Registered number: 01281415

Registered office:
25 Cabot Square
Canary Wharf
London
E14 4QA
United Kingdom

MORGAN STANLEY UK GROUP

Report and financial statements

31 December 2017

6

MORGAN STANLEY UK GROUP

CONTENTS **PAGE**

MORGAN STANLEY UK GROUP

STRATEGIC REPORT

The Directors present their Strategic report for Morgan Stanley UK Group (the "Company") for the year ended 31 December 2017.

PRINCIPAL ACTIVITY

During 2017, the Company's principal activity was to act as an intermediate holding Company and provide property services to other Morgan Stanley Group undertakings.

In June 2017, the Company transferred the majority of it investments to other Morgan Stanley Group undertakings, and therefore from this date and going forward the Company's principal activity is primarily to provide property services to other Morgan Stanley Group undertakings.

The Company's ultimate parent undertaking and controlling entity is Morgan Stanley, which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the "Morgan Stanley Group". The Company's immediate parent undertaking is Morgan Stanley International Limited, which, together with its subsidiaries forms the "MSI Group".

The Company is designated a material service entity in the recovery and/or resolution plans of the Morgan Stanley Group and the MSI Group.

Further information on the Morgan Stanley Group and MSI Group is available in the public documents available at www.morganstanley.com/investorrelations.

No significant change in the Company's principal activity is expected.

BUSINESS REVIEW

The Company provides property services to Morgan Stanley Group's operating undertakings. The scope of services provided and contractual arrangements of the Company may continue to evolve as a normal consequence of changes to the recovery and resolution planning requirements or other regulatory changes impacting the Morgan Stanley Group or the MSI Group (including but not limited to the impact of United Kingdom's (the "UK") decision to leave the European Union (the "EU"). The Company manages these potential impacts on its business by maintaining a constant planning dialogue with all Morgan Stanley Group undertakings supported.

Overview of 2017 performance

The income statement for the year is set out on page 8. The Company generated a profit after tax for the financial year of $331,089,000 compared with a profit of $133,722,000 after tax in the prior year. Results of both years are impacted by the Company's previous investing activities, which generated returns of $359,428,000 in 2017 and $159,660,000 in the prior year. Modified for the impact of these investing activities, the Company generated positive pre-tax results of $754,000 for current year and $2,625,000 for prior year. The decline in earnings is primarily the result of the Company and Morgan Stanley Group updating its Global Transfer Pricing Policy, effective 1 January 2017. This change in transfer pricing policy is consistent with evolving transfer pricing guidance under the Organisation for Economic Co-operation and Development (the "OECD")'s and evolving regulatory guidance. Following this change, the Company charges other Morgan Stanley Group undertakings on primarily a cost recovery basis.

As a result of the Company completing several transactions, as a means of simplifying its capital structure, assets and liabilities have decreased year over year. The decrease in the Company's total assets of $17,529,580,000 is primarily due to a decrease of $16,333,802,000 in investments in subsidiaries. Total liabilities decreased to $697,276,000, primarily due to repayment of financing from other Morgan Stanley Group undertakings.

The performance of the Company is included in the results of the Morgan Stanley and MSI Group. The Company's Directors believe that providing further performance indicators for the Company itself would not enhance an understanding of the development, performance or position of the business of the Company.

STRATEGIC REPORT

BUSINESS REVIEW (CONTINUED)

Risk management

The key risk of the Company is its exposure to other Morgan Stanley Group undertakings. In 2017 the Morgan Stanley Group established a global network of material service entities, and as a material service entity, the Company is subject to additional operational oversight and governance. This additional governance is designed to support the continuity of support services in business as usual and recovery and resolution scenarios. The risks of the Company, expressed in terms of the Morgan Stanley Group risk categories are set out below. Further information on how the Morgan Stanley Group and MSI Group manage these risks is available in the public documents available at www.morganstanley.com/investorrelations.

Credit risk
Credit risk refers to the risk of loss arising when a borrower, counterparty or issuer does not meet its financial obligations to the Company. Credit risk includes the risk that economic, social and political conditions and events in a foreign country will adversely affect an obligor's ability and willingness to fulfil their obligations.

As noted above, the primary credit risk of the entity is the concentration of exposure to other Morgan Stanley Group undertakings.

Liquidity risk
Liquidity risk refers to the risk that the Company will be unable to finance its operations. The Company sources its financing from other Morgan Stanley Group undertakings.

As a material service entity the Company maintains minimum liquidity, which is monitored on an ongoing basis to ensure compliance with recovery and resolution requirements as established by Morgan Stanley Group's regulators as described above.

Operational risk
Operational risk refers to the risk of loss, or of damage to the Company's reputation, resulting from inadequate or failed processes, people and systems, or from external events (e.g. fraud, theft, legal and compliance risks, cyber attacks or damage to physical assets).

GOING CONCERN

Retaining sufficient liquidity and capital to withstand market pressures remains central to the Company's strategy. The Company has access to Morgan Stanley Group capital and liquidity as required.

Taking the above factors into consideration, the Directors believe it is reasonable to assume that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Approved by the Board and signed on its behalf by

Susan Watts – Director
20 April 2018

DIRECTORS' REPORT

The Directors present their report and financial statements (which comprise the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of financial position and the related notes, 1 to 23) for the Company for the year ended 31 December 2017.

RESULTS AND DIVIDENDS

The profit for the year, after tax, was $331,089,000 (2016: $133,722,000 profit after tax).

The Company paid the following dividends during the year (see note 20):

- on 3 May 2017, the Directors approved a coupon payment on the Additional Tier 1 capital instruments of $118,625,000 (2016: $157,625,000) which was paid on 31 May 2017;
- on 4 May 2017, the Company paid a dividend of $3,940,000 (2016: $20,027,000) to the Company's Class A preference shareholder;
- on 5 May 2017, the Company paid $69,910,000 (2016: $nil) and $74,344,000 (2016: $nil) to the Company's Class B preference shareholder and Class C preference shareholder respectively;
- on 8 June 2017, the Company paid a dividend in specie of its equity interest in Morgan Stanley UK Limited to Morgan Stanley International Limited of $201 (2016: $nil); and
- on 12 June 2017, the Company paid a dividend in specie of $14,633,802,000 (2016: $nil) to Morgan Stanley International Limited, transferring equity interest in Morgan Stanley Investments (UK).

RISK MANAGEMENT AND FUTURE DEVELOPMENTS

Information regarding risk management and future developments has been included in the Strategic report.

DIRECTORS

The following Directors held office throughout the year and to the date of approval of this report:

J D Bendall
K M Lazaroo
S E Watts

DIRECTORS' AND OFFICERS' LIABILITY INSURANCE

Directors' and Officers' Liability Insurance is taken out by Morgan Stanley, the Company's ultimate parent undertaking, for the benefit of the Directors and Officers of the Company and its subsidiary undertakings.

DIRECTORS' INDEMNITY

Qualifying third party indemnity provisions (as defined in Section 234 of the Companies Act 2006) were in force during the year and up to and including the date of the Directors' report for the benefit of the Directors of the Company and its subsidiary undertakings.

EVENTS AFTER THE REPORTING DATE

There have been no significant events since the reporting date.

DIRECTORS' REPORT

AUDITOR

Deloitte LLP have expressed their willingness to continue in office as auditor of the Company and, under Sections 485 to 488 of the Companies Act 2006, will be deemed to be re-appointed.

