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May 18, 2020

Re: Application of Morgan Stanley to Acquire by Merger E*TRADE Financial Corporation – Response to Additional Information Request

VIA E-APPS

Ivan J. Hurwitz
Senior Vice President, Bank Applications
Federal Reserve Bank of New York
33 Liberty Street, New York, NY 10045

Dear Mr. Hurwitz:

On March 25, 2020, Morgan Stanley, New York, New York, filed an application (the "**Application**"), pursuant to Sections 4(j) and 4(k) of the Bank Holding Company Act of 1956, as amended, and Regulation Y promulgated thereunder, as well as Section 163(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, requesting approval of the Board of Governors of the Federal Reserve System (the "**Federal Reserve**") for Morgan Stanley to acquire by merger E*TRADE Financial Corporation ("**E*TRADE**"), Arlington, Virginia, with Morgan Stanley as the surviving entity (the "**Proposed Transaction**").

This letter responds to the requests for additional information regarding the Application and the Proposed Transaction that Federal Reserve staff emailed to me on April 17, 2020 (the "**April 17th Additional Information Request**") and supplements Morgan Stanley's first set of responses to the April 17th Additional Information Request that were submitted on April 29, 2020. By this letter, Morgan Stanley provides responses to another 20 requested items in the April 17th Additional Information Request – specifically, Additional Information Requests 3, 5, 6, 7, 14, 16, 17, 18, 19, 28, 29, 30, 31, 33, 34, 35, 36, 39, 41 and 43. Morgan Stanley expects to provide responsive information to the remaining Additional Information Requests included in the April 17th Additional Information Request, as well as information responsive to the second set of Additional Information Requests dated May 8, 2020, in a subsequent submission in the next few weeks (expected to be made on or about June 1, 2020).

Appendix 1 and Confidential Appendix 2 to this letter reproduce the requested items and related text from the April 17th Additional Information Request using bold type and provide responses following their corresponding items. Also included with this letter is a Confidential Exhibits Volume.

Morgan Stanley respectfully requests confidential treatment under the federal Freedom of Information Act, 5 U.S.C. § 552 ("**FOIA**"), and the implementing regulations of the Federal

Reserve, 12 C.F.R. Part 261, for the responses included in Confidential Appendix 2 and the information contained in the Confidential Exhibits Volume to this application, as well as any other information marked "confidential" (collectively, the "**Confidential Materials**"). The Confidential Materials include, for example, non-public information regarding the business strategies and plans of (i) Morgan Stanley and its subsidiary banks, Morgan Stanley Bank, N.A. and Morgan Stanley Private Bank, National Association (together the "**Morgan Stanley Banks**"), and (ii) E*TRADE and its subsidiary banks, E*TRADE Bank and E*TRADE Savings Bank (together the "**E*TRADE Banks**"), and other information regarding additional matters of a similar nature, which is commercial or financial information that is customarily and actually treated as confidential by Morgan Stanley or E*TRADE and that is being provided to the government under an assurance of confidentiality. Certain information in the Confidential Materials may also include confidential supervisory information, which is statutorily protected from disclosure. None of the information in the Confidential Materials is the type of information that would otherwise be made available to the public under any circumstances. All such information, if made public, could result in substantial and irreparable harm to Morgan Stanley, the Morgan Stanley Banks, E*TRADE, and the E*TRADE Banks. In addition, potential investors could be influenced or misled by such information, which is not reported in any documents filed or to be filed in accordance with the disclosure requirements of applicable securities laws, as a result of which Morgan Stanley or E*TRADE could be exposed to potential inadvertent violations of law or exposure to legal claims. Accordingly, confidential treatment is respectfully requested with respect to the Confidential Materials under FOIA, specifically 5 U.S.C. § 552(b)(4) and (b)(8), and the Federal Reserve's implementing regulations, specifically 12 CFR 261.14(a)(4) and (a)(8). The Confidential Materials may also be exempt from disclosure under other provisions of law.

We also request that, if the Federal Reserve should make a preliminary determination not to comply with the request for confidential treatment, Morgan Stanley be given notice thereof in ample time to permit it to make an appropriate submission as to why such information should be preserved in confidence. If the Confidential Materials, or any memoranda, notes or writings made by employees, agents or other persons under the control of the Federal Reserve or any Federal Reserve Bank that incorporate, include or relate to any of the matters referred to in the Confidential Materials, are the subject of a FOIA request or a request or demand for disclosure by any governmental agency, Congressional office or committee, or court or grand jury, we request, pursuant to the Federal Reserve's regulations, that you notify Morgan Stanley and the undersigned prior to making such disclosure.

