

SYNALLOY CORP
Form 10-Q
August 07, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
x 1934

For the Quarterly Period Ended June 30, 2018

OR

..TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934

For the Transition Period from _____ to _____

COMMISSION FILE NUMBER 0-19687

Synalloy Corporation

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

57-0426694

(I.R.S. Employer Identification No.)

4510 Cox Road, Suite 201, Richmond, Virginia

(Address of principal executive offices)

23060

(Zip Code)

(804) 822-3260

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x No "

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

Large accelerated Filer " Accelerated filer x Non-accelerated filer " (Do not check if smaller reporting company)

Smaller reporting company " Emerging growth company "

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes " No "

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

The number of shares outstanding of the registrant's common stock as of July 31, 2018 was 8,802,206.

Synalloy Corporation
Index

PART I. FINANCIAL INFORMATION

<u>Item 1.</u>	Financial Statements	
	<u>Condensed Consolidated Balance Sheets as of June 30, 2018 (unaudited) and December 31, 2017</u>	<u>4</u>
	<u>Condensed Consolidated Statements of Operations for the Three and Six Months Ended June 30, 2018 and June 30, 2017 (unaudited)</u>	<u>5</u>
	<u>Condensed Consolidated Statements of Cash flows for the Six Months Ended June 30, 2018 and June 30, 2017 (unaudited)</u>	<u>6</u>
	<u>Notes to Condensed Consolidated Financial Statements</u>	<u>7</u>
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>15</u>
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>18</u>
Item 4.	<u>Controls and Procedures</u>	<u>18</u>

PART II. OTHER INFORMATION

Item 1.	<u>Legal Proceedings</u>	<u>19</u>
<u>Item 1A.</u>	<u>Risk Factors</u>	<u>19</u>
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>19</u>
Item 3.	<u>Defaults Upon Senior Securities</u>	<u>19</u>
Item 4.	<u>Mine Safety Disclosures</u>	<u>19</u>
Item 5.	<u>Other Information</u>	<u>19</u>
Item 6.	<u>Exhibits</u>	<u>20</u>
	<u>Signatures and Certifications</u>	<u>21</u>

PART I

Item 1. FINANCIAL STATEMENTS

3

Synalloy Corporation
Condensed Consolidated Balance Sheets

	June 30, 2018 (unaudited)	December 31, 2017
Assets		
Current assets		
Cash and cash equivalents	\$ 18,950	\$ 14,706
Accounts receivable, less allowance for doubtful accounts of \$5,000 and \$35,000, respectively	41,370,921	28,704,481
Inventories, net	90,571,141	72,125,181
Prepaid expenses and other current assets	18,707,741	6,802,072
Total current assets	150,668,753	107,646,440
Non-current assets		
Property, plant and equipment, net of accumulated depreciation of \$53,278,938 and \$50,451,436 respectively	35,605,480	35,080,009
Goodwill	6,003,525	6,003,525
Intangible assets, net of accumulated amortization of \$11,710,526 and \$10,568,479 respectively	9,738,474	10,880,521
Deferred charges, net and other non-current assets	265,441	263,655
Total assets	\$202,281,673	\$ 159,874,150
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable	\$27,357,477	\$24,256,812
Accrued expenses and other current liabilities	11,025,061	8,993,454
Total current liabilities	38,382,538	33,250,266
Long-term debt	53,933,944	25,913,557
Deferred income taxes	1,260,805	635,910
Long-term deferred gain, sale-leaseback	5,766,213	5,933,350
Long-term portion of earn-out liability	3,748,503	3,170,099
Other long-term liabilities	1,365,907	1,270,542
Total non-current liabilities	66,075,372	36,923,458
Commitments and contingencies – See Note 11		
Shareholders' equity		
Common stock, par value \$1 per share; authorized 24,000,000 shares; issued 10,300,000 shares	10,300,000	10,300,000
Capital in excess of par value	35,496,900	35,193,152
Retained earnings	65,630,953	58,129,382
Accumulated other comprehensive loss	—	(10,864)
	111,427,853	103,611,670
Less cost of common stock in treasury: 1,497,793 and 1,566,769 shares, respectively	13,604,090	13,911,244
Total shareholders' equity	97,823,763	89,700,426
Total liabilities and shareholders' equity	\$202,281,673	\$ 159,874,150

See accompanying notes to condensed consolidated financial statements.

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Synalloy Corporation

Condensed Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net sales	\$71,893,763	\$51,511,045	\$130,374,365	\$93,714,624
Cost of sales	56,177,441	43,333,118	103,424,624	78,133,119
Gross profit	15,716,322	8,177,927	26,949,741	15,581,505
Selling, general and administrative expense	7,738,752	6,281,988	13,594,872	12,170,664
Acquisition related costs	690,217	386,519	690,217	744,996
Operating income	7,287,353	1,509,420	12,664,652	2,665,845
Other expense (income)				
Interest expense	403,852	341,005	717,835	521,320
Change in fair value of interest rate swaps	(19,255)	16,927	(92,458)	(24,503)
Earn-out adjustment	2,307,598	(3,391)	2,461,658	(3,391)
Other, net	(59,112)	—	29,185	—
Income before income taxes	4,654,270	1,154,879	9,548,432	2,172,419
Provision for income taxes	976,998	325,000	2,035,998	641,000
Net income	\$3,677,272	\$829,879	\$7,512,434	\$1,531,419
Net income per common share:				
Basic	\$0.42	\$0.10	\$0.86	\$0.18
Diluted	\$0.41	\$0.10	\$0.85	\$0.18
Weighted average shares outstanding:				
Basic	8,776,239	8,699,488	8,761,182	8,686,714
Dilutive effect from stock options and grants	87,537	23,650	72,804	17,616
Diluted	8,863,776	8,723,138	8,833,986	8,704,330

