell	117,264	117,263		116,584	679
Securities borrowed	129,707	129,705		129,374	331
Customer and other receivables(1)	53,112	53,031		47,525	5,506
Loans(2)	42,874	42,765		11,288	31,477
Financial Liabilities:					
Deposits	$ 112,194	$ 112,273	$	$ 112,273	$
Commercial paper and other short-term borrowings	795	795		787	8
Securities sold under agreements to repurchase	145,115	145,157		138,161	6,996
Securities loaned	32,799	32,826		31,731	1,095
Other secured financings	9,009	9,034		5,845	3,189
Customer and other payables(1)	154,654	154,654		154,654	
Long-term borrowings	117,938	123,133		122,099	1,034

(1) Accrued interest, fees and dividend receivables and payables where carrying value approximates fair value have been excluded.
(2) Includes all loans measured at fair value on a non-recurring basis.

The fair value of the Company s unfunded lending commitments, primarily related to corporate lending in the Institutional Securities business segment, that are not carried at fair value at December 31, 2013 was $853 million, of which $669 million and $184 million would be categorized in Level 2 and Level 3 of the fair value hierarchy, respectively. The carrying value of these commitments, if fully funded, would be $75.4 billion.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Available for Sale Securities.

The following tables present information about the Company s available for sale securities (AFS Securities):

	At September 30, 2014				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Other-than-Temporary Impairment	Fair Value
	(dollars in millions)				
Available for sale debt securities:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 32,297	$ 36	$ 95	$	$ 32,238
U.S. agency securities(1)	16,243	47	129		16,161
Total U.S. government and agency securities	48,540	83	224		48,399
Corporate and other debt:					
Commercial mortgage-backed securities:					
Agency	2,320		87		2,233
Non-Agency	1,789	5	10		1,784
Auto loan asset-backed securities	2,101	1	3		2,099
Corporate bonds	3,639	8	25		3,622
Collateralized loan obligations	1,087		16		1,071
FFELP student loan asset-backed securities(2)	4,302	23	3		4,322
Total corporate and other debt	15,238	37	144		15,131
Total available for sale debt securities	63,778	120	368		63,530
Available for sale equity securities	15	2			17
Total	$ 63,793	$ 122	$ 368	$	$ 63,547

	At December 31, 2013				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Other-than-Temporary Impairment	Fair Value
	(dollars in millions)				
Available for sale debt securities:					
U.S. government and agency securities:					
U.S. Treasury securities	$ 24,486	$ 51	$ 139	$	$ 24,398
U.S. agency securities(1)	15,813	26	234		15,605
Total U.S. government and agency securities	40,299	77	373		40,003
Corporate and other debt:					
Commercial mortgage-backed securities:					
Agency	2,482		84		2,398
Non-Agency	1,333	1	18		1,316
Auto loan asset-backed securities	2,041	2	1		2,042

Corporate bonds	3,415	3	61		3,357
Collateralized loan obligations	1,087		20		1,067
FFELP student loan asset-backed securities(2)	3,230	12	8		3,234
Total corporate and other debt	13,588	18	192		13,414
Total available for sale debt securities	53,887	95	565		53,417
Available for sale equity securities	15		2		13
Total	$ 53,902	$ 95	$ 567	$	$ 53,430

(1) U.S. agency securities are composed of three main categories consisting of agency-issued debt, agency mortgage pass-through pool securities and collateralized mortgage obligations.

(2) FFELP Federal Family Education Loan Program. Amounts are backed by a guarantee from the U.S. Department of Education of at least 95% of the principal balance and interest on such loans.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present the fair value of investments in AFS Securities that are in an unrealized loss position:

At September 30, 2014	Less than 12 Months Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(dollars in millions)					
Available for sale debt securities:						
U.S. government and agency securities:						
U.S. Treasury securities	$ 12,448	$ 16	$ 5,897	$ 79	$ 18,345	$ 95
U.S. agency securities	2,278	9	4,828	120	7,106	129
Total U.S. government and agency securities	14,726	25	10,725	199	25,451	224
Corporate and other debt:						
Commercial mortgage-backed securities:						
Agency			1,933	87	1,933	87
Non-Agency	485	3	566	7	1,051	10
Auto loan asset-backed securities	1,267	3			1,267	3
Corporate bonds	956	5	1,276	20	2,232	25
Collateralized loan obligations			1,071	16	1,071	16
FFELP student loan asset-backed securities	747	1	440	2	1,187	3
Total corporate and other debt	3,455	12	5,286	132	8,741	144
Total available for sale debt securities	18,181	37	16,011	331	34,192	368
Total	$ 18,181	$ 37	$ 16,011	$ 331	$ 34,192	$ 368

At December 31, 2013	Less than 12 Months Fair Value	Less than 12 Months Gross Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
	(dollars in millions)					
Available for sale debt securities:						
U.S. government and agency securities:						
U.S. Treasury securities	$ 13,266	$ 139	$	$	$ 13,266	$ 139
U.S. agency securities	8,438	211	651	23	9,089	234
Total U.S. government and agency securities	21,704	350	651	23	22,355	373
Corporate and other debt:						
Commercial mortgage-backed securities:						
Agency	958	15	1,270	69	2,228	84
Non-Agency	841	16	86	2	927	18
Auto loan asset-backed securities	557	1	85		642	1
Corporate bonds	2,350	52	383	9	2,733	61
Collateralized loan obligations	1,067	20			1,067	20
FFELP student loan asset-backed securities	1,388	7	76	1	1,464	8

Total corporate and other debt	7,161	111	1,900	81	9,061	192
Total available for sale debt securities	28,865	461	2,551	104	31,416	565
Available for sale equity securities	13	2			13	2
Total	$ 28,878	$ 463	$ 2,551	$ 104	$ 31,429	$ 567

Gross unrealized gains and losses are recorded in Accumulated other comprehensive income (loss), net of tax (AOCI).