We further ask that Morgan Stanley and the undersigned be furnished with a copy of all written materials pertaining to such request (including, but not limited to, the request itself and any determination with respect to such request) and that Morgan Stanley and the undersigned be given sufficient advance notice of any intended release so that Morgan Stanley may, if deemed necessary or appropriate, pursue any available remedies.

* * *

If you have any questions regarding this letter or the confidential treatment request, please feel free to contact me at (212) 450-4296 or luigi.deghenghi@davispolk.com, or my colleague Ryan Johansen at (212) 450-3408 or ryan.johansen@davispolk.com.

Yours sincerely,

Luigi L. De Ghenghi

Enclosures

cc: Alison M. Thro, Federal Reserve
Eric F. Grossman, Morgan Stanley
Sebastiano Visentini, Morgan Stanley
Andrew S. Baer, Morgan Stanley
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Dohyun Kim, Skadden, Arps, Slate, Meagher & Flom LLP

APPENDIX 1

Responses to April 17th Additional Information Request

Defined terms used but not defined in these responses have the same meaning set forth in Morgan Stanley's Application.

3. Please describe how E*TRADE's margin loans have performed during the current economic downturn. Provide a summary of expected losses (e.g., total losses experienced, how many loans suffered greater than $100k in losses) or any material risk events.

Please see Confidential Exhibit D.[1]

5. Please indicate whether the recent economic downturn would have any adverse impact on the combined enterprise-wide risk management and compliance programs, and discuss how Morgan Stanley plans to address such an impact. In this regard, also address whether Morgan Stanley is planning any changes to the overall integration plans.

Impact on Risk and Compliance Programs

Morgan Stanley's risk appetite, limits, capacity, management framework and monitoring (collectively, the "**risk program**") and compliance programs are reflective of the firm's business mix and associated risk profile and are reviewed on at least an annual basis. Upon closing of the Proposed Transaction, Morgan Stanley will incorporate E*TRADE into its firm-wide risk and compliance programs.

The recent economic downturn is not expected to have any material adverse impact on the proposed combined risk and compliance programs. While a prolonged economic crisis could have a negative impact on the firm's earnings, Morgan Stanley does not anticipate that the economic crisis would adversely affect the structure, resources or overall quality and effectiveness of its proposed combined risk and compliance programs.

Morgan Stanley believes that its current risk and compliance programs are functioning effectively notwithstanding the challenges posed by largely remote working conditions. Morgan Stanley's risk management and compliance groups continue to perform their respective control and monitoring activities, while meeting and communicating internally with respect to these activities with increased frequency since the onset of the COVID-19 pandemic.

[1] The exhibit lettering used in this submission continues in sequence from the lettering used in the submission dated April 29, 2020.

Morgan Stanley remains highly committed to ensuring it maintains strong risk management and compliance programs to manage severe economic stress scenarios. Compliance risk focus areas will continue to be documented in the firm's annual compliance plan with monitoring conducted through an integrated risk assessment.

With respect to its annual compliance plan, although Morgan Stanley continues to monitor the impact of COVID-19 on its compliance monitoring and risk assessment efforts, to date Morgan Stanley does not believe that any change to the annual compliance plan is currently warranted.

Morgan Stanley does not currently have any plans to reduce risk management or compliance headcount in 2020. Morgan Stanley will continue to evaluate its optimal organizational structure for risk management and compliance, inclusive of E*TRADE, as it implements a post-closing target operating model. Morgan Stanley does not currently foresee making any material changes to its target operating model as a result of the COVID-19 pandemic.

Impact on Integration Plans

Morgan Stanley has developed a comprehensive post-closing integration framework for both the Morgan Stanley and E*TRADE businesses and their respective operations and controls infrastructure. The governance of the integration framework consists of multiple committees, composed of senior executives from both Morgan Stanley and E*TRADE, which oversee the merger integration office. The integration framework includes 19 work streams, with multiple sub-work streams, that drive various aspects of the integration from both a business and infrastructure perspective. The merger integration office is responsible for overseeing and coordinating day-to-day integration activities across all of the work streams; mobilizing appropriate levels of resources, including engaging external consultants, to assist with integration-related activities; establishing appropriate targets and milestones; managing and maintaining tracking and reporting requirements, communicating with the relevant stakeholders; and managing timelines and facilitating constant coordination between work streams. The work streams are performing review and due diligence activities to arrive at target operating model design recommendations by the end of August 2020, which will then be reviewed and socialized by senior executives. There are currently no plans to revise the overall integration timeline or plans as a result of the COVID-19 pandemic. While COVID-19 has required both firms to perform pre-integration related activities on a largely remote (work from home) basis, this has not materially impaired the firms' ability to move forward with overall integration plans. Morgan Stanley has also hired external consultants to assist with some of the integration activities. The firm will continue to monitor the situation and update its integration plans accordingly, including updates to mitigate any potential risks arising from the COVID-19 pandemic.