See accompanying notes to condensed consolidated financial statements

Synalloy Corporation

Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended June 30,	
	2018	2017
Operating activities		
Net income	\$7,512,434	\$1,531,419
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation expense	2,874,216	2,545,195
Amortization expense	1,147,916	1,211,225
Amortization of debt issuance costs	45,492	27,219
Deferred income taxes	624,895	(450,864)
Earn-out adjustment	2,461,658	(3,391)
Reduction of losses on accounts receivable	(30,000)	(18,958)
Provision for losses on inventories	746,960	229,044
Gain on disposal of property, plant and equipment	(17,762)	—
Amortization of deferred gain on sale-leaseback	(167,137)	(167,136)
Straight line lease cost on sale-leaseback	184,344	203,265
Change in fair value of interest rate swaps	(92,458)	(24,503)
Change in fair value of equity securities	29,185	—
Change in environmental reserves	—	15,298
Issuance of treasury stock for director fees	276,000	287,475
Employee stock option and grant compensation	416,179	330,238
Changes in operating assets and liabilities:		
Accounts receivable	(12,768,096)	(12,193,408)
Inventories	(19,192,920)	(5,281,753)
Other assets and liabilities, net	(2,105,247)	(526,153)
Accounts payable	3,100,665	5,109,121
Accrued expenses	1,372,968	2,170,359
Accrued income taxes	889,103	(560,732)
Net cash used in operating activities	(12,691,605)	(5,567,040)
Investing activities		
Purchases of property, plant and equipment	(3,381,925)	(2,831,976)
Purchases of equity securities	(336,951)	(3,831,521)
Acquisition of the stainless pipe and tube assets of Marcegaglia USA, Inc. ("MUSA")	—	(11,953,513)
Cash placed in escrow for acquisition of the galvanized pipe and tube assets of MUSA	(10,378,281)	—
Net cash used in investing activities	(14,097,157)	(18,617,010)
Financing activities		
Net borrowings from line of credit	28,020,386	24,241,144
Payments on capital lease obligation	(52,549)	(67,260)
Payments of debt issuance costs	(53,146)	—
Payments on earn-out liability to MUSA	(1,172,065)	—
Proceeds from exercised stock options	50,380	—
Net cash provided by financing activities	26,793,006	24,173,884
Increase in cash and cash equivalents	4,244	(10,166)
Cash and cash equivalents at beginning of period	14,706	62,873
Cash and cash equivalents at end of period	\$18,950	\$52,707

Supplemental disclosure

Cash paid for:

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Interest	\$613,918	\$345,009
Income taxes	\$471,000	\$1,659,565

See accompanying notes to condensed consolidated financial statements

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

Unless indicated otherwise, the terms "Company," "we," "us," and "our" refer to Synalloy Corporation and its consolidated subsidiaries.

1. Basis of Financial Statement Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included as required by Regulation S-X, Rule 10-01. Operating results for the six-month period ended June 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

2. Recently Issued Accounting Standards

Adoption of Recently Issued Accounting Standards

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers (Topic 606)". Topic 606 supersedes the revenue recognition requirements in Topic 605 "Revenue Recognition" (Topic 605), and requires entities to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Company adopted Topic 606 as of January 1, 2018 using the modified retrospective transition method. The adoption of this Topic did not have an effect on the Company's consolidated financial statements. See Note 3 for further details.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments (Topic 825)", to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. The standard is effective for all public companies for annual and interim reporting periods beginning after December 15, 2017. The standard requires equity investments (except for those under the equity method of accounting) to be measured at fair value, with changes in fair value recognized in net income. The amendments in the update supersede the guidance to classify equity securities with readily determinable fair values into different categories, and require equity securities to be measured at fair value with changes recognized in net income as opposed to other comprehensive income. The Company adopted ASU 2016-01 effective January 1, 2018 and the effects of this standard are included in the accompanying condensed consolidated financial statements for the three-month and six-month periods ended June 30, 2018. The Company applied the amendments by means of a cumulative effective adjustment to the balance sheet as of January 1, 2018, which resulted in a reclassification of \$10,864 from Accumulated Other Comprehensive Loss to Retained Earnings.

In January 2017, the FASB issued ASU No. 2017-01 "Business Combinations (Topic 805): Clarifying the Definition of a Business." ASU 2017-01 provides guidance to evaluate whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. If substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single asset or a group of similar assets, the assets acquired (or disposed of) are not considered a business. The Company adopted ASU 2017-01 as of January 1, 2018 on a prospective basis. The adoption of this Topic did not have an effect on the Company's consolidated financial statements as of June 30, 2018.

In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting," which amends the scope of modification accounting for share-based payment arrangements, provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting under ASC 718. ASU 2017-09 is effective for fiscal years beginning after December 15, 2017. We adopted ASU 2017-09 as of January 1, 2018 on a prospective basis. The adoption of this Topic did not have an impact on the Company's consolidated financial statements as of June 30, 2018.