Statement as to disclosure of information to the auditor

Each of the persons who are Directors of the Company at the date when this report is approved confirms that:

- so far as each of the Directors is aware, there is no relevant audit information (being information needed by the Company's auditor in connection with preparing their report) of which the Company's auditor is unaware; and
- each of the Directors has taken all the steps that he/she ought to have taken as a Director to make himself/herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

DIRECTORS' RESPONSIBILITIES STATEMENT

The Directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with UK Generally Accepted Accounting Practice (UK Accounting Standards and applicable law), including Financial Reporting Standard ("FRS") 101 *Reduced disclosure framework* ("FRS 101"). Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards, including FRS 101, have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Approved by the Board and signed on its behalf by

Susan Watts – Director

20 April 2018

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY UK GROUP

Opinion

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2017 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice including Financial Reporting Standard 101 "Reduced disclosure framework"; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of Morgan Stanley UK Group which comprise:

- the income statement;
- the statement of comprehensive income;
- the statement of changes in equity;
- the statement of financial position; and
- the related notes 1 to 23.

The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards, including Financial Reporting Standard 101 "Reduced disclosure framework" (United Kingdom Generally Accepted Accounting Practice).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the Directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the Directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the Company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY UK GROUP (CONTINUED)

Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in respect of these matters.

Responsibilities of Directors

As explained more fully in the Directors' responsibilities statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MORGAN STANLEY UK GROUP (CONTINUED)

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report or the Directors' Report.

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of Directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

James Polson (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom
20 April 2018

MORGAN STANLEY UK GROUP

INCOME STATEMENT
Year ended 31 December 2017

	Note	2017 $'000	2016 $'000
Fee income		229,087	271,986
Net gains on available-for-sale financial assets	4	10,803	2,035
Net gains on investments in subsidiaries	5	348,625	157,625
Interest income	6	74,518	33,516
Interest expense	6	(90,294)	(56,067)
Other income	7	494	697
Other expense	8	(213,051)	(247,507)
PROFIT BEFORE TAXATION		360,182	162,285
Income tax expense	9	(29,093)	(28,563)
PROFIT FOR THE YEAR		331,089	133,722

All operations were continuing in the current and prior year.

The notes on pages 12 to 33 form an integral part of the financial statements.

STATEMENT OF COMPREHENSIVE INCOME
Year ended 31 December 2017

	Note	2017 $'000	2016 $'000
PROFIT FOR THE YEAR		331,089	133,722
OTHER COMPREHENSIVE INCOME, NET OF TAX			
Items that may be reclassified subsequently to profit or loss:			
Available-for-sale reserve:			
Net change in fair value of available-for-sale financial assets	11	550	(1,205)
Net amount reclassified to income statement	11	(10,803)	-
OTHER COMPREHENSIVE INCOME AFTER INCOME TAX FOR THE YEAR		(10,253)	(1,205)
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		320,836	132,517

The notes on pages 12 to 33 form an integral part of the financial statements.

MORGAN STANLEY UK GROUP

STATEMENT OF CHANGES IN EQUITY
Year ended 31 December 2017

	Note	Share capital $'000	Share premium $'000	Available-for-sale reserve $'000	Capital contribution reserve $'000	Capital redemption reserve $'000	Retained earnings $'000	Total equity $'000
Balance at 1 January 2016		7,138,796	304,218	11,458	6,064,670	250,000	2,352,002	16,121,144
Profit for the year		-	-	-	-	-	133,722	133,722
Other comprehensive income		-	-	(1,205)	-	-	-	(1,205)
Total comprehensive income		-	-	(1,205)	-	-	133,722	132,517
Transactions with owners:								
Dividends	20	-	-	-	-	-	(148,900)	(148,900)
Balance at 31 December 2016		7,138,796	304,218	10,253	6,064,670	250,000	2,336,824	16,104,761
Profit for the year		-	-	-	-	-	331,089	331,089
Other comprehensive income		-	-	(10,253)	-	-	-	(10,253)
Total comprehensive income		-	-	(10,253)	-	-	331,089	320,836
Transactions with owners:								
Dividends	20	-	-	-	-	-	(14,877,224)	(14,877,224)
Cancellation of A preference shares	19	(200,000)	-	-	-	-	-	(200,000)
Issue of capital	19	6,314,670	-	-	(6,064,670)	(250,000)	-	-
Cancellation of Additional Tier 1 capital	19	(1,300,000)	-	-	-	-	-	(1,300,000)
Reduction of capital	19	(11,943,466)	(304,218)	-	-	-	12,247,684	-
Balance at 31 December 2017		10,000	-	-	-	-	38,373	48,373

The notes on pages 12 to 33 form an integral part of the financial statements.

MORGAN STANLEY UK GROUP

Registered number: 01281415

STATEMENT OF FINANCIAL POSITION
As at 31 December 2017

	Note	2017 $'000	2016 $'000
ASSETS			
Loans and receivables:			
Cash and short-term deposits		51,242	665
Other receivables	10	363,646	1,532,199
		414,888	1,532,864
Available-for-sale financial assets	11	-	39,275
Current tax assets		980	706
Prepayments and accrued income		23,446	29,912
Investments in subsidiaries	12	78	16,333,880
Property, plant and equipment	13	306,257	338,592
TOTAL ASSETS		745,649	18,275,229
LIABILITIES AND EQUITY			
Financial liabilities at amortised cost:			
Subordinated loans	14	-	359,563
Other payables	15	482,032	1,623,185
		482,032	1,982,748
Provisions	16	118,861	85,417
Current tax liabilities		8,037	-
Deferred tax liabilities	17	7,575	10,222
Accruals and deferred income		80,771	92,081
TOTAL LIABILITIES		697,276	2,170,468
EQUITY			
Share capital	19	10,000	7,138,796
Share premium account	19	-	304,218
Available-for-sale reserve	19	-	10,253
Capital contribution reserve	19	-	6,064,670
Capital redemption reserve	19	-	250,000
Retained earnings		38,373	2,336,824
Equity attributable to owners of the Company		48,373	16,104,761
TOTAL EQUITY		48,373	16,104,761
TOTAL LIABILITIES AND EQUITY		745,649	18,275,229

These financial statements were approved by the Board and authorised for issue on 20 April 2018

Signed on behalf of the Board

Susan Watts - Director

The notes on pages 12 to 33 form an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

1. CORPORATE INFORMATION

The Company is incorporated and domiciled in England and Wales, UK, at the following registered address: 25 Cabot Square, Canary Wharf, London, E14 4QA, UK. The Company is a private company and is unlimited by shares. The registered number of the Company is 01281415.

The Company's immediate parent undertaking is Morgan Stanley International Limited, which has its registered office at 25 Cabot Square, Canary Wharf, London, E14 4QA and is registered in England and Wales, UK. Copies of its financial statements can be obtained from the Registrar of Companies for England and Wales, Companies House, Crown Way, Cardiff, CF14 3UZ.

The Company's ultimate parent undertaking and controlling entity and the largest and smallest group of which the Company is a member and for which group financial statements are prepared is Morgan Stanley which, together with the Company and Morgan Stanley's other subsidiary undertakings, form the Morgan Stanley Group. Morgan Stanley has its registered office c/o The Corporation Trust Company, The Corporation Trust Center, 1209 Orange Street, Wilmington, DE 19801, United States of America and is incorporated in the state of Delaware, in the United States of America. Copies of its financial statements can be obtained from www.morganstanley.com/investorrelations.

2. BASIS OF PREPARATION

The Company is not required to prepare consolidated financial statements by virtue of the exemption under Section 401 of the Companies Act 2006. The results of the Company are included within the financial statements of Morgan Stanley, which has prepared consolidated financial statements for the year ended 31 December 2017. The financial statements therefore present information about the Company as an individual entity and not about its group.

