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MORGAN STANLEY TOSTAO LIMITED

Report and financial statements

31 December 2012



MORGAN STANLEY TOSTAO LIMITED

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MORGAN STANLEY TOSTAO LIMITED

DIRECTORS' REPORT

The Directors present their report and financial statements (which comprise the profit and loss account, the balance sheet, and the related notes, 1 to 14) for Morgan Stanley Tostao Limited (the "Company") for the year ended 31 December 2012

RESULTS AND DIVIDENDS

The profit for the year, after tax, was A\$97,573,000 (2011 A\$142,301,000 profit after tax)

During the year dividends of A\$33,453,000 were paid (2011 A\$142,905,000)

PRINCIPAL ACTIVITY

The Company is an exempt company incorporated under the laws of the Cayman Islands

The principal activity of the Company is to enter into financing transactions and investments

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 management and control of the Company is in the United Kingdom, and the entity is liable to UK Corporation Tax on its taxable profits

There have not been any significant changes in the Company's principal activity in the year under review and no significant change in the Company's principal activity is expected

BUSINESS REVIEW

During 2012, global market and economic conditions have remained challenging with continuing concerns about the European sovereign debt crisis, lack of robust economic recovery in the United States ("US") and other developed markets and slowing economic growth in emerging markets. These on-going conditions present difficulties and uncertainty for the business outlook that may adversely impact the financial performance of the Company in the future

The profit and loss account for the year is set out on page 6. The Company's profit for the year has reduced from A\$142,301,000 in the prior year to A\$97,573,000 in the current year. This is driven by a reduction in the Australian Dollar floating rate of interest, which has reduced from an average of 6.56% in 2011 to 5.98% in 2012. In addition, the Company received no group relief in the current year compared to A\$142,301,000 in the prior year resulting in an increase in the tax expense from nil to A\$32,313,000.

The balance sheet for the Company is as set out on page 7. The Company's net assets at the end of the year were A\$2,239,192,000 in comparison to A\$2,175,072,000 in the prior year. The increase is due mainly to interest accrued and unpaid of A\$130,813,000, which has been offset by dividends paid of A\$33,453,000 and corporation tax payable for the year of A\$32,313,000.

The performance of the Company is included in the results of the Morgan Stanley Group which are disclosed in the Morgan Stanley Group's Annual Report on Form 10-K to the United States Securities and Exchange Commission. The Morgan Stanley Group manages its key performance indicators on a global basis but in consideration of individual legal entities. For this reason, 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.

The risk management section below sets out the Company's and the Morgan Stanley Group's policies for the management of liquidity and cash flow risk and other significant business risks.

MORGAN STANLEY TOSTAO LIMITED

DIRECTORS' REPORT

Risk management

Risk is an inherent part of the Company's business activity and is managed within the context of the broader Morgan Stanley Group's business activities. The Morgan Stanley Group seeks to identify, assess, monitor and manage each of the various types of risk involved in its activities on a global basis, in accordance with defined policies and procedures and in consideration of the individual legal entities.

Morgan Stanley has taken transformative steps during this extremely difficult environment, including the de-risking of the balance sheet and those related to capital and liquidity outlined below.

Credit risk

Credit risk refers to the risk of loss arising from borrower or counterparty default when a borrower, counterparty or obligor does not meet its obligations.

The Morgan Stanley Group manages credit risk exposure on a global basis as well as giving consideration to each individual legal entity. It does this by ensuring transparency of material credit risks, ensuring compliance with established limits, approving material extensions of credit, escalating risk concentrations to appropriate senior management and mitigating credit risk through the use of collateral and other arrangements.

Liquidity and capital resources

Liquidity and funding risk refers to the risk that the Company will be unable to meet its funding obligations in a timely manner. Liquidity risk stems from the potential risk that the Company will be unable to obtain necessary funding through borrowing money at favourable interest rates or maturity terms, or selling assets in a timely manner and at a reasonable price.