As discussed in Note 2 to the consolidated financial statements in the 2013 Form 10-K, AFS Securities with a current fair value less than their amortized cost are analyzed as part of the Company s ongoing assessment of

40

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

temporary versus other-than-temporarily impaired at the individual security level. The unrealized losses reported above on available for sale debt securities are primarily due to rising long-term interest rates since those securities were purchased. While the securities in an unrealized loss position greater than twelve months have increased in 2014, the risk of credit loss is considered minimal because all of the Company s agency securities as well as the Company s asset-backed securities, CMBS and CLOs are highly rated and the Company s corporate bonds are all investment grade. The Company does not intend to sell these securities and is not likely to be required to sell these securities prior to recovery of the amortized cost basis. The Company does not expect to experience a credit loss on these securities based on consideration of the relevant information (as discussed in Note 2 to the consolidated financial statements in the 2013 Form 10-K), including for U.S. government and agency securities, the existence of the explicit and implicit guarantee provided by the U.S. government. The Company believes that the debt securities with an unrealized loss position were not other-than-temporarily impaired at September 30, 2014 and December 31, 2013. For more information, see the Other-than-temporary impairment discussion in Note 2 to the consolidated financial statements in the 2013 Form 10-K.

The following table presents the amortized cost and fair value of available for sale debt securities by contractual maturity dates at September 30, 2014:

At September 30, 2014	Amortized Cost	Fair Value	Annualized Average Yield
		(dollars in millions)	
U.S. government and agency securities:			
U.S. Treasury securities:			
After 1 year through 5 years	$ 32,297	$ 32,238	0.7%
Total	32,297	32,238	
U.S. agency securities:			
After 1 year through 5 years	1,193	1,191	0.9%
After 5 years through 10 years	1,892	1,893	1.2%
After 10 years	13,158	13,077	1.4%
Total	16,243	16,161	
Total U.S. government and agency securities	48,540	48,399	0.9%
Corporate and other debt:			
Commercial mortgage-backed securities:			
Agency:			
After 1 year through 5 years	713	708	0.9%
After 5 years through 10 years	358	353	0.9%
After 10 years	1,249	1,172	1.5%
Total	2,320	2,233	
Non-Agency:			
After 10 years	1,789	1,784	1.7%
Total	1,789	1,784	

Auto loan asset-backed securities:			
Due within 1 year	38	38	0.7%
After 1 year through 5 years	1,994	1,992	0.8%
After 5 years through 10 years	69	69	1.2%
Total	2,101	2,099	
Corporate bonds:			
Due within 1 year	190	190	0.9%
After 1 year through 5 years	2,939	2,926	1.4%
After 5 years through 10 years	510	506	2.7%
Total	3,639	3,622	

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At September 30, 2014	Amortized Cost	Fair Value	Annualized Average Yield
		(dollars in millions)	
Collateralized loan obligations:			
After 10 years	1,087	1,071	1.4%
Total	1,087	1,071	
FFELP student loan asset-backed securities:			
After 1 year through 5 years	135	136	0.7%
After 5 years through 10 years	629	630	0.8%
After 10 years	3,538	3,556	0.9%
Total	4,302	4,322	
Total corporate and other debt	15,238	15,131	1.2%
Total available for sale debt securities	$ 63,778	$ 63,530	1.0%

See Note 7 for additional information on securities issued by VIEs, including U.S. agency mortgage-backed securities, non-agency CMBS, auto loan asset-backed securities, CLO and FFELP student loan asset-backed securities.

The following table presents information pertaining to sales of AFS Securities during the quarters and nine months ended September 30, 2014 and 2013:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(dollars in millions)			
Gross realized gains	$ 20	$ 6	$ 37	$ 47
Gross realized losses	$	$ 1	$ 1	$ 4

Gross realized gains and losses are recognized in Other revenues in the condensed consolidated statements of income.

6. Collateralized Transactions.

The Company enters into reverse repurchase agreements, repurchase agreements, securities borrowed and securities loaned transactions to, among other things, acquire securities to cover short positions and settle other securities obligations, to accommodate customers needs and to finance the Company s inventory positions. The Company manages credit exposure arising from such transactions by, in appropriate circumstances, entering into master netting agreements and collateral agreements with counterparties that provide the Company, in the event of a counterparty default (such as bankruptcy or a counterparty s failure to pay or perform), with the right to net a counterparty s rights and obligations under such agreement and liquidate and set off collateral held by the Company against the net amount owed by the counterparty. The Company s policy is generally to take possession of securities purchased under agreements to resell and securities borrowed, and to receive securities and cash posted as collateral (with rights of rehypothecation), although in certain cases, the Company may agree for such collateral to be posted to a third-party custodian under a tri-party arrangement that enables the Company to take control of such collateral in the event of a counterparty default. The Company also monitors the fair value of the underlying securities as compared with the related receivable or payable, including accrued interest, and, as necessary, requests additional collateral as provided under the applicable agreement to ensure such transactions are adequately collateralized.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present information about the offsetting of these instruments and related collateral amounts. For information related to offsetting of derivatives, see Note 10.

	At September 30, 2014				
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of Financial Condition	Financial Instruments Not Offset in the Condensed Consolidated Statements of Financial Condition(3)	Net Exposure
	(dollars in millions)				
Assets					
Federal funds sold and securities purchased under agreements to resell	$ 157,991	$ (58,997)	$ 98,994	$ (93,819)	$ 5,175
Securities borrowed	147,347	(7,044)	140,303	(129,103)	11,200
Liabilities					
Securities sold under agreements to repurchase	$ 142,703	$ (58,997)	$ 83,706	$ (64,858)	$ 18,848
Securities loaned	34,701	(7,044)	27,657	(27,148)	509

(1) Amounts include $4.9 billion of Federal funds sold and securities purchased under agreements to resell, $6.2 billion of Securities borrowed, $18.7 billion of Securities sold under agreements to repurchase and $0.1 billion of Securities loaned, which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable.