6. Following consummation of the proposed merger, please describe changes, if any, to Morgan Stanley's enterprise-wide risk appetite and/or risk capacity. Your response should include, if applicable, anticipated changes to Morgan Stanley's risk management framework and/or total borrowing capacity, and to monitoring of operational and cybersecurity risks.

As noted in response to Additional Information Request 5 above, Morgan Stanley has developed a comprehensive post-closing integration framework for combining Morgan Stanley and E*TRADE's businesses and respective infrastructure operations and controls. The integration framework contemplates the incorporation of E*TRADE into Morgan Stanley's enterprise-wide risk management framework, including updating and modifying its risk limits, controls, policies and procedures as necessary.

As part of developing the integration framework, Morgan Stanley continues to do further work on its assessment of E*TRADE's risk profile and risk program, including E*TRADE's controls, policies and procedures relating to credit and liquidity risk, money transfers, fraud detection, information and cybersecurity, and data leakage risk, among other risks. Upon completion of this work, which Morgan Stanley currently estimates will be by the end of August 2020, the firm will be in a position to determine whether any changes will be made to Morgan Stanley's enterprise-wide risk appetite, risk and/or borrowing capacity, monitoring of operational and cybersecurity risks, or any other aspect of its risk management framework. However, based on the work it has done to date, Morgan Stanley currently believes that E*TRADE's risk management framework is generally aligned with Morgan Stanley's and that E*TRADE's business mix and risk profile are not expected to require Morgan Stanley to make any material changes to its risk management framework or its risk appetite statement. Should there be any change in Morgan Stanley's current assessment, Morgan Stanley will supplement its response to this Additional Information Request or otherwise inform the Federal Reserve, as applicable.

7. Page 3 of the notification notes that the proposed transaction is expected to add approximately $56 billion in low-cost deposits, which would provide significant funding benefits to Morgan Stanley and will enable it to reduce its reliance upon more expensive wholesale funding. Please confirm our understanding that the $56 billion in low-cost deposits includes the deposits that E*TRADE currently maintains through sweep deposit arrangements with third-party financial institutions. If so, describe how the inclusion of sweep deposits in the total low-cost deposits would impact the FDIC insurance coverage that E*TRADE's sweep programs currently provide wherein customers have additional coverage of up to $1.25 million for individuals and $2.5 million for joint account holders. Further, please provide the combined firms' wholesale versus retail deposit profile.

Composition of $56.3 Billion of Deposits

Morgan Stanley and E*TRADE confirm the staff's understanding that the approximately $56.3 billion in low-cost deposits as of December 31, 2019 include the deposits that E*TRADE currently maintains through sweep deposit arrangements with third-party financial institutions.

The sweep deposits sourced from E*TRADE's broker-dealer sweep program comprise approximately $44.8 billion of the low-cost deposits. In turn, the sweep deposits consist of approximately $16.9 billion that are placed with third-party financial institutions and approximately $27.9 billion that are placed at the E*TRADE Banks. In addition, as of December 31, 2019, there was approximately $0.8 billion of E*TRADE Bank's Premium Savings Account balances placed at third-party financial institutions through a reciprocal deposit program. The table below provides additional information on the composition of E*TRADE's $56.3 billion of low-cost deposits as of December 31, 2019.

	Qtr ended 12/31/19
Low-Cost Deposits ($B)	
Brokerage sweep deposits	$ 27.9
Bank sweep deposits	6.4
Savings, checking and other banking assets	4.3
Total on-balance sheet low-cost deposits	**38.6**
Brokerage sweep deposits at unaffiliated financial institutions	16.9
Bank sweep deposits at unaffiliated financial institutions	0.8
Total low-cost deposits placed at third parties	**17.7**
Total low-cost deposits	**$ 56.3**

Impact on FDIC Insurance Coverage

Through its two IDIs, Morgan Stanley is currently able to provide FDIC insurance in an aggregate amount of up to $500,000 for individuals and $1 million for joint account holders. Morgan Stanley also offers participation in the Certificate of Deposit Account Registry Service ("**CDARS**") and the Insured Cash Sweep ("**ICS**") products for clients requiring additional FDIC insurance coverage. CDARS and ICS are multi-bank deposit products that provide clients with access to multi-million dollar FDIC insurance coverage through the Promontory Interfinancial Network.