The Morgan Stanley Group's senior management establishes the overall liquidity and funding policies of the Morgan Stanley Group and the liquidity risk management policies and procedures conducted within the Company are consistent with those of the Morgan Stanley Group. The Morgan Stanley Group's liquidity and funding risk management policies are designed to mitigate the potential risk that entities within the Morgan Stanley Group, including the Company, may be unable to access adequate financing to service their financial liabilities when they become payable without material, adverse franchise or business impact. The key objective of the liquidity and funding risk management framework is to support the successful execution of both the Company's and the Morgan Stanley Group's business strategies while ensuring ongoing and sufficient liquidity through the business cycle and during periods of stressed market conditions.

Morgan Stanley continues to actively manage its capital and liquidity position to ensure adequate resources are available to support the activities of the Morgan Stanley Group, including the Company, to enable the Morgan Stanley Group to withstand market stresses, and to meet regulatory stress testing requirements proposed by regulators globally. The Morgan Stanley Group regularly performs stress testing to ensure that the Morgan Stanley Group, including the Company, has sufficient resources at its disposal to absorb losses associated with certain stressed scenarios.

On 21 June 2012, Moody's Investor Services announced the conclusion of an industry-wide reassessment and revised ratings for 15 global capital markets banks. The Morgan Stanley Group's long- and short-term debt ratings were lowered two notches to Baa1/P-2 from A2/P-1, and a negative outlook was assigned.

While certain aspects of a credit ratings downgrade are quantifiable pursuant to contractual provisions, the impact it will have on the Morgan Stanley Group's business and results of operation in future periods is inherently uncertain and will depend on a number of inter-related factors, including among others, the magnitude of the downgrade, individual client behaviour and future mitigating actions the Morgan Stanley Group may take.

MORGAN STANLEY TOSTAO LIMITED

DIRECTORS' REPORT

Operational risk

Operational risk refers to the risk of financial or other loss, or potential damage to the Company's or the Morgan Stanley Group's reputation, resulting from inadequate or failed internal processes, people, resources and systems or from other external events (e.g. fraud, legal and compliance risks, damage to physical assets, etc.) Legal, regulatory and compliance risk is included in the scope of operational risk and is discussed below under "Legal, regulatory and compliance risk"

The Morgan Stanley Group has established an operational risk management process that operates on a global and regional basis to identify, measure, monitor and control risk. Effective operational risk management is essential to reducing the impact of operational risk incidents and mitigating legal, regulatory, and reputational risks.

Legal, regulatory and compliance risk

Legal risk includes the risk of exposure to fines, penalties, judgements, damages and/or settlements in connection with regulatory or legal actions as a result of non-compliance with applicable legal or regulatory requirements and standards or litigation. Legal risk also includes contractual and commercial risk such as the risk that a counterparty's performance obligations will be unenforceable. The Morgan Stanley Group is generally subject to extensive regulation in the different jurisdictions in which it conducts its business. In the current environment of rapid and possibly transformational regulatory change, the Morgan Stanley Group also views regulatory change as a component of legal risk.

The Morgan Stanley Group has established procedures based on legal and regulatory requirements on a worldwide basis that are designed to foster compliance with applicable statutory and regulatory requirements. The Morgan Stanley Group, principally through the Legal and Compliance Division, also has established procedures that are designed to require that the Morgan Stanley Group's policies relating to business conduct, ethics and practices are followed globally. In connection with its businesses, the Morgan Stanley Group has and continuously develops various procedures addressing issues such as regulatory capital requirements, sales and trading practices, new products, information barriers, potential conflicts of interest, structured transactions, use and safekeeping of customer funds and securities, lending and credit granting, anti-money laundering, privacy and recordkeeping. In addition, the Morgan Stanley Group has established procedures to mitigate the risk that a counterparty's performance obligations will be unenforceable, including consideration of counterparty legal authority and capacity, adequacy of legal documentation, the permissibility of a transaction under applicable law and whether applicable bankruptcy or insolvency laws limit or alter contractual remedies. The legal and regulatory focus on the financial services industry presents a continuing business challenge for the Morgan Stanley Group.

Significant changes in the way that major financial services institutions are regulated are occurring in the United Kingdom ("UK"), Europe, the US and worldwide. The reforms being discussed and, in some cases, already implemented, include several that contemplate comprehensive restructuring of the regulation of the financial services industry. Such measures will likely lead to stricter regulation of financial institutions generally, and heightened prudential requirements for systemically important firms in particular. Such measures could include taxation of financial transactions, liabilities and employee compensation as well as reforms of the over-the-counter ("OTC") derivatives markets, such as mandated exchange trading and clearing, position limits, margin, capital and registration requirements. Changes in tax legislation in the UK and worldwide, such as taxation of financial transactions, liabilities and employees compensation, are also possible.