Recently Issued Accounting Standards Not Yet Adopted

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)," to increase the transparency and comparability of lease recognition and disclosure. The update establishes a right of use ("ROU") model which requires lessees to recognize lease

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

contracts with a term greater than one year on the balance sheet as ROU assets and lease liabilities. Leases will be classified as either financing or operating which will determine expense classification and recognition. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 and must be applied using the modified retrospective approach. Early adoption is permitted. While the Company expects ASU 2016-02 to add material ROU assets and lease liabilities to the consolidated balance sheets related to its current land and building operating leases, it is evaluating other effects that the new standard will have on the consolidated financial statements as well as its business processes, internal controls, and accounting policies. As part of its assessment, the Company is reviewing its lease portfolio and identifying which attributes of its leases will be impacted by ASU 2016-02.

3. Revenues

Adoption of ASC Topic 606, "Revenue from Contracts with Customers"

On January 1, 2018, the Company adopted Topic 606 using the modified retrospective method applied to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under Topic 605. The Company operates as a manufacturer of various products, and revenue is comprised of short-term contracts with point-in-time performance obligations. As a result, the Company did not identify any differences in its recognition of revenue between Topic 606 and Topic 605. Accordingly, there was no adjustment required to opening retained earnings for the cumulative impact of adopting Topic 606 and no impact to revenues for the three-month or six-month periods ended June 30, 2018 as a result of applying Topic 606.

Revenue Recognition

Revenues are recognized when control of the promised goods or services is transferred to our customers upon shipment, in an amount that reflects the consideration we expect to be entitled to in exchange for those goods or services.

The following table presents the Company's revenues, disaggregated by product group. Substantially all of the Company's revenues are derived from contracts with customers where performance obligations are satisfied at a point-in-time.

	Three Months Ended		Six Months Ended	
	Jun 30, 2018	Jun 30, 2017	Jun 30, 2018	Jun 30, 2017
Storage tank and vessel	\$9,071,649	\$6,057,865	\$14,847,421	\$12,331,705
Seamless carbon steel pipe and tube	8,403,288	6,391,212	16,835,901	12,112,688
Stainless steel pipe	38,899,542	26,639,245	70,183,404	44,353,889
Specialty chemicals	15,519,284	12,422,723	28,507,639	24,916,342
Total revenues	\$71,893,763	\$51,511,045	\$130,374,365	\$93,714,624

Arrangements with Multiple Performance Obligations

Our contracts with customers may include multiple performance obligations. For such arrangements, revenue for each performance obligation is based on its standalone selling price and revenue is recognized as each performance obligation is satisfied. The Company generally determines standalone selling prices based on the prices charged to customers using the adjusted market assessment approach or expected cost plus margin.

Deferred Revenues

Deferred revenues are recorded when cash payments are received in advance of satisfying the performance obligation, including amounts which are refundable. The deferred revenue balance increased \$55,163 during the first six months of 2018 to \$240,037 as of June 30, 2018 due to receiving \$1,481,644 in advance of satisfying our performance obligations during the period, offset by \$1,426,481 of revenue that was recognized during the period after satisfying the performance obligations that were included

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

in the beginning deferred revenue balance or received during the current period. Deferred revenues are included in "Accrued expenses and other current liabilities" on the accompanying Condensed Consolidated Balance Sheets.

Our payment terms vary by the financial strength or location of our customer and the products offered. The length of time between invoicing and when payment is due is not significant. For certain customers, payment is required before the products or services are delivered to the customer.

Practical Expedients and Elections

When shipping and handling activities are performed after a customer obtains control of goods, the Company reflects shipping and handling activities as part of satisfying the obligation of providing goods to the customer.

In some instances, the Company withholds various states' sales taxes upon shipments into those states. Accordingly, management makes an accounting policy election to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are imposed on and concurrent with a specific revenue-producing transaction and collected from a customer.

The Company expenses sales commissions when incurred because the amortization period would have been one year or less. These costs are recorded within selling, general, and administrative expenses.

The Company does not disclose the value of unsatisfied performance obligations since contracts are expected to be completed within one year.

4. Inventories

Inventories are stated at the lower of cost or net realizable value. Cost is determined by either specific identification or weighted average methods. The components of inventories are as follows:

	Jun 30, 2018	Dec 31, 2017
Raw materials	\$46,202,040	\$37,748,316
Work-in-process	16,477,860	9,491,408
Finished goods	27,891,241	24,885,457
	\$90,571,141	\$72,125,181

5. Stock options and restricted stock

During the first six months of 2018, stock options for 40,606 shares of common stock were exercised by officers or employees for an aggregate exercise price of \$474,378. No options were exercised by employees or directors in 2017. Stock compensation expense for the three and six-months ended June 30, 2018 was \$223,979 and \$416,179, respectively. Stock compensation expense for the three and six-months ended June 30, 2017 was approximately \$210,000 and \$330,000, respectively.

On February 7, 2018, the Compensation & Long-Term Incentive Committee (the "Committee") of the Company's Board of Directors approved stock grants under the Company's 2015 Stock Awards Plan to certain management employees of the Company where 65,527 shares with a market price of \$12.47 per share were granted under the Plan. These stock awards vest in either 20 percent or 33 percent increments annually on a cumulative basis, beginning one

year after the date of grant. In order for the awards to vest, the employee must be in the continuous employment of the Company since the date of the award. Any portion of an award that has not vested is forfeited upon termination of employment. The Company may terminate any portion of the award that has not vested upon an employee's failure to comply with all conditions of the award or the 2015 Stock Awards Plan. An employee is not entitled to any voting rights with respect to any shares not yet vested, and the shares are not transferable.