Morgan Stanley continues to assess the potential post-closing legal entity structures for the integration of E*TRADE's legal entities with Morgan Stanley, and as of the date of this response no decision has been made regarding such legal entity structures. Specifically with respect to the E*TRADE Banks, factors such as client service delivery, impact on funding capabilities, and regulatory considerations are being evaluated in deciding whether to merge the E*TRADE Banks with the Morgan Stanley Banks or to independently operate them, in addition to continuing to review potential risk, liquidity, capital, and tax considerations, among other factors.

The final legal entity structure with respect to the number of IDIs operated by Morgan Stanley will obviously determine the specific details of the amount of FDIC deposit insurance coverage available to customers of the E*TRADE Banks. In light of the fact that the CDARS and ICS products already offer Morgan Stanley clients the ability to obtain greater deposit insurance coverage than would be available solely from the Morgan Stanley Banks, Morgan Stanley expects that customers of the E*TRADE Banks would have similar opportunities in the event of any combination of the E*TRADE Banks and the Morgan Stanley Banks.

Breakdown of Wholesale and Retail Deposits

As of December 31, 2019, the Morgan Stanley Banks had deposits of $199.4 billion, including deposits from affiliates. Based on data reported in the FR 2052a filings of the Morgan Stanley Banks, retail deposits comprised 77%, or $153.7 billion, of the total balance. Wholesale deposits comprised the remaining 23%, or $45.6 billion, of the total balance.

As of December 31, 2019, the E*TRADE Banks had deposits of $38.6 billion. E*TRADE is not currently subject to FR 2052a reporting obligations, and regards all of its deposits as retail deposits. Applying the FR 2052a definitions for consistency, however, approximately $38.5 billion of the E*TRADE Banks' deposits, or 99.6%, would be classified as retail deposits, with $142.8 million, or 0.4%, classified as wholesale deposits.

Accordingly, based on the foregoing data as of December 31, 2019, on a pro forma basis the combined organization is expected to have deposits of approximately $238.0 billion, including deposits from affiliates. Retail deposits are expected to comprise $192.2 billion, or 80.7%, of the total balance. Wholesale deposits are expected to comprise the remaining $45.7 billion, or 19.2%, of the total balance.

14. Please provide more detail regarding the Morgan Stanley litigation matters listed: nos. 328, 372, 360, 286, and 264.

Please see <u>Confidential Exhibit E</u>.

16. According to the Summary of Deposits (SOD), $179.8 billion deposits are booked at two branches of Morgan Stanley, and $42.7 billion deposits are booked at two branches of E*TRADE (as of June 2019).

a. Separately for both Morgan Stanley and E*TRADE, provide the breakdown of aggregate deposits by the location of depositors (ZIP code), i.e., the aggregate deposit amount of depositors residing in each five-digit ZIP code.

Please see <u>Confidential Exhibit F</u> and the first part of <u>Confidential Exhibit G</u>.

b. **Separately for both Morgan Stanley and E*TRADE, provide the aggregate deposit amounts tied to any brokerage account by the location of depositors (ZIP code).**

All deposits related to Morgan Stanley's Bank Deposit Program ("**BDP**") and Savings Program[2] are tied to a brokerage account, and accordingly information responsive to this request is identical to that produced in response to Additional Information Request 16.a, above. Please see Confidential Exhibit F. For E*TRADE, please see the second part of Confidential Exhibit G.

17. Separately for both Morgan Stanley and E*TRADE, provide the aggregate account value of all brokerage accounts by the location of customers (zip code).

Please see Confidential Exhibit H and Confidential Exhibit I.

18. Provide a list of activities and products in which Morgan Stanley plans to initiate new operations, or expand existing operations, subsequent to the closing of the E*TRADE merger.

As noted in Section V.B. of the Preliminary Statement of the Application, Morgan Stanley's and E*TRADE's products and services are largely complementary, with limited overlap. Based on Morgan Stanley's current assessments, Morgan Stanley expects that it would maintain the current suite of Morgan Stanley's and E*TRADE's products and services and, in an initial phase following the completion of the Proposed Transaction, focus on extending E*TRADE's products and services to existing Morgan Stanley clients and extending its products and services to existing E*TRADE clients.

Existing Morgan Stanley clients would benefit from E*TRADE's self-directed brokerage capabilities and offerings, including commission-free equities trading through the digital self-directed channel, as well as such digital banking products as checking and savings accounts and high-yield savings accounts. E*TRADE's digital banking platform would enable Morgan Stanley clients to open deposit accounts directly with one or more of its IDIs, a capability not currently available to clients of the Morgan Stanley Banks.

Existing E*TRADE clients would benefit from access to Morgan Stanley's full service advice offering, financial wellness and education platform, a wider range of investment and wealth management products, deeper research resources, and introductions to Morgan Stanley's financial advisors. Existing E*TRADE clients would also have expanded access to Morgan Stanley's lending products (e.g., securities-based loans and mortgages).