(2) Amounts relate to master netting agreements and collateral agreements, which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.

(3) Amounts relate to master netting agreements and collateral agreements, which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.

	At December 31, 2013				
	Gross Amounts(1)	Amounts Offset in the Condensed Consolidated Statements of Financial Condition(2)	Net Amounts Presented in the Condensed Consolidated Statements of Financial Condition	Financial Instruments Not Offset in the Condensed Consolidated Statements of Financial Condition(3)	Net Exposure
	(dollars in millions)				
Assets					
Federal funds sold and securities purchased under agreements to resell	$ 183,015	$ (64,885)	$ 118,130	$ (106,828)	$ 11,302
Securities borrowed	137,082	(7,375)	129,707	(113,339)	16,368
Liabilities					
Securities sold under agreements to repurchase	$ 210,561	$ (64,885)	$ 145,676	$ (111,599)	$ 34,077
Securities loaned	40,174	(7,375)	32,799	(32,543)	256

(1) Amounts include $11.1 billion of Federal funds sold and securities purchased under agreements to resell, $13.2 billion of Securities borrowed and $33.3 billion of Securities sold under agreements to repurchase, which are either not subject to master netting agreements or collateral agreements or are subject to such agreements but the Company has not determined the agreements to be legally enforceable.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) Amounts relate to master netting agreements and collateral agreements, which have been determined by the Company to be legally enforceable in the event of default and where certain other criteria are met in accordance with applicable offsetting accounting guidance.
(3) Amounts relate to master netting agreements and collateral agreements, which have been determined by the Company to be legally enforceable in the event of default but where certain other criteria are not met in accordance with applicable offsetting accounting guidance.

The Company also engages in margin lending to clients that allows the client to borrow against the value of qualifying securities and is included within Customer and other receivables in the condensed consolidated statement of financial condition. Under these agreements and transactions, the Company either receives or provides collateral, including U.S. government and agency securities, other sovereign government obligations, corporate and other debt, and corporate equities. Customer receivables generated from margin lending activities are collateralized by customer-owned securities held by the Company. The Company monitors required margin levels and established credit limits daily and, pursuant to such guidelines, requires customers to deposit additional collateral, or reduce positions, when necessary. Margin loans are extended on a demand basis and are not committed facilities. Factors considered in the review of margin loans are the amount of the loan, the intended purpose, the degree of leverage being employed in the account, and overall evaluation of the portfolio to ensure proper diversification or, in the case of concentrated positions, appropriate liquidity of the underlying collateral or potential hedging strategies to reduce risk. Additionally, transactions relating to concentrated or restricted positions require a review of any legal impediments to liquidation of the underlying collateral. Underlying collateral for margin loans is reviewed with respect to the liquidity of the proposed collateral positions, valuation of securities, historic trading range, volatility analysis and an evaluation of industry concentrations. For these transactions, adherence to the Company s collateral policies significantly limits the Company s credit exposure in the event of a customer default. The Company may request additional margin collateral from customers, if appropriate, and, if necessary, may sell securities that have not been paid for or purchase securities sold but not delivered from customers. At September 30, 2014 and December 31, 2013, there were approximately $28.9 billion and $29.2 billion, respectively, of customer margin loans outstanding.

Other secured financings include the liabilities related to transfers of financial assets that are accounted for as financings rather than sales, consolidated VIEs where the Company is deemed to be the primary beneficiary, and certain equity-linked notes and other secured borrowings. These liabilities are generally payable from the cash flows of the related assets accounted for as Trading assets (see Notes 7 and 9).

The Company pledges its trading assets to collateralize repurchase agreements and other secured financings. Pledged financial instruments that can be sold or repledged by the secured party are identified as Trading assets (pledged to various parties) in the condensed consolidated statements of financial condition. The carrying value and classification of Trading assets by the Company that have been loaned or pledged to counterparties where those counterparties do not have the right to sell or repledge the collateral were as follows:

	At September 30, 2014	At December 31, 2013
	(dollars in millions)	
Trading assets:		
U.S. government and agency securities	$ 15,008	$ 21,589
Other sovereign government obligations	5,344	5,748
Corporate and other debt	6,124	7,388
Corporate equities	7,785	8,713
Total	$ 34,261	$ 43,438

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company receives collateral in the form of securities in connection with reverse repurchase agreements, securities borrowed and derivative transactions, customer margin loans and securities-based lending. In many cases, the Company is permitted to sell or repledge these securities held as collateral and use the securities to secure repurchase agreements, to enter into securities lending and derivative transactions or for delivery to counterparties to cover short positions. The Company additionally receives securities as collateral in connection with certain securities-for-securities transactions in which the Company is the lender. In instances where the Company is permitted to sell or repledge these securities, the Company reports the fair value of the collateral received and the related obligation to return the collateral in the condensed consolidated statements of financial condition. At September 30, 2014 and December 31, 2013, the total fair value of financial instruments received as collateral where the Company is permitted to sell or repledge the securities was $537 billion and $533 billion, respectively, and the fair value of the portion that had been sold or repledged was $437 billion and $381 billion, respectively.

At September 30, 2014 and December 31, 2013, cash and securities deposited with clearing organizations or segregated under federal and other regulations or requirements were as follows:

	At September 30, 2014	At December 31, 2013
	(dollars in millions)	
Cash deposited with clearing organizations or segregated under federal and other regulations or requirements	$ 45,106	$ 39,203
Securities(1)	12,502	15,586
Total	$ 57,608	$ 54,789

(1) Securities deposited with clearing organizations or segregated under federal and other regulations or requirements are sourced from Federal funds sold and securities purchased under agreements to resell and Trading assets in the condensed consolidated statements of financial condition.

7. Variable Interest Entities and Securitization Activities.

The Company is involved with various special purpose entities (SPE) in the normal course of business. In most cases, these entities are deemed to be VIEs.