Many of these reforms, if enacted, may materially affect the Company's and the Morgan Stanley Group's business, financial condition, results of operations and cash flows in the future.

MORGAN STANLEY TOSTAO LIMITED

DIRECTORS' REPORT

DIRECTORS

The following Directors held office throughout the year and to the date of approval of this report (except where otherwise shown)

| | |
|------------|------------------------------|
| P K M Falk | (resigned 14 September 2012) |
| S I Merry | |
| G Adams | (appointed 16 August 2012) |
| | (resigned 27 March 2013) |
| S E Long | (appointed 27 March 2013) |

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

DIRECTORS' INDEMNITY

Qualifying third party indemnity provisions (as defined in section 234 of the Companies Act 2006 of the United Kingdom (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

POST BALANCE SHEET EVENTS

There have been no significant events since the balance sheet date

POLICY AND PRACTICE ON PAYMENT OF CREDITORS

It is the Company's policy that payments to suppliers are made in accordance with those terms and conditions agreed between the Company and its suppliers, providing that all trading terms and conditions have been complied with

As at 31 December 2012 the Company had no trade creditors (2011 nil)

DIRECTORS' RESPONSIBILITIES STATEMENT

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

The Company was incorporated as an exempt company under the laws of the Cayman Islands. The Directors and the shareholders of the Company require the financial statements of the Company to be prepared in accordance with Part 15 of the Companies Act 2006 of the United Kingdom (that would have applied had these been statutory accounts under the Companies Act 2006) and drawn up in Australian Dollars

The Directors are required to prepare such financial statements for each financial year which 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 have been followed, and

MORGAN STANLEY TOSTAO LIMITED

DIRECTORS' REPORT

- 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



Director

S. Merry

26 April 2013

MORGAN STANLEY TOSTAO LIMITED

PROFIT AND LOSS ACCOUNT Year ended 31 December 2012

| | Note | 2012 A\$'000 | 2011 A\$'000 |
|--|------|-----------------|-----------------|
| Interest income | 2 | 130,813 | 142,300 |
| Other income | 3 | - | 1 |
| Other expense | 4 | (927) | - |
| | | <hr/> | <hr/> |
| PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION | | 129,886 | 142,301 |
| Tax on profit on ordinary activities | 7 | (32,313) | - |
| | | <hr/> | <hr/> |
| PROFIT FOR THE FINANCIAL YEAR | 11 | <u>97,573</u> | <u>142,301</u> |

All operations were continuing in the current and prior year

There were no recognised gains or losses during the current or prior year other than those disclosed above
Accordingly no statement of total recognised gains and losses has been prepared

A reconciliation of the movement in shareholders' funds is disclosed in note 11 to the financial statements

The notes on pages 8 to 12 form an integral part of the financial statements

MORGAN STANLEY TOSTAO LIMITED

Registered number MC 142158

BALANCE SHEET

As at 31 December 2012

| | Note | 2012 A\$'000 | 2011 A\$'000 |
|---|------|------------------|------------------|
| CURRENT ASSETS | | | |
| Debtors | 8 | 2,272,698 | 2,175,072 |
| | | <u>2,272,698</u> | <u>2,175,072</u> |
| CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR | | | |
| | 9 | (33,506) | - |
| | | <u>2,239,192</u> | <u>2,175,072</u> |
| NET CURRENT ASSETS | | | |
| | | <u>2,239,192</u> | <u>2,175,072</u> |
| TOTAL ASSETS LESS CURRENT LIABILITIES | | | |
| | | <u>2,239,192</u> | <u>2,175,072</u> |
| NET ASSETS | | | |
| | | <u>2,239,192</u> | <u>2,175,072</u> |
| CAPITAL AND RESERVES | | | |
| Called up share capital | 10 | 10 | 10 |
| Share premium account | 11 | 2,162,882 | 2,162,882 |
| Profit and loss account | 11 | 76,300 | 12,180 |
| | | <u>2,239,192</u> | <u>2,175,072</u> |
| SHAREHOLDERS' FUNDS | | | |
| | | <u>2,239,192</u> | <u>2,175,072</u> |