[2] The Morgan Stanley Preferred Savings Program is an investment option in a brokerage account. Funds are deposited with MSPBNA and/or MSBNA. The BDP is described in further detail in the response to Additional Information Request 30, below.

As part of the initial phase following completion of the Proposed Transaction, clients of the combined firm would also benefit from the execution of the Morgan Stanley Banks' strategic plans for the three-year period from January 1, 2020 through December 21, 2022 ("**Strategic Plans**"). The Strategic Plans are described in Confidential Exhibit J and the response to Additional Information Request 19 below and include planned increases in commercial lending, securities-based lending, residential mortgage lending, and community development financing. Depending on the strategic decisions taken regarding the potential combination of one or both of the E*TRADE Banks and the Morgan Stanley Banks, the Strategic Plans may be extended to include the E*TRADE Banks.

In connection with their ongoing integration planning, Morgan Stanley and E*TRADE will evaluate potential areas of expansion of operations or commencement of new operations, including any new products or services, to meet the needs of the combined firm's client base. As of the date of this response, the firms have not yet made any decisions regarding any such new products and services. In any event, any new products or services would likely be launched as part of a subsequent phase following completion of the Proposed Transaction, and would need to be vetted through the combined firm's new product approval process and be consistent with the combined firm's risk appetite within its risk management framework. To the extent any proposed new products or services to be offered following completion of the Proposed Transaction are identified before closing, Morgan Stanley will supplement its response to this Additional Information Request or otherwise inform the Federal Reserve, as applicable.

19. How would the combined entity use the deposit influx as a result of the Proposed Transaction to expand its lending and broker-dealer activities? How would this affect:

a. Commercial lending (expected volume increase)

i. Lending to SMEs (expected volume increase)

ii. Syndicated funded commitments (expected volume increase)

iii. Syndicated pipeline commitments (expected volume increase)

b. Consumer lending (expected volume increase)

c. Real estate (mortgage) lending (expected volume increase)

d. Underwriting activities (expected volume increase)

e. Broker-dealer activities (expected volume increase)?

The Morgan Stanley Banks currently operate under Strategic Plans that were reviewed and approved by their respective Boards of Directors in January 2020. The Morgan Stanley Banks had combined lending balances of approximately $137 billion as of December 31, 2019. As described in more detail in Confidential Exhibit J, the Strategic Plans include planned increases in commercial lending, securities-based lending, residential mortgage lending, and community development financing. These planned increases in lending activities stand to benefit from reduced reliance on wholesale funding and greater access to low-cost deposit funding as a result of the Proposed Transaction, and are consistent with the risk appetite of the Morgan Stanley Banks and of Morgan Stanley as a whole.

The Strategic Plans remain the most current articulation of the strategic direction of the Morgan Stanley Banks. However, the COVID-19 pandemic is expected to have a material impact on the future earnings and growth of the Morgan Stanley Banks and, as a result, adjustments to the Strategic Plans may be warranted. In any event, Morgan Stanley remains committed to ensuring its customers have access to credit during this challenging economic period.

Please see Confidential Exhibit J for further information on the Strategic Plans.

28. Describe the current clientele breakdown (including institutional and retail investors, and retirement plans) of Morgan Stanley and E*TRADE's online brokerage platform and their respective shares in terms of client assets, as of the most recent quarter for which data are available.

Clientele Breakdown for Morgan Stanley

As of December 31, 2019, Morgan Stanley's Wealth Management business had a total of $2.7 trillion in client assets under management, of which 16%, or approximately $432 billion, was classified as institutional[3] and 84%, or approximately $2.3 trillion, was classified as retail.

Within the wirehouse channel, which consists of large-scale broker-dealers such as Bank of America Merrill Lynch, Wells Fargo and UBS Wealth Management Americas, among others, as of December 31, 2018,[4] Morgan Stanley accounted for approximately 34% of the assets under management or approximately 7% of the overall industry (based on Cerulli's estimate[5] of $31.6 trillion of assets under management).

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[3] Morgan Stanley defines the term "institutional" as referring to its Institutional Wealth Services business, which consists of Corporate Retirement Plans, Global Stock Plan Services, Graystone Consulting, Corporate Cash, Government Entities and Workplace Wealth Solutions to help advisors support institutional clients and businesses.