The Company applies accounting guidance for consolidation of VIEs to certain entities in which equity investors do not have the characteristics of a controlling financial interest. Except for certain asset management entities, the primary beneficiary of a VIE is the party that both (1) has the power to direct the activities of a VIE that most significantly affect the VIE s economic performance and (2) has an obligation to absorb losses or the right to receive benefits that in either case could potentially be significant to the VIE. The Company consolidates entities of which it is the primary beneficiary.

The Company s variable interests in VIEs include debt and equity interests, commitments, guarantees, derivative instruments and certain fees. The Company s involvement with VIEs arises primarily from:

Interests purchased in connection with market-making activities, securities held in its AFS Securities portfolio and retained interests held as a result of securitization activities, including re-securitization transactions.

Guarantees issued and residual interests retained in connection with municipal bond securitizations.

Servicing of residential and commercial mortgage loans held by VIEs.

Loans made to and investments in VIEs that hold debt, equity, real estate or other assets.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Derivatives entered into with VIEs.

Structuring of credit-linked notes (CLN) or other asset-repackaged notes designed to meet the investment objectives of clients.

Other structured transactions designed to provide tax-efficient yields to the Company or its clients.

The Company determines whether it is the primary beneficiary of a VIE upon its initial involvement with the VIE and reassesses whether it is the primary beneficiary on an ongoing basis as long as it has any continuing involvement with the VIE. This determination is based upon an analysis of the design of the VIE, including the VIE s structure and activities, the power to make significant economic decisions held by the Company and by other parties, and the variable interests owned by the Company and other parties.

The power to make the most significant economic decisions may take a number of different forms in different types of VIEs. The Company considers servicing or collateral management decisions as representing the power to make the most significant economic decisions in transactions such as securitizations or CDOs. As a result, the Company does not consolidate securitizations or CDOs for which it does not act as the servicer or collateral manager unless it holds certain other rights to replace the servicer or collateral manager or to require the liquidation of the entity. If the Company serves as servicer or collateral manager, or has certain other rights described in the previous sentence, the Company analyzes the interests in the VIE that it holds and consolidates only those VIEs for which it holds a potentially significant interest of the VIE.

The structure of securitization vehicles and CDOs is driven by several parties, including loan seller(s) in securitization transactions, the collateral manager in a CDO, one or more rating agencies, a financial guarantor in some transactions and the underwriter(s) of the transactions, who serve to reflect specific investor demand. In addition, subordinate investors, such as the B-piece buyer (*i.e.,* investors in most subordinated bond classes) in commercial mortgage-backed securitizations or equity investors in CDOs, can influence whether specific loans are excluded from a CMBS transaction or investment criteria in a CDO.

For many transactions, such as re-securitization transactions, CLNs and other asset-repackaged notes, there are no significant economic decisions made on an ongoing basis. In these cases, the Company focuses its analysis on decisions made prior to the initial closing of the transaction and at the termination of the transaction. Based upon factors, which include an analysis of the nature of the assets, including whether the assets were issued in a transaction sponsored by the Company and the extent of the information available to the Company and to investors, the number, nature and involvement of investors, other rights held by the Company and investors, the standardization of the legal documentation and the level of the continuing involvement by the Company, including the amount and type of interests owned by the Company and by other investors, the Company concluded in most of these transactions that decisions made prior to the initial closing were shared between the Company and the initial investors. The Company focused its control decision on any right held by the Company or investors related to the termination of the VIE. Most re-securitization transactions, CLNs and other asset-repackaged notes have no such termination rights.

Except for consolidated VIEs included in other structured financings and managed real estate partnerships in the tables below, the Company accounts for the assets held by the entities primarily in Trading assets and the liabilities of the entities as Other secured financings in the condensed consolidated statements of financial condition. For consolidated VIEs included in other structured financings, the Company accounts for the assets held by the entities primarily in Premises, equipment and software costs, and Other assets in the condensed consolidated statements of financial condition. For consolidated VIEs included in managed real estate partnerships, the Company accounts for the assets held by the entities primarily in Trading assets in the condensed consolidated statements of financial condition. Except for consolidated VIEs included in other structured financings, the assets and liabilities are measured at fair value, with changes in fair value reflected in earnings.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The assets owned by many consolidated VIEs cannot be removed unilaterally by the Company and are not generally available to the Company. The related liabilities issued by many consolidated VIEs are non-recourse to the Company. In certain other consolidated VIEs, the Company either has the unilateral right to remove assets or provides additional recourse through derivatives such as total return swaps, guarantees or other forms of involvement.

As part of the Company s Institutional Securities business segment s securitization and related activities, the Company has provided, or otherwise agreed to be responsible for, representations and warranties regarding certain assets transferred in securitization transactions sponsored by the Company (see Note 11).

The following tables present information at September 30, 2014 and December 31, 2013 about VIEs that the Company consolidates. Consolidated VIE assets and liabilities are presented after intercompany eliminations and include assets financed on a non-recourse basis:

	At September 30, 2014			
	Mortgage and Asset-Backed Securitizations	Managed Real Estate Partnerships(1)	Other Structured Financings	Other
	(dollars in millions)			
VIE assets	$ 610	$ 282	$ 950	$ 1,306
VIE liabilities	$ 367	$ 4	$ 82	$

(1) On April 1, 2014, the Company deconsolidated approximately $1.6 billion in total assets that were related to certain legal entities associated with a real estate fund sponsored by the Company.

