1585 Broadway
New York, NY 10036

Morgan Stanley

March 5, 2009

Neil M. Barofsky
Special Investor General - TARP
1500 Pennsylvania Avenue, NW
Suite 1064
Washington, DC 20220
SIGTARP.response@do.treas.gov

BY EMAIL

Dear Mr. Barofsky:

I write in response to your letter of February 6, 2009, requesting information regarding Morgan Stanley's use of government funds received through the Treasury Department's Troubled Asset Relief Program (TARP). I appreciate the opportunity to share more with you about our role in the TARP program and how we are using the capital we received.

As you know, Morgan Stanley was one of nine financial institutions initially selected by the Treasury Department to receive an injection of capital under the TARP Capital Purchase Program (CPP), which has since been extended to many other financial institutions. On October 26, 2008, we entered into an agreement with the Treasury Department, pursuant to which we sold preferred stock and warrants to the Treasury Department for an aggregate purchase price of $10 billion. Since then, we have been putting that money to good use by focusing on our core businesses, including helping companies raise debt and equity in the capital markets.

Because Morgan Stanley received CPP funds as a capital injection, we did not segregate those funds and have no separate financial statements that would specify the use of funds that originated specifically with the U.S. Treasury's purchase of Morgan Stanley preferred shares. Similarly, we do not have any business plans that relate specifically to the use of CPP funds. Further, like all financial institutions, we are currently engaged in a constant process of revising our business plans to meet the demands of one of the most challenging business environments any of us has ever experienced.

With the infusion of CPP funds, we were able to increase the total debt raised for clients as lead manager nearly four-fold from October to December 2008. During the fourth quarter of 2008, we helped our clients raise $56 billion in debt to invest in their businesses, including leading American companies like Pepsi and Time Warner Cable. We also helped clients raise $40 billion in equity to fund their businesses. And, we made $10.6 billion in new commercial loans.

Although our consumer lending business is on a much smaller scale than our capital markets and commercial lending businesses, we also expanded our retail banking solutions for clients. We made approximately $650 million in new commitments to lend to consumers during the last three months of 2008, a majority of which were for financing or re-financing of residential and commercial real estate and capital for small businesses, at a time when traditional sources of capital were difficult to secure.

Some of the highlights of our major transactions during the fourth quarter of 2008 include:

- Debt Underwriting. Morgan Stanley underwrote approximately 10 percent of U.S. dollar denominated debt in October 2008—a 274 percent increase over the prior month—primarily as a result of our role in major issuances for Pepsi ($3.3 billion) and Verizon Communications ($3.3 billion). We then increased our debt underwriting by another 62 percent in November 2008, including $2 billion for Time Warner Cable, $3.5 billion for Verizon Wireless and $3 billion for BP Capital Markets.

- Equity Underwriting. Morgan Stanley assisted clients in raising nearly $17 billion in equity capital in October 2008, another $13.5 billion in November, and $10 billion in December. We underwrote the largest transactions of the month in both October and November: a $12 billion issuance for GE in October and a $13 billion offering for Wells Fargo in November.

- Commercial Lending C&I. Despite a challenging environment for the non-investment grade commercial lending market, Morgan Stanley approved $10.6 billion in new loans for the fourth quarter of 2008.

In response to your query regarding the executive compensation requirements initially associated with the receipt of CPP funds, we can also offer you assurances regarding how CPP funds have *not* been spent. We understand that the American people are concerned that the financial institutions that have received capital under the TARP program are using these funds wisely. In particular, we know that the American people have been angered by some of the practices on Wall Street relating to compensation and expense management. Accordingly, we have taken steps to ensure that Morgan Stanley is a responsible steward of the public's investment in our business.

Regarding compensation, I can assure you that, while money is fungible, CPP had no impact on the 2008 bonus pool at Morgan Stanley because bonuses paid by the Firm are determined and funded by revenues, not capital. In other words, bonuses paid by the Firm are funded by earnings and not by the U.S. Treasury's investment. The Firm accrues its bonus pool monthly throughout the year based on the Firm's financial performance, and publicly reports compensation expenses quarterly (which includes bonus accruals). In fact, 2008 compensation expenses were lower, not higher, than had been anticipated prior to Morgan Stanley's receipt of CPP funds, due to the challenging market conditions in the later part of 2008.

The following are additional examples of the policies we have implemented to demonstrate how seriously we take our obligation to be good stewards of our shareholders' dollars, including those dollars invested by American taxpayers:

- Executive compensation. We are committed to using executive compensation to align our executives' interests with those of our stockholders, and, accordingly, the American people. Our Chairman and CEO John Mack and our co-presidents Walid Chammah and James Gorman have foregone bonuses for 2008. The 2008 year-end compensation for the 14 members of the Firm's Operating Committee is down an average of 75 percent compared to last year, while the 2008 year-end compensation for the 35 members of our Management Committee is down an average of 65 percent;

- "Clawback" provision. Morgan Stanley was the first U.S. bank to institute a "clawback" provision that allows us to reclaim certain pay from anyone who engages in detrimental conduct or causes a significant financial loss to the Firm. This clawback provision goes beyond what was initially required by TARP because it applies to a broad group of Firm employees and can be triggered by a broad range of actions and events;

- Dividend payouts. Under the terms of the TARP agreement, Morgan Stanley is prohibited from increasing dividends on its common stock, and from making certain repurchases of equity securities, including its common stock, without the U.S. Treasury's consent. Further, as long as the preferred stock to the U.S. Treasury is outstanding, dividend payments and repurchases or redemptions relating to certain equity securities, including Morgan Stanley's common stock, are prohibited until all accrued and unpaid dividends are paid on such preferred stock, subject to limited exceptions;

- "Golden Parachutes". Morgan Stanley's Senior Executive Officers currently are not entitled to cash severance payments upon any termination of employment (including a termination in connection with a bankruptcy, insolvency, or receivership), other than Mr. Mack upon his death or disability;

- Tax Deductions. Morgan Stanley will not take tax deductions for the portion of 2008 beginning with the date of the U.S. Treasury's investment in the Firm for compensation in excess of $500,000 paid to Senior Executive Officers; and

- Risk-Taking: The Compensation, Management Development and Succession ("CMDS") Committee of Morgan Stanley's Board of Directors met with the Firm's Chief Risk Officer to assess whether the structure and design of the Firm's compensation arrangements with executive officers encourage unnecessary and excessive risk-taking that threatens the Firm's value. The CMDS Committee concluded that the current compensation arrangements do not encourage unnecessary and excessive risk-taking. In addition, the CMDS Committee considered risk issues in designing a new performance-based compensation program to further reinforce senior management's accountability for

the Firm's long-term financial performance by tying a greater portion of their compensation directly to the Firm's long-term core financial metrics.

Of course, as a Firm we continually review our compensation practices to ensure, *inter alia*, that we comply with all applicable rules and regulations. That process is ongoing.

I hope this response satisfies your concerns. I certify that, to my knowledge, this response does not contain any untrue statement of material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading.

If I can be of further assistance, please do not hesitate to contact me.

Sincerely yours,

Colm Kelleher
Executive Vice President & Chief Financial Officer