These financial statements were approved by the Board and authorised for issue on 26 April 2013

Signed on behalf of the Board

Director
S. Merry



The notes on pages 8 to 12 form an integral part of the financial statements

MORGAN STANLEY TOSTAO LIMITED

NOTES TO THE FINANCIAL STATEMENTS Year ended 31 December 2012

1. ACCOUNTING POLICIES

The Company's principal accounting policies are summarised below and have been applied consistently throughout the current and preceding year

a) Basis of preparation

The financial statements are prepared under the historical cost convention and in accordance with applicable United Kingdom company law and accounting standards

The Company is incorporated under the laws of the Cayman Islands, which permits the use of United Kingdom company law and the use of United Kingdom accounting standards in the preparation of financial statements

b) 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 Directors' report on pages 1 to 3

As set out in the Directors' report, retaining sufficient liquidity and capital to withstand market pressures remains central to the Morgan Stanley Group's and the Company's strategy and steps have been taken to strengthen the Morgan Stanley Group capital position and ensure that the Company's capital position is satisfactory

Taking all of these 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

c) Functional currency

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

All currency amounts in the financial statements and Directors' report are rounded to the nearest thousand Australian dollars

d) Foreign currencies

All monetary assets and liabilities denominated in currencies other than Australian dollars are translated into Australian dollars at the rates ruling at the balance sheet date. Transactions in currencies other than Australian dollars are recorded at the rates prevailing at the dates of the transactions. All translation differences are taken through the profit and loss account and are presented in 'Other income' or 'Other expense'

e) Recognition of income and expense

i) Interest income and expense

Interest income and interest expense are recognised on an accruals basis within 'Interest income' and 'Interest expense' in the profit and loss account

MORGAN STANLEY TOSTAO LIMITED

NOTES TO THE FINANCIAL STATEMENTS Year ended 31 December 2012

f) Taxation

UK corporation tax is provided at amounts expected to be paid / recovered using the tax rates and laws that have been enacted or substantively enacted at the balance sheet date

g) Cash flow statement

The Company's ultimate parent undertaking produces consolidated financial statements in which the Company is included and which are publicly available. Accordingly, the Company, which is a wholly owned subsidiary, has elected to avail itself of the exemption provided in Financial Reporting Standard ("FRS") 1 (Revised 1996) *Cash flow statements* and not present a cash flow statement

2. INTEREST INCOME

| | 2012 A\$'000 | 2011 A\$'000 |
|---|-----------------|-----------------|
| Interest income from loans to Morgan Stanley Group undertakings | <u>130,813</u> | <u>142,300</u> |

3. OTHER INCOME

| | 2012 A\$'000 | 2011 A\$'000 |
|----------------------------|-----------------|-----------------|
| Net foreign exchange gains | <u>-</u> | <u>1</u> |

4. OTHER EXPENSE

| | 2012 A\$'000 | 2011 A\$'000 |
|----------------|-----------------|-----------------|
| Other expenses | <u>927</u> | <u>-</u> |

5. STAFF COSTS

The Company employed no staff during the year (2011 nil)

6. DIRECTORS' BENEFITS

The Directors did not receive any remuneration for their qualifying services to the Company during the year (2011 A\$m)

MORGAN STANLEY TOSTAO LIMITED

NOTES TO THE FINANCIAL STATEMENTS Year ended 31 December 2012

7. TAX ON PROFIT ON ORDINARY ACTIVITIES

Analysis of expense/(benefit) in the year

| | 2012 A\$'000 | 2011 A\$'000 |
|---|-----------------|-----------------|
| UK corporation tax at 24.50% (2011: 26.49%) | | |
| - Current year | 32,313 | - |
| Tax on profit on ordinary activities | <u>32,313</u> | <u>-</u> |