	At December 31, 2013			
	Mortgage and Asset-Backed Securitizations	Managed Real Estate Partnerships	Other Structured Financings	Other
	(dollars in millions)			
VIE assets	$ 643	$ 2,313	$ 1,202	$ 1,294
VIE liabilities	$ 368	$ 42	$ 67	$ 175

In general, the Company s exposure to loss in consolidated VIEs is limited to losses that would be absorbed on the VIE s assets recognized in its financial statements, net of losses absorbed by third-party holders of the VIE s liabilities. At September 30, 2014 and December 31, 2013, managed real estate partnerships reflected nonredeemable noncontrolling interests in the Company s condensed consolidated financial statements of $236 million and $1,771 million, respectively. The Company also had additional maximum exposure to losses of approximately $124 million and $101 million at September 30, 2014 and December 31, 2013, respectively. This additional exposure relates primarily to certain derivatives (*e.g.*, instead of purchasing senior securities, the Company has sold credit protection to synthetic CDOs through credit derivatives that are typically related to the most senior tranche of the CDO) and commitments, guarantees and other forms of involvement.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables present information about certain non-consolidated VIEs in which the Company had variable interests at September 30, 2014 and December 31, 2013. The tables include all VIEs in which the Company has determined that its maximum exposure to loss is greater than specific thresholds or meets certain other criteria. Most of the VIEs included in the tables below are sponsored by unrelated parties; the Company s involvement generally is the result of the Company s secondary market-making activities and securities held in its AFS Securities portfolio (see Note 5):

	At September 30, 2014				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Municipal Tender Option Bonds	Other Structured Financings	Other
	(dollars in millions)				
VIE assets that the Company does not consolidate (unpaid principal balance)(1)	$ 202,115	$ 30,386	$ 3,319	$ 1,777	$ 16,779
Maximum exposure to loss:					
Debt and equity interests(2)	$ 16,349	$ 3,084	$ 21	$ 1,116	$ 5,101
Derivative and other contracts	45	2	2,125		149
Commitments, guarantees and other	1,008	1,111		622	494
Total maximum exposure to loss	$ 17,402	$ 4,197	$ 2,146	$ 1,738	$ 5,744
Carrying value of exposure to loss Assets:					
Debt and equity interests(2)	$ 16,349	$ 3,084	$ 21	$ 702	$ 5,101
Derivative and other contracts	45	2	5		65
Total carrying value of exposure to loss Assets	$ 16,394	$ 3,086	$ 26	$ 702	$ 5,166
Carrying value of exposure to loss Liabilities:					
Derivative and other contracts	$	$	$	$	$ 49
Commitments, guarantees and other				6	
Total carrying value of exposure to loss Liabilities	$	$	$	$ 6	$ 49

(1) Mortgage and asset-backed securitizations include VIE assets as follows: $17.1 billion of residential mortgages; $89.4 billion of commercial mortgages; $28.8 billion of U.S. agency collateralized mortgage obligations; and $66.8 billion of other consumer or commercial loans.

(2) Mortgage and asset-backed securitizations include VIE debt and equity interests as follows: $0.9 billion of residential mortgages; $2.4 billion of commercial mortgages; $4.9 billion of U.S. agency collateralized mortgage obligations; and $8.1 billion of other consumer or commercial loans.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At December 31, 2013				
	Mortgage and Asset-Backed Securitizations	Collateralized Debt Obligations	Municipal Tender Option Bonds	Other Structured Financings	Other
	(dollars in millions)				
VIE assets that the Company does not consolidate (unpaid principal balance)(1)	$ 177,153	$ 29,513	$ 3,079	$ 1,874	$ 10,119
Maximum exposure to loss:					
Debt and equity interests(2)	$ 13,514	$ 2,498	$ 31	$ 1,142	$ 3,693
Derivative and other contracts	15	23	1,935		146
Commitments, guarantees and other		272		649	527
Total maximum exposure to loss	$ 13,529	$ 2,793	$ 1,966	$ 1,791	$ 4,366
Carrying value of exposure to loss Assets:					
Debt and equity interests(2)	$ 13,514	$ 2,498	$ 31	$ 731	$ 3,693
Derivative and other contracts	15	3	4		53
Total carrying value of exposure to loss Assets	$ 13,529	$ 2,501	$ 35	$ 731	$ 3,746
Carrying value of exposure to loss Liabilities:					
Derivative and other contracts	$	$ 2	$	$	$ 57
Commitments, guarantees and other				7	
Total carrying value of exposure to loss Liabilities	$	$ 2	$	$ 7	$ 57

(1) Mortgage and asset-backed securitizations include VIE assets as follows: $16.9 billion of residential mortgages; $78.4 billion of commercial mortgages; $31.5 billion of U.S. agency collateralized mortgage obligations; and $50.4 billion of other consumer or commercial loans.

(2) Mortgage and asset-backed securitizations include VIE debt and equity interests as follows: $1.3 billion of residential mortgages; $2.0 billion of commercial mortgages; $5.3 billion of U.S. agency collateralized mortgage obligations; and $4.9 billion of other consumer or commercial loans.

The Company s maximum exposure to loss often differs from the carrying value of the variable interests held by the Company. The maximum exposure to loss is dependent on the nature of the Company s variable interest in the VIEs and is limited to the notional amounts of certain liquidity facilities, other credit support, total return swaps, written put options, and the fair value of certain other derivatives and investments the Company has made in the VIEs. Liabilities issued by VIEs generally are non-recourse to the Company. Where notional amounts are utilized in quantifying maximum exposure related to derivatives, such amounts do not reflect fair value writedowns already recorded by the Company.

The Company s maximum exposure to loss does not include the offsetting benefit of any financial instruments that the Company may utilize to hedge these risks associated with the Company s variable interests. In addition, the Company s maximum exposure to loss is not reduced by the amount of collateral held as part of a transaction with the VIE or any party to the VIE directly against a specific exposure to loss.