The diluted earnings per share calculations exclude the effect of potentially dilutive shares when the inclusion of those shares in the calculation would have an anti-dilutive effect. For the six months ended June 30, 2018 and June 30, 2017 the Company had

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

weighted average shares of common stock, in the form of stock grants and options, of 36,815 and 144,064, respectively, which were not included in the diluted earnings per share calculation as their effect was anti-dilutive.

6. Income Taxes

The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state jurisdictions. The Company is no longer subject to U.S. federal examinations for years before 2014 or state income tax examinations for years before 2013. During the first six-months of 2018, the Company did not identify nor reserve for any unrecognized tax benefits.

The effective tax rate was 21 percent for the three and six-month periods ended June 30, 2018, respectively. The effective tax rate was 28 percent and 30 percent for the three and six-month periods ended June 30, 2017. The prior year effective tax rate was different than the 34 percent statutory rate primarily due to state tax expense, net of federal benefit and other permanent differences, including the manufacturer's exemption.

On December 22, 2017, the Tax Cuts and Jobs Act ("The Act") was signed into law by the President of the United States, enacting significant changes to the Internal Revenue Code effective January 1, 2018. The Act included a number of provisions including, but not limited to, a permanent reduction of the U.S. corporate tax rate from a blended 35 percent to 21 percent, eliminating the deduction for domestic production activities, limiting the tax deductibility of interest expense, accelerating the expensing of certain business assets and reducing the amount of executive pay that could qualify as a tax deduction. Many effects of The Act are international in nature, such as the one-time transition tax, base erosion anti-abuse tax and the global intangible low-taxed income tax, and thus would not pertain to the Company as it has no international operations.

In December 2017, the Company recorded \$381,000 of income tax benefit related to adopting various provisions of the Act. Under Staff Accounting Bulletin No. 118 ("SAB 118") our income tax benefit is provisional in nature and is subject to further clarification of the new law, including but not limited to U.S. state conformity that cannot be estimated at this time and measurement of underlying tax basis in certain business assets. The ultimate impact may differ from provisional amounts due to, among other things, additional analysis, changes in interpretations and assumptions the Company has made, and additional regulatory guidance that may be issued. Further guidance may be forthcoming from federal and state agencies, which could result in additional adjustments. The accounting is expected to be completed no later than the filing of the 2017 U.S. corporate income tax return in 2018.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

7. Segment Information

The following table summarizes certain information regarding segments of the Company's operations:

	Three Months Ended		Six Months Ended	
	Jun 30, 2018	Jun 30, 2017	Jun 30, 2018	Jun 30, 2017
Net sales				
Metals Segment	\$56,374,479	\$39,088,322	\$101,866,726	\$68,798,282
Specialty Chemicals Segment	15,519,284	12,422,723	28,507,639	24,916,342
	\$71,893,763	\$51,511,045	\$130,374,365	\$93,714,624
Operating income				
Metals Segment	\$9,090,516	\$2,359,054	\$15,107,047	\$3,923,568
Specialty Chemicals Segment	1,106,672	1,137,911	1,970,161	2,645,371
Unallocated corporate expenses	2,219,618	1,601,026	3,722,339	3,158,098
Acquisition related costs	690,217	386,519	690,217	744,996
Operating income	7,287,353	1,509,420	12,664,652	2,665,845
Interest expense	403,852	341,005	717,835	521,320
Change in fair value of interest rate swaps	(19,255)) 16,927	(92,458)) (24,503)
Earn-out adjustment	2,307,598	(3,391)) 2,461,658	(3,391)
Other loss (income), net	(59,112)) —	29,185	—
Income before income taxes	\$4,654,270	\$1,154,879	\$9,548,432	\$2,172,419
	As of			
	Jun 30, 2018	Dec 31, 2017		
Identifiable assets				
Metals Segment	\$158,144,084	\$130,456,857		
Specialty Chemicals Segment	29,549,710	25,394,078		
Corporate	14,587,879	4,023,215		
	\$202,281,673	\$159,874,150		
Goodwill				
Metals Segment	\$4,648,795	\$4,648,795		
Specialty Chemicals Segment	1,354,730	1,354,730		
	\$6,003,525	\$6,003,525		

8. Fair Value of Financial Instruments

The Company makes estimates of fair value in accounting for certain transactions, in testing and measuring impairment and in providing disclosures of fair value in its condensed consolidated financial statements. The Company determines the fair values of its financial instruments for disclosure purposes by maximizing the use of observable inputs and minimizing the use of unobservable inputs. Fair value disclosures for assets and liabilities are grouped into three levels. The levels prioritize the inputs used to measure the fair value of the assets or liabilities. These levels are:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

Level 2 - Inputs other than quoted prices that are observable for assets and liabilities, either directly or indirectly. These inputs include quoted prices for similar assets or liabilities in active markets or quoted prices for identical or similar assets or liabilities in markets that are less active.

Level 3 - Unobservable inputs that are supported by little or no market activity for assets or liabilities and includes certain pricing models, discounted cash flow methodologies and similar techniques.

The Company's financial instruments include cash and cash equivalents, accounts receivable, derivative instruments, accounts payable, earn-out liabilities, revolving line of credit and equity investments. For short-term instruments, other than those required to be reported at fair value on a recurring basis and for which additional disclosures are included below, management concluded the historical carrying value is a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization. Therefore, as of June 30, 2018 and December 31, 2017, the carrying amount for cash and cash equivalents, accounts receivable, accounts payable and the Company's revolving line of credit, which is based on a variable interest rate, approximates their fair value.