Statement of compliance

These financial statements are prepared in accordance with UK Generally Accepted Accounting Practice (UK Accounting Standards and applicable law), including FRS 101.

The Company meets definition of a qualifying entity as defined in FRS 100 *Application of financial reporting requirements*. The Company has taken advantage of the disclosure exemptions available under FRS 101 in relation to financial instruments, fair value measurement, capital management, presentation of comparative information in respect of certain assets and shares outstanding, presentation of a cash-flow statement, accounting standards not yet effective and related party transactions.

Where relevant, equivalent disclosures have been provided in the group accounts of Morgan Stanley, in which the Company is consolidated. Copies of Morgan Stanley's accounts can be obtained as detailed at note 1.

New standards and interpretations adopted during the year

The following amendment to standards relevant to the Company's operations was adopted during the year. This amendment did not have a material impact on the Company's financial statements.

An amendment to International Accounting Standards ("IAS") 12 *'Income taxes'* was issued by the International Accounting Standards Board ("IASB") in January 2016, for application in annual periods beginning on or after 1 January 2017. The amendment was endorsed by the EU in November 2017.

There were no other standards or interpretations relevant to the Company's operations which were adopted during the year.

2. BASIS OF PREPARATION (CONTINUED)

International Financial Reporting Standard 9 'Financial instruments' ("IFRS 9")

IFRS 9 was issued by the IASB in November 2009, reissued in October 2010, amended in November 2013, and revised and reissued by the IASB in July 2014. IFRS 9 is applicable retrospectively, except where otherwise prescribed by transitional provisions of the standard, and is effective for annual periods beginning on or after 1 January 2018. The standard was endorsed by the EU in November 2016. The impact of the implementation of IFRS 9 on retained earnings as at 1 January 2018 is not material to the Company.

Basis of measurement

The financial statements of the Company are prepared under the historical cost basis, except for certain financial instruments that have been measured at fair value as explained in the accounting policies below, and in accordance with applicable UK Accounting Standards, including FRS 101, and UK company law.

Critical judgements in applying the Company's accounting policies

No judgements have been made in the process of applying the Company's accounting policies that have had a significant effect on the amounts recognised in the financial statements.

The going concern assumption

The Company's business activities, together with the factors likely to affect its future development, performance and position, are reflected in the Business Review section of the Strategic report on pages 1 to 2.

As set out in the Strategic report, retaining sufficient liquidity and capital to withstand market pressures remains central to the Morgan Stanley Group's and the Company's strategy.

Taking the above factors into consideration, the Directors believe it is reasonable to assume that the Company will have access to adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Functional currency

Items included in the financial statements are measured and presented in US dollars, the currency of the primary economic environment in which the Company operates.

All currency amounts in the financial statements and Strategic and Directors' reports are rounded to the nearest thousand US dollars.

b. Foreign currencies

All monetary assets and liabilities denominated in currencies other than US dollars are translated into US dollars at the rates ruling at the reporting date. Transactions and non-monetary assets and liabilities denominated in currencies other than US dollars are recorded at the rates prevailing at the dates of the transactions. Foreign exchange differences on available-for-sale financial assets are recorded in the 'Available-for-sale reserve' in equity. All other translation differences are taken through the income statement. Exchange differences recognised in the income statement are presented in 'Other income' or 'Other expense', except where noted in 3(c) below.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

c. Financial instruments

The Company classifies its financial assets into the following categories on initial recognition: available-for-sale financial assets, investments in subsidiaries and loans and receivables.

The Company classifies its financial liabilities as financial liabilities at amortised cost on initial recognition.

More information regarding these classifications is included below:

i) Available-for-sale financial assets

Financial assets classified as available-for-sale are non-derivative financial assets that are either designated in this category or not classified in any of the other categories of financial instruments. Financial assets classified as available-for-sale are recorded on trade date and are initially recognised and subsequently measured at fair value (see note 3(d) below).

Transaction costs that are directly attributable to the acquisition of an available-for-sale financial asset are added to the fair value on initial recognition.

For equity instruments, dividend income and impairment losses are recognised in the income statement in 'Net gains/ (losses) on available-for-sale financial assets'. All other gains and losses on equity instruments classified as available-for-sale are recognised in the 'Available-for-sale reserve' within equity.

On disposal or impairment of an available-for-sale financial asset, the cumulative gain or loss in the 'Available-for-sale reserve' is reclassified to the income statement and reported in 'Net gains/ (losses) on available-for-sale financial assets'.

ii) Investments in subsidiaries

Subsidiaries are entities over which the Company has control. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Investments in subsidiaries are stated at cost, less provision for any impairment (see note 3(f) below). Dividends, impairment losses and reversals of impairment losses are recognised in the income statement in 'Net gains/ (losses) on investments in subsidiaries'.

iii) Loans and receivables and financial liabilities at amortised cost

Financial assets classified as loans and receivables are recognised when the Company becomes a party to the contractual provisions of the instrument. They are initially measured at fair value (see note 3(d) below) and subsequently measured at amortised cost less allowance for impairment. Interest is recognised in the income statement in 'Interest income', using the effective interest rate method as described below. Transaction costs that are directly attributable to the acquisition of the financial asset are added to or deducted from the fair value on initial recognition. Impairment losses and reversals of impairment losses on financial assets classified as loans and receivables are recognised in the income statement in 'Other expense'.

Financial assets classified as loans and receivables include cash and short-term deposits and other receivables.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

c. Financial instruments (continued)

iii) Loans and receivables and financial liabilities at amortised cost (continued)

Financial liabilities at amortised cost are recognised when the Company becomes a party to the contractual provisions of the instrument. They are initially measured at fair value (see note 3(d) below) and subsequently measured at amortised cost. Interest is recognised in the income statement in 'Interest expense' using the effective interest rate method as described below. Transaction costs that are directly attributable to the issue of the financial liability are added to or deducted from the fair value on initial recognition.

The effective interest rate method is a method of calculating the amortised cost of a financial instrument (or a group of financial instruments) and of allocating the interest income or interest expense over the expected life of the financial instrument. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial instrument (or, where appropriate a shorter period) to the carrying amount of the financial instrument. The effective interest rate is established on initial recognition of the financial instrument. The calculation of the effective interest rate includes all fees and commissions paid or received, transaction costs, and discounts or premiums that are an integral part of the effective interest rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument.

d. Fair value

Fair value measurement
Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e. the "exit price") in an orderly transaction between market participants at the measurement date.

Fair value is a market-based measure considered from the perspective of a market participant rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, assumptions are set to reflect those that the Company believes market participants would use in pricing the asset or liability at the measurement date.

In determining fair value, the Company uses various valuation approaches and establishes a hierarchy for inputs used in measuring fair value that maximises the use of relevant observable inputs and minimises the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability that were developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect assumptions the Company believes other market participants would use in pricing the asset or liability, that are developed based on the best information available in the circumstances.

The hierarchy is broken down into three levels based on the observability of inputs as follows, with Level 1 being the highest and Level 3 being the lowest level:

- Level 1 – Quoted prices (unadjusted) in an active market for identical assets or liabilities

  Valuations based on quoted prices in active markets that the Morgan Stanley Group has the ability to access for identical assets or liabilities. Valuation adjustments and block discounts are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgement.