[4] Morgan Stanley evaluated its market share for purposes of this question based on data provided by Cerulli, which was last updated as of December 31, 2018. *See* U.S. Broker / Dealer Marketplace 2019: Value Levers – Technology, Planning and Practice Management, 11/4/2019; Exhibit 4.01 Assets by Intermediary Segment, 2013 – 2018 ($ billions). As of December 31, 2018, Morgan Stanley's Wealth Management business had a total of $2.3 trillion in assets under management, of which 17%, or approximately $384 billion, was classified as institutional, and 83%, or approximately $1.9 trillion, was classified as retail.

[5] Cerulli defines the wirehouse channel to include full-service broker/dealer firms, with a history of national distribution, investment banking, and brokerage, offering a full range of investment services and products.

In terms of share of wallet, Morgan Stanley estimates that its Wealth Management business accounts for approximately 50% of its clients' investable assets.

Clientele Breakdown for E*TRADE

As of March 31, 2020, E*TRADE's online brokerage platform had a total of approximately $587 billion client assets, of which 45%, or approximately $266 billion, was classified as institutional and 55%, or approximately $321 billion, was classified as retail. Retirement plans, which are a subset within retail, comprise 13%, or approximately $74 billion, of the total client assets of E*TRADE's online brokerage platform.

In terms of share of wallet, E*TRADE estimates that its online brokerage platform accounts for approximately 12% of its clients' investable assets.

The table below provides E*TRADE's clientele breakdown as of March 31, 2020 for its online brokerage platform.

(as of March 31, 2020)	**Accounts**	**Client Assets (in billions)**	**Client Assets (as percentage)**
Retail	**5,498,596**	**$321.2**	**54.7%**
Non-Retirement	*4,262,177*	*$247.1*	*42.1%*
Retirement	*1,236,419*	*$74.1*	*12.6%*
Advisor Services	**144,453**	**$16.6**	**2.8%**
Corporate Services	**1,946,956**	**$249.5 (includes $113.7 unvested)**	**42.5% (includes 19.4% unvested)**
Total	**7,590,005**	**$587.3**	**100.0%**

29. Provide the volume of total deposits, brokered deposits, and uninsured deposits for both Morgan Stanley and the E*TRADE banks both before and after the merger.

At March 31, 2020, the Morgan Stanley Banks had aggregate deposits of $253.9 billion, including deposits from affiliates, and ETB had total consolidated deposits of $42.6 billion.[6]

[6] As noted in the Application, the other of the E*TRADE Banks, ETSB, is a consolidated subsidiary of ETB. Amounts of total deposits, brokered deposits and uninsured deposits for ETSB are therefore included in the amounts provided for ETB throughout this response.

At March 31, 2020, the Morgan Stanley Banks had aggregate brokered deposits and uninsured deposits of $82.4 billion and $78.3 billion, respectively, and ETB had brokered deposits and uninsured deposits of $39.9 billion and $6.0 billion, respectively.

As of the date of this response, Morgan Stanley and E*TRADE have not made any decision about a potential consolidation the Morgan Stanley Banks and the E*TRADE Banks. However, on a pro forma consolidated basis as of March 31, 2020, excluding any deposits the Morgan Stanley Banks had with the E*TRADE Banks and vice versa, the total deposits, brokered deposits and uninsured deposits of the combined firm's IDIs would be $296.5 billion, $122.3 billion, and $84.3 billion, respectively.

30. Provide details on sweeping activities conducted by Morgan Stanley and E*TRADE's broker-dealer subsidiary, including a breakdown of banks and other financial institutions into which the funds are swept.

Morgan Stanley's Sweep Activities

Under Morgan Stanley's BDP, free credit balances[7] in any of the following Morgan Stanley Wealth Management brokerage account types are automatically deposited into deposit accounts ("**Deposit Accounts**") established for account holders by and in the name of Morgan Stanley Smith Barney LLC, as agent and custodian for its clients.

- Active Assets Account;
- CashPlus Account;
- Basic Securities Account;
- Individual Retirement Account ("**IRA**");
- Education Savings Account, commonly referred to as a Coverdell Education Savings Account;
- Business Active Assets Account; and
- Business Basic Securities Account, and Versatile Investment Program Plan Account, Retirement Plan Manager Account or Employee Benefit Trust Account, each of which are account types used at Morgan Stanley to hold assets in connection with "employee benefit plans."

Deposit Accounts are established at MSBNA and MSPBNA and include a Demand Deposit Account and a Money Market Deposit Account. Once the deposited

[7] For this purpose, the definition of free credit balance is the same as that used in Rule 15c3-3 under the Securities Exchange Act of 1934. *See* 17 C.F.R. § 240.15c3-3(a)(8).

funds from any individual client account reach $20,000,000 (the "**Deposit Maximum**"), any excess free credit balance in that account above the Deposit Maximum will be swept into a money market mutual fund ("**MMF**"), the Morgan Stanley Institutional Liquidity Funds Government Securities Portfolio.