During the second quarter of 2018, the Company recorded a gain on the investment in equity securities of \$59,112 which is included in "Other expense (income)" on the accompanying Condensed Consolidated Statements of Operations. The fair value of equity securities held by the Company as of June 30, 2018 and December 31, 2017 was \$845,000 and \$537,233, respectively, and is included in "Prepaid expenses and other current assets" on the accompanying Consolidated Balance Sheets. The equity securities are classified as a Level 1 financial instrument. The Company has one interest rate swap contract, which is classified as a Level 2 financial instrument as it is not actively traded and is valued using pricing models that use observable market inputs. The fair value of the contract was an asset of \$220,440 and \$127,981 at June 30, 2018 and December 31, 2017, respectively. The interest rate swap was priced using discounted cash flow techniques. Changes in its fair value were recorded to other income (expense) with corresponding offsetting entries to current assets or liabilities, as appropriate. Significant inputs to the discounted cash flow model include projected future cash flows based on projected one-month LIBOR and the average margin for companies with similar credit ratings and similar maturities. It is classified as Level 2 as it is not actively traded and is valued using pricing models that use observable market inputs.

To manage the impact on earnings of fluctuating nickel prices, the Company occasionally enters into six-month forward option contracts, which are classified as Level 2. At June 30, 2018, the Company did not have any such contracts in place. At December 31, 2017, the Company had contracts in place with notional quantities totaling approximately 1,351,494 pounds with strike prices ranging from \$3.75 to \$4.64 per pound. The fair value of the option contract in place at December 31, 2017 was an asset of \$9,027. The fair value of the contracts was priced using discounted cash flows techniques based on forward curves and volatility levels by asset class determined on the basis of observable market inputs, when available. Changes in their fair value were recorded to "Other expense (income)" with corresponding offsetting entries to other current assets. The fair value of the forward option contracts approximates their carrying value.

The fair value of contingent consideration liabilities ("earn-out") resulting from the Bristol Metals-Munhall acquisition discussed in Note 9 is classified as Level 3. The fair value was estimated by applying the Monte Carlo Simulation approach using management's projection of pounds shipped and price per unit. Each quarter-end the Company re-evaluates its assumptions and adjusts to the updated fair value.

The following table presents a summary of changes in fair value of the Company's earn-out liability during the period:

Balance at December 31, 2017	\$4,833,850
Earn-out payments to MUSA	(1,172,065)
Change in fair value during the period	2,461,658
Balance at June 30, 2018	\$6,123,443

There were no transfers of assets or liabilities between Level 1, Level 2 and Level 3 in the three-month or six-month periods ended June 30, 2018 or year ended December 31, 2017. During the first six months of 2018, there have been no changes in the fair value methodologies used by the Company.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

9. Acquisitions

On February 28, 2017, the Company's subsidiary Bristol Metals, LLC ("BRISMET"), acquired the stainless steel pipe and tube assets of MUSA located in Munhall, PA ("Bristol Metals-Munhall").

Bristol Metals-Munhall's results of operations since acquisition are reflected in the Company's consolidated statements of operations as follows:

	Three Months Ended		Six Months Ended	
	Jun 30, 2018	Jun 30, 2017	Jun 30, 2018	Jun 30, 2017
Revenues	\$14,771,010	\$7,299,734	\$25,739,242	\$8,411,926
Pre-tax income (loss)	(38,142)	211,703	1,019,497	390,896

Pre-tax loss for the second quarter of 2018 includes a \$2,307,598 charge related to an increase in the fair value of the stainless steel earn-out liability during the period, as compared to a gain of \$3,391 in the second quarter of 2017. For the six months ended June 30, 2018, charges related to the earn-out liability fair value adjustments totaled \$2,461,658 as compared to a gain of \$3,391 for the six months ended June 30, 2017.

10. Long-term Debt

On June 29, 2018 the Company amended its Credit Agreement with its bank to increase the limit of the asset based line of credit (the "Line") by \$15,000,000 to a maximum of \$80,000,000. As a result of the amendment, the interest rate on the Line is now calculated using One Month LIBOR plus a spread of 1.65 percent. None of the other provisions of the Credit Agreement were changed as a result of this amendment.

Pursuant to the Credit Agreement, the Company is subject to certain covenants including maintaining a minimum fixed charge coverage ratio and a limitation on the Company's maximum amount of capital expenditures per year, which is in line with currently projected needs. At June 30, 2018, the Company was in compliance with all debt covenants.

11. Contingencies

The Company is from time-to-time subject to various claims, possible legal actions for product liability and other damages, and other matters arising out of the normal conduct of the Company's business.

Management is not currently aware of any asserted or unasserted matters which could have a material effect on the financial condition or results of operations of the Company.

12. Leases

On June 29, 2018, the Company and Store Master Funding XII, LLC, an affiliate of Store Capital Corporation ("Store"), entered into an Amended and Restated Master Lease Agreement (the "Master Lease"), pursuant to which the Company will lease the Munhall, PA facility, purchased by Store from MUSA on June 29, 2018, for the remainder of the initial term of 20 years set forth in the Master Lease, with two renewal options of ten years each. The lease includes a rent escalator equal to the lesser of 1.25 times the percentage increase in the Consumer Price Index since the previous increase or 2 percent.