- Level 2 – Valuation techniques using observable inputs

  Valuations based on one or more quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

d. Fair value (continued)

Fair value measurement (continued)

- Level 3 – Valuation techniques with significant unobservable inputs

  Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

The availability of observable inputs can vary from product to product and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new and not yet established in the marketplace, the liquidity of markets and other characteristics particular to the product. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgement. Accordingly, the degree of judgement exercised by the Company in determining fair value is greatest for instruments categorised in Level 3 of the fair value hierarchy.

Valuation techniques
Where appropriate, valuation adjustments are made to account for various factors such as liquidity risk (bid-ask adjustments), credit quality, model uncertainty and concentration risk.

Adjustments for liquidity risk adjust model-derived mid-market levels of Level 2 and Level 3 financial instruments for the bid-mid or mid-ask spread required to properly reflect the exit price of a risk position. Bid-mid and mid-ask spreads are marked to levels observed in trade activity, broker quotes or other external third-party data. Where these spreads are unobservable for the particular position in question, spreads are derived from observable levels of similar positions.

Adjustments for model uncertainty are taken for positions whose underlying models are reliant on significant inputs that are neither directly nor indirectly observable, hence requiring reliance on established theoretical concepts in their derivation. These adjustments are derived by making assessments of the possible degree of variability using statistical approaches and market-based information where possible.

Valuation process
The Valuation Review Group ("VRG") within the Financial Control Group ("FCG") is responsible for the Company's fair value valuation policies, processes and procedures. VRG is independent of the business units and reports to the Chief Financial Officer of the Morgan Stanley Group ("CFO"), who has final authority over the valuation of the Company's financial instruments. VRG implements valuation control processes designed to validate the fair value of the Company's financial instruments measured at fair value including those derived from pricing models.

e. Derecognition of financial assets and liabilities

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risk and rewards of ownership of the asset.

If the asset has been transferred, and the entity neither transfers nor retains substantially all of the risks and rewards of the asset, then the entity determines whether it has retained control of the asset.

If the entity has retained control of the asset, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset. If the entity has not retained control of the asset, it derecognises the asset and separately recognises any rights or obligation created or retained in the transfer.

The Company derecognises financial liabilities when the Company's obligations are discharged, cancelled or they expire.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Impairment of financial assets

At each reporting date, an assessment is made as to whether there is any objective evidence of impairment in the value of a financial asset classified as either available-for-sale, loans and receivables or investments in subsidiaries. Impairment losses are recognised if an event has occurred which will have an adverse impact on the expected future cash flows of an asset and the expected impact can be reliably estimated.

Impairment losses on available-for-sale financial assets are measured as the difference between cost (net of any principal repayment and amortisation) and the current fair value (see note 3(d) above). Where there is evidence that the available-for-sale financial asset is impaired, the cumulative loss that had been previously recognised in other comprehensive income is reclassified from the 'Available-for-sale reserve' and recognised in the income statement within 'Net gains/ (losses) on available-for-sale financial assets'.

Impairment losses on investments in subsidiaries are measured as the difference between cost and the current estimated recoverable amount. When the recoverable amount is less than the cost, an impairment is recognised within the income statement in 'Net gains/ (losses) on investments in subsidiaries' and is reflected against the carrying amount of the impaired asset on the statement of financial position.

Impairment losses on loans and receivables are measured as the difference between the carrying amount of the loans and receivables and the present value of estimated cash flows discounted at the asset's original effective interest rate. Such impairment losses are recognised in the income statement within 'Other expense' and are recognised against the carrying amount of the impaired asset on the statement of financial position. Interest on the impaired asset continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset.

Subsequent increases in the fair value of previously impaired equity available-for-sale financial assets are reported as fair value gains in the 'Available-for-sale reserve' through other comprehensive income and not separately identified as an impairment reversal. For all other financial assets, if in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed as described for the relevant categories of financial asset in note 3(c)(ii) and (iii). Any reversal is limited to the extent that the value of the asset may not exceed the original amortised cost of the asset had no impairment occurred.

g. Fee income

Fee income within the income statement includes fee income from Morgan Stanley Group undertakings for the provision of property services. These amounts are recognised as the related services are performed or received.

h. Property, plant and equipment

Property, plant and equipment are stated at cost net of depreciation and any provision for impairment in value (see note 3(i) below) which are included within 'Other expense' in the income statement.

For premises held under operating leases, a reinstatement provision is recognised for the estimated cost to reinstate the premises at the end of the lease period. When the reinstatement provision is established and included within 'Provisions' in the statement of financial position, an equivalent asset is recognised and included in the cost of leasehold improvements at the initial present value of the reinstatement obligations. The discount effect included in the reinstatement provision is reversed over time using a constant effective yield method and included within 'Interest expense' in the income statement. The reinstatement asset is depreciated over the useful economic life of the relevant leasehold improvement asset and the depreciation charge is included within 'Other expense' in the income statement.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

h. Property, plant and equipment (continued)

Depreciation is provided on property, plant and equipment at rates calculated to write off the cost of the assets on a straight line basis over their expected useful lives as follows:

Leasehold improvements, including reinstatement assets	- shorter of remaining lease term and 39 years
Fixtures, fittings and equipment	- 2 to 9 years

The carrying amount of an item of property, plant and equipment shall be derecognised on disposal or when no further economic benefits are expected from its use or disposal.

Gains and losses on disposals are determined by comparing proceeds with carrying amount.

i. Impairment of non-financial assets

Non-financial assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Such impairment losses are recognised in the income statement within 'Other expense' and are recognised against the carrying amount of the impaired asset on the statement of financial position. Non-financial asset, that have suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

j. Cash and cash equivalents

Cash and cash equivalents comprise cash and demand deposits with banks, along with highly liquid investments, with original maturities of three months or less, that are readily convertible to known amounts of cash and subject to insignificant risk of change in value.

k. Grants

Grants received in respect of capital expenditure are treated as deferred income and released to 'Other income' in the income statement over the expected useful lives of the related asset on a straight line basis.

l. Income tax

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is calculated based on taxable profit for the year. Taxable profit may differ from profit/ (loss) before taxation as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the reporting date. Current tax is charged or credited in the income statement, except when it relates to items charged or credited directly to other comprehensive income or equity, in which case the current tax is also recorded within other comprehensive income or equity respectively.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

l. Income tax (continued)

The carrying amount of deferred tax assets is reviewed at each reporting date and limited to the extent that it is probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to other comprehensive income or equity, in which case the deferred tax is reflected within other comprehensive income or equity, respectively.

Current tax assets are offset against current tax liabilities when there is a legally enforceable right to set off current tax assets against current tax liabilities and the Company intends to settle its current tax assets and current tax liabilities on a net basis or to realise the asset and settle the liability simultaneously. Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and current tax liabilities on a net basis.

m. Operating leases

Rentals payable under operating leases are charged to 'Other expense' in the income statement on a straight line basis over the lease term. Lease incentives are allocated on a straight line basis over the lease term as a reduction to rental expense.

n. Provisions

Provisions are recognised when the Company has a present obligation as a result of a past event, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and when a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the year end date, taking into account the risks and uncertainties surrounding the obligation.

o. Offsetting of financial assets and financial liabilities

Where there is a currently legally enforceable right to set off the recognised amounts and an intention to either settle on a net basis or to realise the asset and the liability simultaneously, financial assets and financial liabilities are offset and the net amount is presented on the statement of financial position. In the absence of such conditions, financial assets and financial liabilities are presented on a gross basis.