The BDP is the default sweep choice. If clients are ineligible to participate in the BDP, any free credit balances will be swept to one of the following MMFs, each of which is offered by Morgan Stanley, based on eligibility:

- Institutional Liquidity Funds Government Securities Portfolio, which is available for clients that are U.S. persons and not eligible for the BDP[8] or, as noted above, have free credit balances that are above the Deposit Maximum.

- Treasury Liquidity Fund, which is available for clients residing outside of the U.S. and not eligible for BDP.

- U.S. Government Money Market Trust, which is available for IRA accounts that are not eligible for BDP.

Please see <u>Confidential Exhibit K</u> for further information on the BDP.

E*TRADE*'s *Sweep Activities

E*TRADE Securities offers its customers multiple options for uninvested cash within their brokerage accounts, including a Cash Balance Program (i.e., free credits) that is held with E*TRADE Securities and various FDIC-insured sweep deposits. For the FDIC-insured sweep deposits, available cash in a customer's brokerage account is swept automatically on a daily basis between the brokerage account and the selected sweep option.

FDIC-insured sweep deposit options include:

- Extended Insurance Sweep Deposit Account (ESDA) – provides FDIC insurance coverage up to $1.25 million per account (or $2.5 million for joint accounts) through the placement of sweep deposits at the E*TRADE Banks and unaffiliated depository institutions;

- Retirement Sweep Deposits Account (RSDA) – available to E*TRADE Securities' retirement customers[9] and provides FDIC insurance coverage up to

[8] Examples of clients ineligible for BDP include (a) those with legal addresses in certain non-U.S. jurisdictions where the ability to offer BDP is restricted, and (b) certain entity types such as financial institutions.

[9] "Retirement customers" refers to accounts that are for retirement purposes such as the following: IRA, Rollover IRA, Roth IRA, Coverdell IRA, 401(k), Contributory IRA, SEP/SIMPLE IRA, Coverdell Education Savings Account and other accounts defined by the Internal Revenue Code of 1986 as well as qualified plans under Title I of the Employee Retirement Income Security Act of 1974.

$500,000 per account (or $1.0 million for joint accounts) through placement of sweep deposits at the E*TRADE Banks; and

- International Sweep Deposit Account (ISDA) – available to E*TRADE Securities customers who reside outside the United States, provides FDIC insurance coverage up to $250,000 per account (or $500,000 for joint accounts) through the placement of sweep deposits at ETSB.

Please see Confidential Exhibit L for further information on E*TRADE's sweep activities.

31. Describe the structure of the combined institution's consumer compliance program following the merger. In your response, please discuss:

a. Which functions will be housed at the holding company level, and which will be housed at subsidiary banks;

b. The experience level of staff responsible for managing the combined organization's compliance program, and general staffing plans;

c. Internal audit plans for the compliance program;

d. Third-party oversight plans for the combined institution;

e. Plans for outsourcing compliance functions to third party providers, including plans for overseeing those third party providers; and

f. The governance structure overseeing the compliance program.

No changes are expected to the structure of Morgan Stanley's consumer compliance program, which is currently maintained at the level of the Morgan Stanley Banks, following the completion of the Proposed Transaction. The most significant sources of consumer compliance risk related to E*TRADE and its subsidiaries are expected to arise from the activities of the E*TRADE Banks, and therefore the consumer compliance management program for the E*TRADE Banks would be maintained at the bank level.

The combined firm's consumer compliance program would be overseen by the existing risk governance framework for the Morgan Stanley Banks ("**Bank Risk Governance Framework**"). Under the Bank Risk Governance Framework, compliance risk is overseen by each bank's Compliance Committee, which reports to its Risk Committee and to the Risk Committee of the relevant bank's board of directors.

After completion of the Proposed Transaction, elements of the consumer compliance program requiring coordination at the holding company level, such as privacy and third-party oversight, will have the necessary processes in place to ensure consistency across the firm. At the bank level, the banks' vendor management programs will continue to oversee and govern oversight of third-party vendors used by the banks.

Compliance staff at both the Morgan Stanley Banks and the E*TRADE Banks have started the process of planning for the integration of the banks' consumer compliance programs. As part of the integration planning, a side-by-side analysis will be completed covering the consumer compliance program in order to determine the post-closing target operating model. The guiding principles include ensuring that existing clients and businesses of each firm do not encounter material disruption as a result of the Proposed Transaction and creating an integrated compliance culture reflecting of contributions of both firms.