Synalloy Corporation

Notes to Condensed Consolidated Financial Statements (unaudited)

The amount of future minimum lease payments under operating leases are as follows:

Remainder of 2018	\$1,408,869
2019	2,859,865
2020	2,917,062
2021	2,975,404
2022	3,034,912
2023	3,095,610
Thereafter	45,337,403

13. Subsequent Events

On May 29, 2018, BRISMET, a subsidiary of the Company's Metals Segment, entered into an asset purchase agreement to acquire the galvanized tube assets and operations of MUSA located in Munhall, PA. The effective date of the transaction was July 1, 2018, which was funded through an increase to the Company's current credit facility. The purchase price for the transaction totaled \$10,378,281, which was placed into an escrow account on June 29, 2018, and is recorded in "Prepaid expenses and other current assets" on the accompanying Condensed Consolidated Balance Sheet at June 30, 2018. The assets purchased and liabilities assumed from MUSA include accounts receivable, inventory, equipment, and accounts payable. Because the transaction closed on July 1, 2018, the purchase accounting is not complete at the time of this filing.

On August 7, 2018, the Company announced that its Board of Directors has approved an annual dividend of \$0.25 per share, to be paid in December of 2018.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is management's discussion of certain significant factors that affected the Company during the three-month and six-month periods ended June 30, 2018.

Consolidated net sales for the second quarter of 2018 was \$71,893,763, an increase of \$20,382,718 or 40 percent when compared to net sales for the second quarter of 2017 of \$51,511,045. For the second quarter of 2018, the Company recorded net income of \$3,677,272, or \$0.41 per share (diluted), compared to net income of \$829,879 or \$0.10 per share for the same quarter in the prior year.

The second quarter and first six months of 2018 include financial results in the Company's Metals Segment related to the Bristol Metals-Munhall stainless acquisition (which closed on February 28, 2017) as follows:

For the second quarters of 2018 and 2017, net sales for Bristol Metals-Munhall were \$14,771,010 and \$7,299,734, respectively, with operating income of \$2,270,374 and \$247,997, respectively.

For the first six months of 2018 and 2017, net sales for Bristol Metals-Munhall were \$25,739,242 and \$8,411,926, respectively, with operating income of \$3,482,072 and \$444,476, respectively.

Metals Segment

Metals Segment net sales for the second quarter of 2018 totaled \$56,374,479, an increase of \$17,286,157 or 44 percent from the second quarter of 2017. Net sales for the first six months of 2018 were \$101,866,726, an increase of \$33,068,444 or 48 percent from 2017.

Sales for the second quarter and first six months of 2018 compared to the prior year are summarized as follows:

	Sales Increase (decrease) from prior year period			Units shipped
	\$	%	Average selling price ⁽¹⁾	
Second quarter				
Storage tank and vessel	\$3,013,783	49.7%	35.4%	14.3%
Seamless carbon steel pipe and tube	2,012,077	31.5%	25%	6.5%
Stainless steel pipe	12,260,297	46.0%	25.6%	20.4%
Total second quarter change	\$17,286,157			
First six months				
Storage tank and vessel	\$2,515,717	20.4%	24.1%	(3.7)%
Seamless carbon steel pipe and tube	4,723,214	39%	22.2%	16.8%
Stainless steel pipe	25,829,513	58.2%	18.5%	39.7%
Total first 6 months change	\$33,068,444			

⁽¹⁾ Average price increases for the second quarter of 2018 as compared to the second quarter of 2017 primarily relate to the following:

- Storage tank and vessels - product mix change to larger, more complex tanks;
- Seamless carbon steel pipe and tube - pass through of higher mill price input material;
- Stainless steel pipe - pass through of input and cost increases related to:
 - a. Alloy surcharges increase of 10%;
 - b. Alloy mix with higher nickel content cost increase of 7%;
 - c. Base raw material input mill pricing increase of 6%

Average price increases for the first six months of 2018 as compared to the first six months of 2017 relate to the same factors indicated above, however with lower average impacts due to lower material cost inputs in the first quarter of 2018.

The backlog for BRISMET as of June 30, 2018 was \$35,507,218, while the backlog for our subsidiary, Palmer of Texas Inc., totaled \$22,965,205, representing improvements of 50 percent and 28 percent, respectively, over levels at the end of the second quarter in 2017.

The Metals Segment's operating income increased \$6,731,462 to \$9,090,516 for the second quarter of 2018 compared to operating income of \$2,359,054 for the second quarter of 2017. For the first six months of 2018, operating income for the Metals Segment increased \$11,183,479 to an operating profit of \$15,107,047 compared to operating income of \$3,923,568 for the same period of 2017. Current year operating results were affected by the following factors:

1. Nickel prices and resulting surcharges for 304 and 316 alloys continued to rise during the second quarter of 2018, with surcharges for both alloys increasing by \$0.12 and \$0.11 per pound, respectively;
2. Year over year improvements in volume, pricing, and product mix combined for a 57 percent improvement in gross profit margins in the second quarter of 2018 compared to the same quarter in 2017;
3. Seamless carbon pipe and tube showed significant improvement with a 31 percent increase in sales driving a 450 percent improvement in operating profit over the prior year; and
4. The period did benefit from first quarter customer requests for shipments of \$1,329,840 in storage tanks and vessels to be moved into April.

Specialty Chemicals Segment

Net sales for the Specialty Chemicals Segment in the second quarter of 2018 were \$15,519,284, representing a \$3,096,561 or 25 percent increase from the same quarter of 2017. Sales for the first six months of 2018 were \$28,507,639, up \$3,591,297 or 14 percent from 2017 results.