Securitization transactions generally involve VIEs. Primarily as a result of its secondary market-making activities, the Company owned additional securities issued by securitization SPEs for which the maximum exposure to loss is less than specific thresholds. These additional securities totaled $11.5 billion at September 30, 2014. These securities were either retained in connection with transfers of assets by the Company, acquired in connection with secondary market-making activities or held in the Company s AFS Securities portfolio

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(see Note 5). Securities issued by securitization SPEs consisted of $0.9 billion of securities backed primarily by residential mortgage loans, $8.1 billion of securities backed by U.S. agency collateralized mortgage obligations, $1.0 billion of securities backed by commercial mortgage loans, $0.5 billion of securities backed by CDOs or CLOs and $1.0 billion backed by other consumer loans, such as credit card receivables, automobile loans and student loans. The Company s primary risk exposure is to the securities issued by the SPE owned by the Company, with the risk highest on the most subordinate class of beneficial interests. These securities generally are included in Trading assets Corporate and other debt or AFS Securities and are measured at fair value (see Note 4). The Company does not provide additional support in these transactions through contractual facilities, such as liquidity facilities, guarantees or similar derivatives. The Company s maximum exposure to loss generally equals the fair value of the securities owned.

The Company s transactions with VIEs primarily include securitizations, municipal tender option bond trusts, credit protection purchased through CLNs, other structured financings, collateralized loan and debt obligations, equity-linked notes, managed real estate partnerships and asset management investment funds. The Company s continuing involvement in VIEs that it does not consolidate can include ownership of retained interests in Company-sponsored transactions, interests purchased in the secondary market (both for Company-sponsored transactions and transactions sponsored by third parties), derivatives with securitization SPEs (primarily interest rate derivatives in commercial mortgage and residential mortgage securitizations and credit derivatives in which the Company has purchased protection in synthetic CDOs), and as servicer in residential mortgage securitizations in the U.S. and Europe and commercial mortgage securitizations in Europe. Such activities are further described in Note 7 to the consolidated financial statements in the 2013 Form 10-K.

Transfers of Assets with Continuing Involvement.

The following tables present information at September 30, 2014 regarding transactions with SPEs in which the Company, acting as principal, transferred financial assets with continuing involvement and received sales treatment:

	At September 30, 2014			
	Residential Mortgage Loans	Commercial Mortgage Loans	U.S. Agency Collateralized Mortgage Obligations	Credit-Linked Notes and Other
	(dollars in millions)			
SPE assets (unpaid principal balance)(1)	$ 26,172	$ 54,534	$ 19,538	$ 10,999
Retained interests (fair value):				
Investment grade	$ 11	$ 86	$ 890	$
Non-investment grade	70	74		1,142
Total retained interests (fair value)	$ 81	$ 160	$ 890	$ 1,142
Interests purchased in the secondary market (fair value):				
Investment grade	$ 11	$ 110	$ 54	$ 351
Non-investment grade	21	42		42
Total interests purchased in the secondary market (fair value)	$ 32	$ 152	$ 54	$ 393
Derivative assets (fair value)	$	$ 557	$	$ 95
Derivative liabilities (fair value)	$	$	$	$ 102

(1) Amounts include assets transferred by unrelated transferors.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At September 30, 2014			
	Level 1	Level 2	Level 3	Total
	(dollars in millions)			
Retained interests (fair value):				
Investment grade	$	$ 984	$ 3	$ 987
Non-investment grade		120	1,166	1,286
Total retained interests (fair value)	$	$ 1,104	$ 1,169	$ 2,273
Interests purchased in the secondary market (fair value):				
Investment grade	$	$ 525	$ 1	$ 526
Non-investment grade		83	22	105
Total interests purchased in the secondary market (fair value)	$	$ 608	$ 23	$ 631
Derivative assets (fair value)	$	$ 564	$ 88	$ 652
Derivative liabilities (fair value)	$	$ 97	$ 5	$ 102

The following tables present information at December 31, 2013 regarding transactions with SPEs in which the Company, acting as principal, transferred assets with continuing involvement and received sales treatment:

	At December 31, 2013			
	Residential Mortgage Loans	Commercial Mortgage Loans	U.S. Agency Collateralized Mortgage Obligations	Credit-Linked Notes and Other
	(dollars in millions)			
SPE assets (unpaid principal balance)(1)	$ 29,723	$ 60,698	$ 19,155	$ 11,736
Retained interests (fair value):				
Investment grade	$ 1	$ 102	$ 524	$
Non-investment grade	136	95		1,319
Total retained interests (fair value)	$ 137	$ 197	$ 524	$ 1,319
Interests purchased in the secondary market (fair value):				
Investment grade	$ 14	$ 170	$ 21	$ 350
Non-investment grade	41	97		68
Total interests purchased in the secondary market (fair value)	$ 55	$ 267	$ 21	$ 418
Derivative assets (fair value)	$ 1	$ 672	$	$ 121
Derivative liabilities (fair value)	$	$ 1	$	$ 120

(1) Amounts include assets transferred by unrelated transferors.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	At December 31, 2013			
	Level 1	Level 2	Level 3	Total
	(dollars in millions)			
Retained interests (fair value):				
Investment grade	$	$ 626	$ 1	$ 627
Non-investment grade		164	1,386	1,550
Total retained interests (fair value)	$	$ 790	$ 1,387	$ 2,177
Interests purchased in the secondary market (fair value):				
Investment grade	$	$ 547	$ 8	$ 555
Non-investment grade		182	24	206
Total interests purchased in the secondary market (fair value)	$	$ 729	$ 32	$ 761
Derivative assets (fair value)	$	$ 615	$ 179	$ 794
Derivative liabilities (fair value)	$	$ 110	$ 11	$ 121

Transferred assets are carried at fair value prior to securitization, and any changes in fair value are recognized in the condensed consolidated statements of income. The Company may act as underwriter of the beneficial interests issued by securitization vehicles. Investment banking underwriting net revenues are recognized in connection with these transactions. The Company may retain interests in the securitized financial assets as one or more tranches of the securitization. These retained interests are included in the condensed consolidated statements of financial condition at fair value. Any changes in the fair value of such retained interests are recognized in the condensed consolidated statements of income.

Net gains on sale of assets in securitization transactions at the time of the sale were not material in the quarters and nine months ended September 30, 2014 and 2013.