Morgan Stanley's and E*TRADE's consumer compliance teams have strong senior level talent that is capable of managing the combined compliance program. Current bank compliance senior managers have been in senior roles managing compliance at the Morgan Stanley Banks for an average of approximately eight years. At E*TRADE, the average level of experience of E*TRADE's bank compliance function is approximately 21 years. The experience level of compliance senior management at the Morgan Stanley Banks and the E*TRADE Banks includes prior experience as Chief Compliance Officers, regulatory, audit, and regulatory consultant roles at prior firms. While no decisions have yet been made about specific roles for individual members of both firms' consumer compliance groups in the combined firm, Morgan Stanley currently expects that all compliance staff roles would be retained following completion of the Proposed Transaction.

Morgan Stanley has no plans to outsource consumer compliance functions to third parties. Following completion of the Proposed Transaction, Morgan Stanley expects that the combined firm's consumer compliance program would continue to be subject to the internal audit function's audit plans and procedures. The audit plans and procedures of internal audit would be modified, as necessary, depending on any potential changes to the target operating model of the combined firm's consumer compliance program relative to the existing program.

33. If the applicant anticipates any changes to or expansion of products or services following this merger, describe any corresponding adjustments that would be made to combined institution's consumer compliance program as a result of such changes.

As noted in the response to Additional Information Request 18, Morgan Stanley's post-closing integration framework is focused – for an initial phase following the completion of the Proposed Transaction – on existing products and services offered by Morgan Stanley and E*TRADE. The integration teams expect that there will be expanded access to digital banking for existing Morgan Stanley clients (i.e., checking and savings accounts) to be provided by E*TRADE's digital banking platform and expanded access for existing E*TRADE clients to Morgan Stanley's lending products (e.g., securities-based loans and mortgages).

Oversight of consumer compliance risks will continue to be subject to Morgan Stanley's consumer compliance management program, which includes effective controls including policies and procedures, training, periodic testing, complaint analysis, fair lending oversight, and advice and guidance including reviews of marketing materials.

As noted in the response to Additional Information Request 18 above, as of the date of this response the firms have not yet made any decisions regarding any new products or services. To the extent that new products or services are offered (i) as part of the implementation of the Morgan Stanley Banks' Strategic Plans (which, depending on the strategic decisions taken regarding the potential combination of one or both of the E*TRADE Banks and the Morgan Stanley Banks, may be extended to include the E*TRADE Banks) or (ii) following the evaluation of potential areas of expansion of operations or commencement of new operations as part of the ongoing post-closing integration planning, any such products or services would need to be vetted through the relevant bank's risk appetite within its risk management framework. In addition, any new products or services offered by the combined firm's IDI(s) would be subject to the new product approval ("**NPA**") process, which includes a robust vetting of all risks, including consumer compliance risks, to ensure compliance with applicable laws, rules and regulations. The Compliance Department would continue to be a mandatory NPA quorum member, ensuring that adequate compliance controls are established prior to the launch of any new products or services for consumer clients and that any such products or services are subject to the banks' consumer compliance program.

34. Please provide the consumer compliance risk assessments and corresponding testing results for E*TRADE's deposit regulations and Morgan Stanley's deposit and lending activities.

Please see <u>Confidential Exhibit M</u> and <u>Confidential Exhibit N</u>.

35. Please provide any consumer related complaints and MIS for the prior 12 months for both firms.

For Morgan Stanley, please see <u>Confidential Exhibit O</u> and <u>Confidential Exhibit P</u>. For E*TRADE, please see <u>Confidential Exhibit Q</u> and <u>Confidential Exhibit R</u>.

36. Please update us on your decision making regarding whether, and which, offices of E*TRADE subsidiaries will be closed at the completion of the transaction.

As noted in the responses to Additional Information Requests 6 and 7 above, as part of its post-closing integration framework Morgan Stanley will continue to assess the potential post-closing legal entity structures for the integration of E*TRADE legal entities with Morgan Stanley. As of the date of this response no decision has been made on such legal entity structures or the target operating model for the combined firm. A key part of this analysis is the determination of the overall real estate strategy for the combined firm. The optimal end-state strategy for E*TRADE's corporate offices and retail locations will be determined as part of this ongoing integration planning. To the extent any decisions are made before closing on whether the offices of any E*TRADE subsidiaries will be closed following completion of the Proposed Transaction, Morgan Stanley will supplement its response to this Additional Information Request or otherwise inform the Federal Reserve, as applicable.

In any event, E*TRADE does not operate any bank branches physically accessible to clients and, accordingly, there are no bank branch closures planned as a result of the Proposed Transaction. In the event Morgan Stanley subsequently decides to combine one or both of the E*TRADE Banks with the Morgan Stanley Banks, it would seek the necessary prior approvals from the OCC under the Bank Merger Act.