4. NET GAINS ON AVAILABLE-FOR-SALE FINANCIAL ASSETS

	2017 $'000	2016 $'000
Dividend income	-	2,035
Net fair value gains reclassified from the available-for-sale reserve on disposal of asset	10,803	-
	10,803	2,035

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

5. NET GAINS ON INVESTMENTS IN SUBSIDIARIES

	2017 $'000	2016 $'000
Income from investments in subsidiaries	348,625	157,625

6. INTEREST INCOME AND INTEREST EXPENSE

'Interest income' represent total interest income for financial assets that are not carried at fair value. No other gains or losses have been recognised in respect of loans and receivables other than as disclosed as 'Interest income', and foreign exchange differences disclosed in 'Other income' (note 7) and 'Other expense' (note 8).

'Interest expense' represents total interest expense for financial liabilities that are not carried at fair value and additionally includes the unwind of the discount rate on provisions (note 16). No other gains or losses have been recognised in respect of financial liabilities at amortised cost other than as disclosed as 'Interest expense', and foreign exchange differences disclosed in 'Other expense' (note 8) and 'Other income' (note 7).

7. OTHER INCOME

	2017 $'000	2016 $'000
Government grants	494	533
Net foreign exchange gains	-	164
	494	697

Income from government grants relates to a Regional Selective Assistance grant awarded towards capital expenditure. The related expense is recognised in 'Other expense'.

8. OTHER EXPENSE

	2017 $'000	2016 $'000
Property service costs	78,992	125,831
Operating lease rentals	74,213	68,020
Depreciation on property, plant and equipment (note 13)	58,251	53,613
Loss on disposal of property, plant and equipment	108	-
Net foreign exchange losses	1,416	-
Auditor's remuneration:		
Fees payable to the Company's auditor for the audit of the Company's annual financial statements	71	43
	213,051	247,507

8. OTHER EXPENSE (CONTINUED)

A description of the Company's significant leasing arrangements is presented at note 18 Commitments and contingencies.

The Company employed no staff during the year (2016: nil).

The amount of remuneration received by Directors in respect of their qualifying services to the Company is disclosed in the Related Party Disclosures note (note 23).

9. INCOME TAX EXPENSE

Analysis of expense/(benefit) in the year

	2017 $'000	2016 $'000
Current tax expense		
UK corporation tax at 19.25% (2016: 20%)		
- Current year	30,884	28,751
- Prior year	550	-
Foreign tax		
- Current year	306	305
Total current tax	31,740	29,056
Deferred tax benefit		
Origination and reversal of temporary differences	(2,530)	(57)
Adjustment in respect of prior years	(47)	(22)
Effect of changes in tax rates	(70)	(414)
Total deferred tax	(2,647)	(493)
Income tax expense	29,093	28,563

Finance (No.2) Act 2015 enacted a reduction in the UK corporation tax rate to 19% with effect from 1 April 2017. Finance Act 2016 enacted a further reduction in the UK corporation tax rate to 17% with effect from 1 April 2020. These reductions in the tax rate may impact the current tax charge in future periods.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

9. INCOME TAX EXPENSE (CONTINUED)

Reconciliation of effective tax rate

The current year income tax expense is lower (2016: lower) than that resulting from applying the average standard rate of corporation tax in the UK for the year of 19.25% (2016: 20%). The main differences are explained below:

	2017 $'000	2016 $'000
Profit before taxation	360,182	162,285
Income tax using the average standard rate of corporation tax in the UK of 19.25% (2016: 20%)	69,335	32,457
Impact on tax of:		
Tax under/(over) provided in prior years	503	(22)
Expenses not deductible for tax purposes	4,808	3,386
Group relief received for no cash consideration	-	(3,647)
Effect of changes in tax rate	(70)	(414)
Effect of taxes in foreign jurisdictions	306	305
Currency translation on tax	565	(2,773)
Tax exempt dividends	(44,275)	(407)
Non-taxable gain on disposal of fixed asset investments	(2,079)	-
Other permanent differences	-	(322)
Total income tax expense in the income statement	29,093	28,563

10. OTHER RECEIVABLES

	2017 $'000	2016 $'000
Amounts due from other Morgan Stanley Group undertakings	363,646	1,532,068
Other amounts receivable	-	131
	363,646	1,532,199

11. AVAILABLE-FOR-SALE FINANCIAL ASSETS

Financial assets classified as available-for-sale are summarised as follows:

	2017 $'000	2016 $'000
Corporate equities	-	39,275

11. AVAILABLE-FOR-SALE FINANCIAL ASSETS (CONTINUED)

Movement in available-for-sale financial assets

	2017 $'000	2016 $'000
Fair value		
At 1 January	39,275	40,480
Changes in fair value recognised in the available-for-sale reserve	550	(1,205)
Disposal	(39,825)	-
At 31 December	-	39,275

All investments classified as available-for-sale financial assets were unlisted.

On 9 June 2017, the Company disposed of its available-for-sale investment to Morgan Stanley & Co. International plc for consideration of €35,413,000 ($39,825,000), resulting in the cumulative gain of $10,803,000 in the available-for-sale reserve being realised and therefore reclassified to the income statement.

12. INVESTMENTS IN SUBSIDIARIES AND OTHER CONTROLLED ENTITIES

	Subsidiary undertakings $'000
Cost	
At 1 January 2017	16,333,880
Disposal	(16,333,802)
At 31 December 2017	78
Carrying amounts	
At 31 December 2016	16,333,880
At 31 December 2017	78

On 12 June 2017, the Company disposed of 400,000,000 ordinary $1 shares in Morgan Stanley Investments (UK) for consideration of $400,000,000 from Morgan Stanley International Limited, and as part of a dividend in specie of $14,633,802,000 to Morgan Stanley International Limited, transferred its remaining equity interest in Morgan Stanley Investments (UK), as well as its equity interest in Morgan Stanley UK Limited.

On 8 June 2017, the Company transferred its $1,300,000,000 holding of Additional Tier 1 capital in Morgan Stanley & Co. International plc to Morgan Stanley International Limited, as consideration for the cancellation of the Company's issued Additional Tier 1 capital.

Details of all subsidiary undertakings (including indirect subsidiaries) of the Company at 31 December 2017 and 31 December 2016 are provided in the Appendix to the financial statements (see pages 34 to 36).

13. PROPERTY, PLANT AND EQUIPMENT

	Leasehold improvement $'000	Fixtures, fittings and equipment $'000	Total $'000
Cost			
At 1 January 2017	791,827	103,951	895,778
Additions	26,024	-	26,024
Disposals	(196)	-	(196)
At 31 December 2017	817,655	103,951	921,606
Depreciation			
At 1 January 2017	453,430	103,756	557,186
Charge for the year	58,101	150	58,251
Disposals	(88)	-	(88)
At 31 December 2017	511,443	103,906	615,349
Carrying amount			
At 31 December 2017	306,212	45	306,257

14. SUBORDINATED LOANS

The amounts subject to subordinated loan agreements are wholly repayable as shown below:

Counterparty	Repayment date	Interest rate	2017 Interest $'000	2017 Balance $'000	2016 Interest $'000	2016 Balance $'000
Morgan Stanley International Limited	21 December 2025	SONIA[1] + 212.1bps	3,191	-	8,406	308,563
Morgan Stanley International Limited	21 December 2025	FED Fund Rate + 208.6bps	52,870	-	1,285	51,000
			56,061	-	9,691	359,563

1 The Sterling Overnight Index Average ("SONIA")

On 8 February 2017, $5,000,000,000 was drawn by the Company under its subordinated loan agreement with Morgan Stanley International Limited and on the same day the Company lent $5,000,000,000 to Morgan Stanley Investments (UK) under its subordinated loan agreement with that company.