During the nine months ended September 30, 2014 and 2013, the Company received proceeds from new securitization transactions of $17.3 billion and $18.8 billion, respectively. During the nine months ended September 30, 2014 and 2013, the Company received proceeds from cash flows from retained interests in securitization transactions of $2.2 billion and $3.8 billion, respectively.

The Company has provided, or otherwise agreed to be responsible for, representations and warranties regarding certain assets transferred in securitization transactions sponsored by the Company (see Note 11).

In addition, in connection with its underwriting of CLO transactions for unaffiliated sponsors, in the nine months ended September 30, 2014 and 2013, the Company sold to those SPEs, corporate loans with an unpaid principal balance of $1.6 billion and $ 1.7 billion, respectively.

Failed Sales.

In order to be treated as a sale of assets for accounting purposes, a transaction must meet all of the criteria stipulated in the accounting guidance for the transfer of financial assets. If the transfer fails to meet these criteria, that transfer of financial assets is treated as a failed sale. In such cases, the Company continues to recognize the assets in Trading assets, and the Company recognizes the associated liabilities in Other secured financings in the condensed consolidated statements of financial condition (see Note 9).

The assets transferred in many transactions accounted for as failed sales cannot be removed unilaterally by the Company and are not generally available to the Company. The related liabilities are non-recourse to the Company. In certain other failed sale transactions, the Company has the right to remove assets or provide additional recourse through derivatives such as total return swaps, guarantees or other forms of involvement.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents information about the carrying value (equal to fair value) of assets and liabilities resulting from transfers of financial assets treated by the Company as secured financings:

	At September 30, 2014 Carrying Value of		At December 31, 2013 Carrying Value of	
	Assets	Liabilities	Assets	Liabilities
	(dollars in millions)			
Credit-linked notes	$ 47	$ 38	$ 48	$ 41
Equity-linked transactions	29	27	40	35
Other	181	181	157	156

Mortgage Servicing Activities.

The Company services residential mortgage loans in the U.S. owned by SPEs sponsored by the Company. The Company generally holds retained interests in Company-sponsored SPEs. As of the quarter ended March 31, 2014, the Company no longer services residential and commercial mortgage loans in Europe.

The Company provides no credit support as part of its servicing activities. The Company is required to make servicing advances to the extent that it believes that such advances will be reimbursed. Reimbursement of servicing advances is a senior obligation of the SPE, senior to the most senior beneficial interests outstanding. Outstanding advances are included in Other assets and are recorded at cost, net of allowances. There were no allowances at September 30, 2014 and December 31, 2013. Advances at September 30, 2014 and December 31, 2013 totaled approximately $11 million and $110 million, respectively.

The following tables present information about the Company s mortgage servicing activities for SPEs to which the Company transferred loans at September 30, 2014 and December 31, 2013:

	At September 30, 2014		
	Residential Mortgage Unconsolidated SPEs	Residential Mortgage Consolidated SPEs	Commercial Mortgage Unconsolidated SPEs
	(dollars in millions)		
Assets serviced (unpaid principal balance)	$	$ 457	$
Amounts past due 90 days or greater (unpaid principal balance)(1)	$	$ 26	$
Percentage of amounts past due 90 days or greater(1)		5.8%	
Credit losses	$	$ 2	$

(1) Amounts include loans that are at least 90 days contractually delinquent, loans for which the borrower has filed for bankruptcy, loans in foreclosure and real estate owned.

	At December 31, 2013		
	Residential Mortgage Unconsolidated SPEs	Residential Mortgage Consolidated SPEs	Commercial Mortgage Unconsolidated SPEs

		(dollars in millions)	
Assets serviced (unpaid principal balance)	$ 785	$ 775	$ 4,114
Amounts past due 90 days or greater (unpaid principal balance)(1)	$ 66	$ 44	$
Percentage of amounts past due 90 days or greater(1)	8.5%	5.6%	
Credit losses	$ 1	$ 17	$

(1) Amounts include loans that are at least 90 days contractually delinquent, loans for which the borrower has filed for bankruptcy, loans in foreclosure and real estate owned.

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Loans and Allowance for Loan Losses.
Loans.

The Company s loans held for investment are recorded at amortized cost, and its loans held for sale are recorded at lower of cost or fair value in the condensed consolidated statements of financial condition.

The Company s outstanding loans at September 30, 2014 and December 31, 2013 included the following:

	September 30, 2014			December 31, 2013		
Loans by Product Type	**Loans Held For Investment**	**Loans Held For Sale**	**Total Loans**	**Loans Held For Investment**	**Loans Held For Sale**	**Total Loans**
			(dollars in millions)			
Corporate loans	$ 18,589	$ 5,997	$ 24,586	$ 13,263	$ 6,168	$ 19,431
Consumer loans	15,389		15,389	11,577		11,577
Residential real estate loans	14,198	106	14,304	10,006	112	10,118
Wholesale real estate loans	3,430	641	4,071	1,855	49	1,904
Total loans, gross of allowance for loan losses	51,606	6,744	58,350	36,701	6,329	43,030
Allowance for loan losses	(141)		(141)	(156)		(156)
Total loans, net of allowance for loan losses(1)(2)	$ 51,465	$ 6,744	$ 58,209	$ 36,545	$ 6,329	$ 42,874

(1) Amounts include loans that are made to non-U.S. borrowers of $6,208 million and $4,729 million at September 30, 2014 and December 31, 2013, respectively.
(2) See Note 11 for further information related to unfunded lending commitments.

The above table does not include loans and lending commitments held at fair value that were recorded as Trading assets of $13,943 million and $12,612 million at September 30, 2014 and December 31, 2013, respectively. At September 30, 2014, loans and lending commitments held at fair value that were recorded as Trading assets consisted of $9,398 million of Corporate loans, $1,537 million of Residential real estate loans and $3,008 million of Wholesale real estate loans. At December 31, 2013, loans and lending commitments held at fair value that were recorded as Trading assets consisted of $9,774 million of Corporate loans, $1,434 million of Residential real estate loans and $1,404 million of Wholesale real estate loans. See Note 4 for further information regarding loans and lending commitments held at fair value that are recorded as Trading assets in the Company s condensed consolidated statement of financial condition.