Factors affecting the tax expense for the year

The current year UK taxation expense is higher than that resulting from applying the average standard UK corporation tax rate of 24.50% (2011: 26.49%). The main differences are explained below:

| | 2012 A\$'000 | 2011 A\$'000 |
|---|-----------------|-----------------|
| Profit on ordinary activities before tax | <u>129,886</u> | <u>142,301</u> |
| Profit on ordinary activities multiplied by the average standard rate of corporation tax in the UK of 24.50% (2011: 26.49%) | 31,822 | 37,696 |
| Effects of: | | |
| Group relief received for no cash consideration | - | (37,696) |
| Currency translation on tax | 491 | - |
| Current tax expense for the year | <u>32,313</u> | <u>-</u> |

Finance Act 2011 enacted a reduction to the UK corporation tax rate to 25% with effect from April 2012. Finance Act 2012 increased the reduction by a further 1%. The combined reduction in the rate to 24% from April 2012 impacted the current tax charge in 2012.

The Finance Act 2012 also enacted an additional reduction of 1% in the UK corporation tax rate to 23% with effect from April 2013. This further reduction in the tax rate will impact the current tax charge in 2013.

8. DEBTORS

| | 2012 A\$'000 | 2011 A\$'000 |
|--|------------------|------------------|
| Amounts due from Morgan Stanley Group undertakings | <u>2,272,698</u> | <u>2,175,072</u> |

MORGAN STANLEY TOSTAO LIMITED

NOTES TO THE FINANCIAL STATEMENTS

Year ended 31 December 2012

9. CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR

| | 2012 A\$'000 | 2011 A\$'000 |
|---|-----------------|-----------------|
| Amounts owed to Morgan Stanley Group undertakings | 8,744 | - |
| Corporation tax payable | 24,762 | - |
| | <u>33,506</u> | <u>-</u> |

10. CALLED UP SHARE CAPITAL

| Shares classified as equity | 2012 A\$'000 | 2011 A\$'000 |
|-------------------------------------|-----------------|-----------------|
| Allotted and fully paid: | | |
| 10,100 ordinary shares of A\$1 each | <u>10</u> | <u>10</u> |

11. RECONCILIATION OF SHAREHOLDERS' FUNDS AND MOVEMENTS ON RESERVES

| | Called up share capital A\$'000 | Share premium account A\$'000 | Profit and loss account A\$'000 | Total A\$'000 |
|-------------------------------|---------------------------------------|--|---------------------------------------|------------------|
| At 1 January 2011 | 10 | 2,162,882 | 12,784 | 2,175,676 |
| Profit for the financial year | - | - | 142,301 | 142,301 |
| Dividends | - | - | (142,905) | (142,905) |
| At 1 January 2012 | <u>10</u> | <u>2,162,882</u> | <u>12,180</u> | <u>2,175,072</u> |
| Profit for the financial year | - | - | 97,573 | 97,573 |
| Dividends | - | - | (33,453) | (33,453) |
| At 31 December 2012 | <u>10</u> | <u>2,162,882</u> | <u>76,300</u> | <u>2,239,192</u> |

12. SEGMENTAL REPORTING

The Company has only one class of business as described in the Directors' report and operates in one geographic market, Europe, Middle East and Africa ("EMEA")

13. RELATED PARTY TRANSACTIONS

The Company is exempt from the requirement to disclose transactions with fellow wholly owned Morgan Stanley Group undertakings under paragraph 3(c) of FRS 8 *Related party disclosures*. There were no other related party transactions requiring disclosure.

MORGAN STANLEY TOSTAO LIMITED

NOTES TO THE FINANCIAL STATEMENTS **Year ended 31 December 2012**

14. PARENT UNDERTAKINGS

The ultimate parent undertaking and controlling entity and the largest group of which the Company is a member and for which group financial statements are prepared is Morgan Stanley Morgan Stanley is incorporated in the state of Delaware, the United States of America and copies of its financial statements can be obtained from www.morganstanley.com/investorrelations

The Company's immediate controlling party is Morgan Stanley Dolor Limited which is registered in the Cayman Islands 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 parent undertaking of the smallest group of companies for which group financial statements are drawn up and of which the Company is a member is Morgan Stanley & Co International plc which is registered in England and Wales Copies of its financial statements can be obtained from the Registrar of Companies for England and Wales, Companies House, Crown Way, Cardiff CF14 3UZ