The subordinated loan agreement could be amended at any time by mutual agreement between the Company and the Lender but subject to prior notification and non-objection of the Prudential Regulation Authority ("PRA").

14. SUBORDINATED LOANS (CONTINUED)

The Company has not defaulted on principal, interest or made any other breaches with respect to its subordinated loans during the year.

On 8 June 2017, the Company cancelled its subordinated loan liability to Morgan Stanley International Limited as consideration for transferring its receivable from Morgan Stanley Investments (UK), with equivalent terms, to Morgan Stanley International Limited.

15. OTHER PAYABLES

	2017 $'000	2016 $'000
Amounts due to other Morgan Stanley Group undertakings	482,032	1,623,185

16. PROVISIONS

	Onerous lease contracts $'000	Lease reinstatement provisions $'000	Total $'000
At 1 January 2017	43,236	42,181	85,417
Additional provisions	17,655	9,009	26,664
Provisions utilised	(6,188)	-	(6,188)
Effect of unwinding discount rate	2,487	2,032	4,519
Foreign exchange revaluation	4,140	4,309	8,449
At 31 December 2017	61,330	57,531	118,861

The onerous lease contracts represent the net present value of expected future costs of excess office space (net of expected sublease income) and lease reinstatement provisions represent the net present value of expected future costs of reinstating leasehold improvements at the end of the lease term. Lease reinstatement provisions are released when the reinstatement obligations have been fulfilled. The related asset for lease reinstatement provisions is included in 'Leasehold improvements' within 'Property, plant and equipment' (note 13).

17. DEFERRED TAX LIABILITIES

Deferred taxes are calculated on all temporary differences under the liability method. The movement in the deferred tax account is as follows:

	2017 Deferred tax asset/(liability) $'000	2016 Deferred tax asset/(liability) $'000
At 1 January	(10,222)	(10,715)
Amount recognised in the income statement		
Current year timing differences	2,530	57
Adjustments in respect of prior years	47	22
Impact of change in UK corporation tax rate	70	414
At 31 December	(7,575)	(10,222)

The deferred tax included in the statement of financial position and changes recorded in 'Income tax expense' are as follows:

	Deferred tax liability 2017 $'000	Income statement 2017 $'000	Deferred tax liability 2016 $'000	Income statement 2016 $'000
Accelerated capital allowances	(7,575)	2,647	(10,222)	493

Finance (No.2) Act 2015 enacted a reduction in the UK corporation tax rate to 19% with effect from 1 April 2017. Finance Act 2016 enacted a further reduction in the UK corporation tax rate to 17% with effect from 1 April 2020. This overall rate reduction to 17% has had an impact on the deferred tax balance as indicated above.

18. COMMITMENTS AND CONTINGENCIES

Leases

The Company has entered into non-cancellable commercial leases on premises and equipment. These leases have an average life of between fifteen and thirty five years. The leases on the premises include renewal options and escalation clauses in line with general rental market conditions and rent adjustments based on price indices. The lease agreements do not contain contingent rent payment clauses or purchase options and they do not impose any restrictions on the Company's ability to pay dividends, engage in debt financing transactions or enter into further lease agreements.

During the year ended 31 December 2017 the Company's subtenant vacated the Company's premises and the Company has not entered into any further sublease arrangements.

18. COMMITMENTS AND CONTINGENCIES (CONTINUED)

	2017 $'000	2016 $'000
Lease payments under non-cancellable operating leases recognised as an expense in the year:		
- Minimum lease payments	74,213	68,020

Future minimum lease payments under non-cancellable operating leases at 31 December are due as follows:

	2017 $'000	2016 $'000
Within one year	68,044	84,491
In the second to fifth years inclusive	263,778	246,930
After five years	849,447	835,092
	1,181,269	1,166,513

Additionally the Company guaranteed certain obligations of another Morgan Stanley Group undertaking under a lease agreement with an unrelated third party.

19. EQUITY

	2017 Number	2017 $'000	2016 Number	2016 $'000
Allotted and fully paid				
Ordinary shares of $1 each	10,000,000	10,000	4,090,356,207	4,090,356
Class A preference shares of $1 each*	-	-	200,000,000	200,000
Class B preference shares of $1 each**	-	-	683,439,836	683,440
Class C preference shares of $1 each**	-	-	865,000,000	865,000
	10,000,000	10,000	5,838,796,043	5,838,796
Other equity instruments				
Additional Tier 1 capital	-	-	-	1,300,000
	10,000,000	10,000	5,838,796,043	7,138,796

*Class A preference shares are non-cumulative non-voting

**Class B and C preference shares are non-cumulative voting

On 26 May 2017 the Company reduced and cancelled its 200,000,000 Class A preference shares of $1 each, for par consideration.

On 8 June 2017, the Company redesignated 683,439,836 Class B non-cumulative voting preference shares of $1 each and 865,000,000 Class C non-cumulative voting preference shares of $1 each for 1,548,439,836 ordinary shares of $1 each.

19. EQUITY (CONTINUED)

On 8 June 2017, the Company issued 6,314,671,635 ordinary shares of $1 each as a bonus issue to Morgan Stanley International Limited, in exchange for the Company's existing 'Capital contribution reserve' of $6,064,670,000 and 'Capital redemption reserve' of $250,000,000. On 9 June 2017, the Company consolidated 11,953,467,678 ordinary shares of $1 each into 10,000,000 ordinary shares of $1,195.346768 each and then performed a capital reduction to reduce the nominal value of each ordinary share to $1 each. The Company's resultant share capital consists of 10,000,000 ordinary shares of $1 each.

Equity shares

Ordinary shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled, on a show of hands, to one vote and, on a poll, one vote per share at meetings of the shareholders of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

Preference shares

The holders of Class A non-cumulative non-voting preference shares were entitled to receive a one year US$ London Interbank Offered Rate ("LIBOR") plus 4.03%-based divided as defined in the Company's Articles of Association. The preference shares ranked ahead of the ordinary shares and pari passu with the holders of B and C preference shares in the event of liquidation.

The holders of Class B non-cumulative voting preference shares were entitled to receive a fixed rate dividend of 7.5% per annum in respect of the paid up portion of each B preference share held. The shares as a class carried an aggregate of 10% of the voting rights of the Company. The preference shares ranked ahead of the ordinary shares and pari passu with the holders of A and C preference shares in the event of liquidation.

The holders of Class C non-cumulative voting preference shares were entitled to receive a one year US$ LIBOR plus 5%-based divided as defined in the Company's Articles of Association. The shares as a class carried an aggregate of 10% of the voting rights of the Company. The preference shares ranked ahead of the ordinary shares and pari passu with the holders of A and B preference shares in the event of liquidation.

Additional Tier 1 capital

The Additional Tier 1 capital instruments ("the Instruments") included a trigger mechanism whereby if the Common Equity Tier 1 capital ratio of the Company fell below a pre-determined level, the Company would write-down the outstanding principal amount of the Instruments, together with any accrued interest coupon. In this situation, Morgan Stanley International Limited, the purchaser of the Instruments, would have no further rights against the Company in respect of the Instruments. The Instruments had no defined maturity, were callable at the Company's discretion after five years from their date of issuance and were subordinated to senior creditors and subordinated loan creditors of the Company. The Instruments were not entitled to any participation in the residual net assets of the Company. Coupons on the Instruments were non-cumulative and payable at a fixed rate of 9% per annum. Payment of the coupon was wholly at the discretion of the Company.