Credit Quality.

The Company s Credit Risk Management department evaluates new obligors before credit transactions are initially approved, and at least annually thereafter for corporate and wholesale real estate loans. For corporate loans, credit evaluations typically involve the evaluation of financial statements, assessment of leverage, liquidity, capital strength, asset composition and quality, market capitalization and access to capital markets, cash flow projections and debt service requirements, and the adequacy of collateral, if applicable. Credit Risk Management will also evaluate strategy, market position, industry dynamics, obligor s management and other factors that could affect the obligor s risk profile. For wholesale real estate loans, the credit evaluation is focused on property and transaction metrics including property type, loan-to-value ratio, occupancy levels, debt service ratio, prevailing capitalization rates, and market dynamics. For residential real estate and consumer loans, the initial credit evaluation typically includes, but is not limited to, review of the obligor s income, net worth,

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

liquidity, collateral, loan-to-value ratio, and credit bureau information. Subsequent credit monitoring for residential real estate loans is performed at the portfolio level. Consumer loan collateral values are monitored on an ongoing basis.

For a description of the Company s loan portfolio and credit quality indicators utilized in its credit monitoring process, see Note 8 to the consolidated financial statements in the 2013 Form 10-K.

The following tables present credit quality indicators for the Company s loans held for investment, gross of allowance for loan losses, by product type, at September 30, 2014 and December 31, 2013.

	September 30, 2014				
Loans by Credit Quality Indicators	**Corporate**	**Consumer**	**Residential Real Estate**	**Wholesale Real Estate**	**Total**
			(dollars in millions)		
Pass	$ 17,923	$ 15,389	$ 14,154	$ 3,430	$ 50,896
Special Mention	567				567
Substandard	90		44		134
Doubtful	9				9
Loss					
Total loans	$ 18,589	$ 15,389	$ 14,198	$ 3,430	$ 51,606

	December 31, 2013				
Loans by Credit Quality Indicators	**Corporate**	**Consumer**	**Residential Real Estate**	**Wholesale Real Estate**	**Total**
			(dollars in millions)		
Pass	$ 12,893	$ 11,577	$ 9,992	$ 1,829	$ 36,291
Special Mention	189			16	205
Substandard	174		14		188
Doubtful	7			10	17
Loss					
Total loans	$ 13,263	$ 11,577	$ 10,006	$ 1,855	$ 36,701

Allowance for Loan Losses and Impaired Loans.

The allowance for loan losses estimates probable losses related to loans specifically identified for impairment in addition to the probable losses inherent in the held for investment loan portfolio.

There are two components of the allowance for loan losses: the inherent allowance component and the specific allowance component.

The inherent allowance component of the allowance for loan losses is used to estimate the probable losses inherent in the loan portfolio and includes non-homogeneous loans that have not been identified as impaired and portfolios of smaller balance homogeneous loans. The Company maintains methodologies by loan product for calculating an allowance for loan losses that estimates the inherent losses in the loan portfolio.

Qualitative and environmental factors such as economic and business conditions, nature and volume of the portfolio and lending terms, and volume and severity of past due loans may also be considered in the calculations. The allowance for loan losses is maintained at a level reasonable to ensure that it can adequately absorb the estimated probable losses inherent in the portfolio.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The specific allowance component of the allowance for loan losses is used to estimate probable losses for non-homogeneous exposures, including loans modified in a Troubled Debt Restructuring (TDR), which have been specifically identified for impairment analysis by the Company and determined to be impaired. As of September 30, 2014 and December 31, 2013, the Company s TDRs were not significant. For further information on allowance for loan losses, see Note 2 to the consolidated financial statements in the 2013 Form 10-K.

The tables below provide details on impaired loans, past due loans and allowances for the Company s held for investment loans:

	September 30, 2014				
Loans by Product Type	Corporate	Consumer	Residential Real Estate	Wholesale Real Estate	Total
	(dollars in millions)				
Impaired loans with allowance	$ 5	$	$	$	$ 5
Impaired loans without allowance(1)	9		29		38
Impaired loans unpaid principal balance	14		29		43
Past due 90 days loans and on nonaccrual	7		35		42

	December 31, 2013				
Loans by Product Type	Corporate	Consumer	Residential Real Estate	Wholesale Real Estate	Total
	(dollars in millions)				
Impaired loans with allowance	$ 63	$	$	$ 10	$ 73
Impaired loans without allowance(1)	6		11		17
Impaired loans unpaid principal balance	69		11	10	90
Past due 90 days loans and on nonaccrual	7		11	10	28

	September 30, 2014			
Loans by Region	Americas	EMEA	Asia-Pacific	Total
	(dollars in millions)			
Impaired loans	$ 43	$	$	$ 43
Past due 90 days loans and on nonaccrual	42			42
Allowance for loan losses	112	23	6	141

	December 31, 2013			
Loans by Region	Americas	EMEA	Asia-Pacific	Total
	(dollars in millions)			
Impaired loans	$ 90	$	$	$ 90
Past due 90 days loans and on nonaccrual	28			28
Allowance for loan losses	123	28	5	156

EMEA Europe, Middle East and Africa.

(1) At September 30, 2014 and December 31, 2013, no allowance was outstanding for these loans as the fair value of the collateral held exceeded or equaled the carrying value.

Table of Contents

MORGAN STANLEY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The table below summarizes information about the allowance for loan losses, loans by impairment methodology, the allowance for lending-related commitments and lending-related commitments by impairment methodology.

	Corporate	Consumer	Residential Real Estate (dollars in millions)	Wholesale Real Estate	Total
Allowance for loan losses:					
Balance at December 31, 2013	$ 137	$ 1	$ 4	$ 14	$ 156
Gross charge-offs				(3)	(3)
Gross recoveries				1	