Net sales were impacted during the second quarter and first six months of 2018 primarily from the initial ramp up of seven significant customers, a new fire retardant and new asphalt additive customers at our subsidiary, CRI Tolling, LLC, two new oil and gas customers at our subsidiary, Manufacturers Chemicals, LLC, a new product launch from an existing customer at Manufacturers Chemicals, and the addition of two new pulp/paper coating customers.

Operating income for the Specialty Chemicals Segment for the second quarters of 2018 and 2017 was \$1,106,672 and 1,137,911, respectively. The result was relatively consistent with the second quarter of 2017 on a dollar basis, but slightly lower profit as a percent of sales, at seven percent versus prior year second quarter at nine percent. Similar to what was reported last quarter, the primary difference in operating profit performance compared to prior year second quarter is the relative product mix experienced. The segment historically experiences operating profit in a range between five percent to 12 percent. In 2017, the second quarter represented the middle of that range at nine percent, with the full year averaging to nine percent, close to the average for the past four years. In the first quarter of 2018, operating profit was six percent of sales, close to the low end of historical quarterly performances. In the second quarter of 2018 quarterly performance improved to seven percent; however, annual performance is still expected to be at approximately 10 percent, one percent higher than previous historical averages, primarily related to higher anticipated volumes on a substantially fixed operating cost base.

Other Items

Unallocated corporate expenses for the second quarter of 2018 increased \$618,592, or 39 percent, to \$2,219,618 (three percent of sales) compared to \$1,601,026 (three percent of sales) for the second quarter of 2017. The second quarter increase resulted primarily from: higher professional fees (\$183,017); higher incentive bonus accruals (\$199,950) and; higher salaries and wages (\$81,641).

Acquisition costs were \$721,317 (\$690,217 in unallocated SG&A and \$31,100 in Metals Segment Cost of Sales) for the second quarter of 2018 and \$734,249 (\$690,217 in unallocated SG&A and \$44,032 in Metals Segment Cost of Sales) for the first six months of 2018, resulting primarily from costs associated with the Bristol Metals-Munhall

galvanized acquisition. Acquisition costs were \$554,921 (\$386,519 in unallocated SG&A and \$168,402 in Metals Segment cost of sales) for the second quarter of 2017 and \$1,001,408 (\$744,996 in unallocated SG&A and \$256,413 in Metals Segment cost of sales) for the first six months of 2017 related to the Bristol Metals-Munhall stainless acquisition.

Interest expense was \$403,852 and \$341,005 for the second quarters of 2018 and 2017, respectively, and \$717,835 and \$521,320 for the first six months of 2018 and 2017, respectively. The increase was primarily related to higher average debt outstanding in

the second quarter and first six months of 2018 (as additional borrowings were required to support working capital requirements associated with increased business activity).

During the second quarter of 2018, the Company increased the earn-out liability, resulting from the acquisition of Bristol Metals-Munhall stainless steel business in 2017, by \$2,307,598. The charge represents the present value of future increased earn-out payments due to substantially increased projected sales of small diameter stainless-steel pipe and tube (outside diameter of ten inches or less) for the remainder of the measurement period, which ends in February, 2021. The increase is primarily related to our plans to add ornamental stainless items to our product line.

The effective tax rate was 21 percent for the three-month and six-month periods ended June 30, 2018, respectively.

The Company's effective tax rate is materially equivalent compared to the U.S. statutory rate of 21 percent. The effective tax rate was 28 percent and 30 percent for the three and six-month periods ended June 30, 2017. The 2017 effective tax rate was lower than the 34 percent federal statutory rate primarily due to state tax expense, net of the federal benefit and other permanent differences, including the manufacturer's exemption.

The Company's cash balance increased \$4,244 to \$18,950 as of June 30, 2018 compared to \$14,706 at December 31, 2017. Fluctuations during the period were comprised of the following:

1. On June 29, 2018, the Company placed \$10,378,281 into an escrow account related to the acquisition of the MUSA galvanized business assets;

2. Net accounts receivable increased \$12,666,440 at June 30, 2018 when compared to the prior year end, which resulted from a 32 percent increase in sales for the last two months of the second quarter 2018 compared to the last two months of the fourth quarter 2017. Days sales outstanding, calculated using a three-month average basis, decreased from 51 days outstanding at the end of December 2017 to 49 days at the end of the second quarter 2018;

3. Net inventories increased \$18,445,960 at June 30, 2018 as compared to the prior year-end 2017. The increase, which was primarily related to the Metals Segment, resulted from higher stainless steel surcharges and generally higher replacement costs during the first six months of 2018, and replenishing seamless carbon steel pipe and tube inventory. Inventory turns decreased from 2.51 turns at December 31, 2017, calculated on a three-month average basis, to 2.43 turns at June 30, 2018;

4. Accounts payable increased \$3,100,665 as of June 30, 2018 from the prior year end. The majority of the increase is related to increased levels of purchasing activity across all sectors of the business. Accounts payable days outstanding were approximately 44 days at June 30, 2018 compared to 60 days at December 31, 2017; and

5. Capital expenditures for the first six months of 2018 were \$3,381,925.

The Company drew \$28,020,386 against its Line during the first six months of 2018 and had \$53,933,944 of borrowings outstanding as of June 30, 2018. Covenants under the Credit Agreement include maintaining a minimum fixed charge coverage ratio and a limitation on the Company's maximum amount of capital expenditures per year, which is in line with currently projected needs. The Company was in compliance with all covenants as of June 30, 2018.