On 8 June 2017 the Company transferred its $1,300,000,000 holding of Additional Tier 1 capital in Morgan Stanley & Co. International plc to Morgan Stanley International Limited as consideration for the cancellation of the Company's issued Additional Tier 1 capital.

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

19. EQUITY (CONTINUED)

Reserves

Share premium

On 9 June 2017, the Company's shareholder reduced the Company's existing share premium account of $304,218,000 to create distributable reserves.

Available-for-sale reserve

On 9 June 2017, the Company disposed of its available-for-sale investment to Morgan Stanley & Co. International plc for consideration of €35,413,000 ($39,825,000), resulting in the cumulative gain of $10,803,000 in the available-for-sale reserve being realised and therefore reclassified to the income statement.

Capital contribution and capital redemption reserve

On 8 June 2017, the Company issued 6,314,671,635 ordinary shares of $1 each to Morgan Stanley International Limited in exchange for the Company's exiting 'Capital contribution reserve' of $6,064,670,000 and 'Capital redemption reserve' of $250,000,000.

20. DIVIDENDS

The following amounts represent the dividends paid in the current and prior year:

	2017		2016	
	Per share	**Total**	**Per share**	**Total**
	$	**$'000**	**$**	**$'000**
Dividends on Class A preference shares	0.0197	3,940	0.10	20,027
Dividends on Class B preference shares	0.102292	69,910	-	-
Dividends on Class C preference shares	0.085947	74,344	-	-
Coupon payment on Additional Tier 1 securities	-	95,228	-	128,873
Dividend in specie	-	14,633,802	-	-
		14,877,224		148,900

On 3 May 2017, the Directors approved a coupon payment on the Company's Additional Tier 1 capital instruments of $118,625,000 (2016: $157,625,000) out of reserves available at 31 December 2016. The coupon was paid on 31 May 2017 and has a related tax benefit of $23,397,000 (2016: $28,752,000). The payment was reflected in the Company's financial statements for the year ended 31 December 2017 as it became due during 2017.

21. EXPECTED MATURITY OF ASSETS AND LIABILITIES

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered, realised or settled.

At 31 December 2017	Less than or equal to twelve months $'000	More than twelve months $'000	Total $'000
ASSETS			
Loans and receivables:			
Cash and short-term deposits	51,242	-	51,242
Other receivables	315,785	47,861	363,646
	367,027	47,861	414,888
Current tax assets	980	-	980
Prepayments and accrued income	23,446	-	23,446
Investments in subsidiaries	-	78	78
Property, plant and equipment	-	306,257	306,257
	391,453	354,196	745,649
LIABILITIES			
Financial liabilities at amortised cost:			
Other payables	764	481,268	482,032
	764	481,268	482,032
Provisions	-	118,861	118,861
Current tax liabilities	8,037	-	8,037
Deferred tax liabilities	-	7,575	7,575
Accruals and deferred income	4,313	76,458	80,771
	13,114	684,162	697,276

21. EXPECTED MATURITY OF ASSETS AND LIABILITIES (CONTINUED)

At 31 December 2016	Less than or equal to twelve months $'000	More than twelve months $'000	Total $'000
ASSETS			
Loans and receivables:			
Cash and short-term deposits	665	-	665
Other receivables	1,532,199	-	1,532,199
	1,532,864	-	1,532,864
Available-for-sale financial assets	39,275	-	39,275
Current tax assets	706	-	706
Prepayments and accrued income	29,912	-	29,912
Investments in subsidiaries	16,333,880	-	16,333,880
Property, plant and equipment	-	338,592	338,592
	17,936,637	338,592	18,275,229
LIABILITIES			
Financial liabilities at amortised cost:			
Subordinated loans	359,563	-	359,563
Other payables	970,885	652,300	1,623,185
	1,330,448	652,300	1,982,748
Provisions	-	85,417	85,417
Deferred tax liabilities	-	10,222	10,222
Accruals and deferred income	1,623	90,458	92,081
	1,332,071	838,397	2,170,468

22. SEGMENT REPORTING

The principal activity of the Company is to provide property services to other Morgan Stanley Group undertakings in the UK.

23. RELATED PARTY DISCLOSURES

Parent and subsidiary relationships

Parent and ultimate controlling entities

The parent and ultimate controlling entities are disclosed in note 1 to the financial statements.

Subsidiary relationships

The Company's subsidiary undertakings (including indirect subsidiaries) at 31 December 2017 and 31 December 2016 are provided in the Appendix to the financial statements (see pages 34 to 36).

23. RELATED PARTY DISCLOSURES (CONTINUED)

Directors' remuneration

The Company paid no remuneration to its Directors during the current or prior year. The charges in respect of Directors' qualifying services to the Company have been borne by another Morgan Stanley Group undertaking. The amount of remuneration received by Directors in respect of their qualifying services to the Company is disclosed below:

	2017 $'000	2016 $'000
Total remuneration of all Directors:		
Aggregate remuneration	727	1,607
Long term incentive schemes	36	68
Company contributions to pension schemes	20	49
	783	1,724
Disclosures in respect of the highest paid Director:		
Aggregate remuneration	259	610
Long term incentive schemes	13	60
Company contributions to pension schemes	8	21

Directors' remuneration has been calculated as the sum of cash, bonuses, and benefits in kind.

All Directors who are employees of the Morgan Stanley Group are eligible for shares and share options of the parent company, Morgan Stanley, awarded under the Morgan Stanley Group's equity-based long term incentive schemes. In accordance with Schedule 5 paragraph 1(3)(a) of The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, the above disclosures include neither the value of shares awarded, nor the gains made on exercise of share options. During the year under these incentive schemes, no Directors exercised share options, including the highest paid Director (2016: none) and all three Directors received restricted stock unit awards in respect of qualifying services, including the highest paid Director (2016: three).

The value of assets (other than shares or share options) awarded under other long term incentive schemes has been included in the above disclosures when the awards vest, which is generally within three years from the date of the award.

The Morgan Stanley Group operates a defined contribution pension scheme, the Morgan Stanley UK Group Pension Plan. There are two Directors to whom retirement benefits are accruing under this defined contribution scheme (2016: two).

In addition, one Director has benefits accruing under the Alternative Retirement Plan, a defined benefit scheme, operated by Morgan Stanley UK Limited (2016: one).

NOTES TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

23. RELATED PARTY DISCLOSURES (CONTINUED)

Directors' remuneration (continued)

The Company has provided the following advances and credit to its Directors during the year (amounts disclosed are gross loan values):

		Amount of advance/ credit		Total amount repaid	
	Interest rate	2017 $'000	2016 $'000	2017 $'000	2016 $'000
Season ticket loan	0%	5	5	5	5

APPENDIX TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

List of subsidiaries, including indirect subsidiaries, as at 31 December 2017 and 31 December 2016:

Name of company	Address of undertaking's registered office	Proportion of shares held by the Company (1)(2) 2017	2016	Nature of business
Morgan Stanley Services (UK) Limited	25 Cabot Square, Canary Wharf. London. E14 4QA	100%	100%	Financial services
Morgan Stanley UK Limited	25 Cabot Square. Canary Wharf. London. E14 4QA	0%	100%	Service company
Morgan Stanley Wertpapiere GmbH	Junghofstrasse 13-15, 60311. Frankfurt am Main, Germany	100%	100%	Financial services
Morgan Stanley Amalthea UK Limited	20 Bank Street, Canary Wharf, London. E14 4AD	100%	100%	Financial services
Morgan Stanley Pension Trustee Limited*	25 Cabot Square. Canary Wharf, London. E14 4QA	0%	100%	Trustee services
Morgan Stanley Investments (UK)	20 Bank Street. Canary Wharf. London, E14 4AD	0%	100%	Holding company
Morgan Stanley & Co. International plc[2a]	25 Cabot Square. Canary Wharf. London, E14 4QA	0%	100%	Financial services
Morgan Stanley & Co. Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Financial services
Morgan Stanley Bank International Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Financial services
Morgan Stanley Investment Management Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Investment management
Morgan Stanley Securities Limited*	25 Cabot Square, Canary Wharf. London, E14 4QA	0%	100%	Financial services
East Sussex Financing Limited*	13 Castle Street. St Helier, Jersey	0%	100%	Holding company
Cottenden Financing Unlimited*[2b]	13 Castle Street. St Helier, Jersey	0%	100%	Financial services
Morgan Stanley Bank International (China) Limited*[2c]	Rooms 2801-2807 & 2816, Yuecai Building, No. 188 Jinghshan Road. Jida, Zhuhai. Guangdong Province, China	0%	100%	Financial services
Morgan Stanley Investment Management (ACD) Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Investment management
Morgan Stanley (France) S.A.*	61 Rue De Monceau, 75008, Paris, France	0%	100%	Financial services
Morgan Stanley Taiwan Limited*	14th & 22nd Floors, Taipei Metro, 207 Tun Hwa South Road, Sec. 2. Taipei, 106, Taiwan	0%	100%	Financial services
Morgan Stanley Strategic Investments Limited*	20 Bank Street, Canary Wharf. London, E14 4AD	0%	100%	Financial services
Morgan Stanley Turnberry Limited*	20 Bank Street. Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Mallard Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Montgomerie Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Northcote Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Silvermere Limited*	20 Bank Street, Canary Wharf. London, E14 4AD	0%	100%	Holding company
Morgan Stanley Equity Trading (DIFC) Limited*	Level 7. The Gate, Dubai International Financial Centre. Sheik Zayed Road, PO Box 506501, Dubai. United Arab Emirates	n/a	100%	Financial services
Shavano Cooperatieve U.A.* [2d]	20 Bank Street, Canary Wharf, London. E14 4AD	0%	100%	Financial services

APPENDIX TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

Name of company	Address of undertaking's registered office	Proportion of shares held by the Company [1][2] 2017	2016	Nature of business
Morgan Stanley Humboldt Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Equity Finance (Denmark) ApS*	Bech-Bruun Dragsted, Langelinie Alle 35, 2100, Kobenhavn, Denmark	0%	100%	Financial services
Morgan Stanley Rivelino Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Dolor Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Holding company
Morgan Stanley Tostao Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Financial services
Morgan Stanley Equity Financing Services (Sweden) AB*	Hovslagargatan 5 A, 111 48, Stockholm, Sweden	0%	100%	Financial services
Morgan Stanley Havel GmbH*	Junghofstrasse 13-15, 60311, Frankfurt am Main, Germany	0%	100%	Holding company
Morgan Stanley Cooper Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Montrose Investments Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Langtree Investments B.V.*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Equity Investments (UK) Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Financial services
Clearcreek, S.L.U.*	Calle Aribau 171, 8036, Barcelona, Spain	0%	100%	Financial services
Cabot 38 Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Maple Investments Limited*	Baker Tilly, 25 Farringdon Street, London, EC4A 4AD	0%	100%	Financial services
Morgan Stanley Millbrae Investments B.V.* [2c]	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Morgan Stanley Derivative Products (Netherlands) B.V.*	Luna Arena, Herikerbergweg 238, 1101 CM, Amsterdam, Netherlands	0%	100%	Financial services
Morgan Stanley Longcross Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Derivative Products Spain S.L.*	Serrano 55, 28006, Madrid, Spain	0%	100%	Financial services
Morgan Stanley Equity Investments (Luxembourg) Unlimited Company*	Custom House, Plaza Block 6, , International Financial Services Centre, Dublin, DUBLIN 1, Ireland	0%	99%	Holding company
Morgan Stanley Langton Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Holding company
Morgan Stanley Bowline Limited*	Baker Tilly, 25 Farringdon Street, London, EC4A 4AD	0%	100%	Holding company
Morgan Stanley Equity Finance (Malta) Limited*	SmartCity Malta, SCM 01 TMF Group (Malta) 401, Ricasoli, Kalkara SCM 1001, Malta	0%	100%	Financial services
Morgan Stanley Equity Derivative Services (Luxembourg) S.à r.l.*	20, rue de la Poste, L-2346, Luxembourg	0%	100%	Financial services
Morgan Stanley Equity Financing Limited*	20 Bank Street, Canary Wharf, London, E14 4AD	0%	100%	Financial services
Drake II Investments Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Financial services
Morgan Stanley Grund S.à r.l.*	46A, Avenue J.F. Kennedy, L-1855, Luxembourg	0%	100%	Financial services
Morgan Stanley Kochi Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Holding company
Morgan Stanley Derivative Products (Portugal), Unipessoal LDA*	Rua Duque de Palmela, No. 23, 1250-097, Lisbon, Portugal	0%	100%	Financial services

APPENDIX TO THE FINANCIAL STATEMENTS
Year ended 31 December 2017

Name of company	Address of undertaking's registered office	Proportion of shares held by the Company [1][2] 2017	2016	Nature of business
Morgan Stanley Corporate Holdings (Luxembourg) Unlimited Company*	Custom House, Plaza Block 6, International Financial Services Centre, Dublin, DUBLIN 1, Ireland	0%	100%	Holding company
Morgan Stanley Heythorp Investments Unlimited Company*	Custom House, Plaza Block 6, International Financial Services Centre, Dublin, DUBLIN 1, Ireland	0%	100%	Holding company
Morgan Stanley Equity Holding (Netherlands) B.V.*	Luna Arena, Herikerbergweg 238, 1101 CM, Amsterdam, Netherlands	0%	100%	Financial services
Morgan Stanley Waterloo Limited*	Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands	0%	100%	Financial services
Morstan Nominees Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Nominee company
Global Equity High Yield Fund B.V.*	Weena 210-212, 3012NJ, Rotterdam, Netherlands	0%	100%	Financial services
Morgan Stanley Client Securities Nominees Limited*	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Nominee company
Morgan Stanley UK Group Partners Excepted Life Assurance Scheme *	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Employee benefit scheme
Morgan Stanley UK Healthcare Trust *	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Employee benefit trust
Morgan Stanley UK Group Excepted Life Assurance Scheme *	25 Cabot Square, Canary Wharf, London, E14 4QA	0%	100%	Employee benefit trust
Morgan Stanley France Holdings I S.A.S*	61 Rue De Monceau, 75008, Paris, France	0%	100%	Holding company
Morgan Stanley France Holdings II S.A.S.*	61 Rue De Monceau, 75008, Paris, France	0%	100%	Holding company

Notes:

(1) The proportion of voting rights held by the Company is the same as the proportion of shares held by the Company unless otherwise stated.

(2) All shares held in each Company are ordinary shares with the exception of:
a) Morgan Stanley & Co. International plc where Additional Tier 1 capital was held
b) Cottenden Financing Unlimited where unlimited ordinary shares were held
c) Morgan Stanley Bank International (China) Limited where registered capital was held
d) Shavano Cooperative U.A. where €1 C membership shares were held
e) Morgan Stanley Millbrae Investments B.V. where ordinary and preference shares were held.

*Denotes shareholdings attributed to the Company which are not all held directly by the Company.