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

This quarterly report includes and incorporates by reference "forward-looking statements" within the meaning of the federal securities laws. All statements that are not historical facts are "forward-looking statements." The words "estimate," "project," "intend," "expect," "believe," "should," "anticipate," "hope," "optimistic," "plan," "outlook," "should," "could," "may" and similar expressions identify forward-looking statements. The forward-looking statements are subject to certain risks and uncertainties, including without limitation those identified below, which could cause actual results to differ materially from historical results or those anticipated. Readers are cautioned not to place undue reliance on these forward-looking statements. The following factors could cause actual results to differ materially from historical results or those anticipated: adverse economic conditions; the impact of competitive products and pricing; product demand and acceptance risks; raw material and other increased costs; raw materials availability; employee relations; ability to maintain workforce by hiring trained employees; labor efficiencies; customer delays or difficulties in the production of products; new fracking regulations; a prolonged decrease in oil and nickel prices; unforeseen delays in completing the integrations of acquisitions; risks associated with mergers, acquisitions, dispositions and other expansion activities; financial stability of our customers; environmental issues; unavailability of debt financing on acceptable terms and exposure to increased market interest rate risk; inability to comply with covenants and ratios required by our debt financing arrangements; ability to weather an economic downturn; loss of consumer or investor confidence and other risks detailed from time-to-time in the Company's Securities and Exchange Commission filings. The Company assumes no obligation to update the information included in this report.

Item 3. Quantitative and Qualitative Disclosures about Market Risks

Information about the Company's exposure to market risk was disclosed in its Annual Report on Form 10-K for the year ended December 31, 2017, which was filed with the Securities and Exchange Commission on March 13, 2018. There have been no material quantitative or qualitative changes in market risk exposure since the date of that filing.

Item 4. Controls and Procedures

Based on the evaluation required by 17 C.F.R. Section 240.13a-15(b) or 240.15d-15(b) of the Company's disclosure controls and procedures (as defined in 17 C.F.R. Sections 240.13a-15(e) and 240.15d-15(e)), the Company's Chief Executive Officer and Chief Financial Officer concluded that that such controls and procedures, as of the end of the period covered by this quarterly report, were effective.

Changes in Internal Control over Financial Reporting

The Company's management, including the Chief Executive Officer and Chief Financial Officer, identified no change in the Company's internal control over financial reporting that occurred during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's control over financial reporting.

PART II

Item 1. Legal Proceedings

It is not unusual for us and our subsidiaries to be involved in various unresolved legal actions, administrative proceedings and claims in the ordinary course of business involving, among other things, product liability, commercial, employment, workers' compensation, and environmental matters. We establish reserves in a manner that is consistent with accounting principles generally accepted in the U.S. for costs associated with such matters when a liability is probable and those costs are capable of being reasonably estimated. We cannot predict with any certainty the outcome of these unresolved legal actions or the range of possible loss or recovery. Based on current information, however, we believe that the eventual outcome of these unresolved legal actions, either individually or in the aggregate, will not have a material adverse effect on our financial position, results of operations or cash flows. There were no material changes in our Legal Proceedings, as discussed in Part I, Item 3 in the Company's Annual Report on Form 10-K for the period ending December 31, 2017.

Item 1A. Risk Factors

There were no material changes in our assessment of risk factors as discussed in Part I, Item 1A in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit
No.

Description

- 10.1 Amended and Restated Synalloy Corporation 2015 Stock Awards Plan
- 10.2 Purchase and Sale Agreement, dated as of May 25, 2018, between Marcegaglia USA, Inc. and Bristol Metals, LLC
- 10.3 Agreement to Designate and Lease, dated as of June 29, 2018, between Registrant and Store Capital Acquisitions, LLC
- 10.4 Amended and Restated Master Lease Agreement, dated as of June 29, 2018, between Registrant and Store Master Funding XII, LLC
- 10.5 First Amendment to Third Amended and Restated Loan Agreement, dated as of June 29, 2018, between Registrant and Branch Banking and Trust Company
- 10.6 Asset Purchase Agreement, dated as of June 29, 2018, but with a closing effective date of July 1, 2018, between Bristol Metals, LLC and Marcegaglia USA, Inc.
Amendment No. 2 to Asset Purchase Agreement, dated as of July 1, 2018, between Bristol Metals, LLC and Marcegaglia USA, Inc., amending the Asset Purchase Agreement, dated as of December 9, 2016, between Bristol Metals, LLC and Marcegaglia USA, Inc., as amended by Amendment No. 1 to Asset Purchase Agreement, dated as of February 28, 2017, between Bristol Metals, LLC and Marcegaglia USA, Inc.
- 10.7 Rule 13a-14(a)/15d-14(a) Certifications of Chief Executive Officer
- 31.1 Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer
- 31.2 Certifications Pursuant to 18 U.S.C. Section 1350
- 32 Certifications Pursuant to 18 U.S.C. Section 1350
- 101.INS* XBRL Instance Document
- 101.SCH* XBRL Taxonomy Extension Schema
- 101.CAL* XBRL Taxonomy Extension Calculation Linkbase
- 101.LAB* XBRL Taxonomy Extension Label Linkbase
- 101.PRE* XBRL Taxonomy Extension Presentation Linkbase
- 101.DEF* XBRL Taxonomy Extension Definition Linkbase

* In accordance with Regulation S-T, the XBRL-related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall be deemed "furnished" and not "filed."

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SYNALLOY CORPORATION
(Registrant)

Date: August 7, 2018 By: /s/ Craig C. Bram
Craig C. Bram
President and Chief Executive Officer
(principal executive officer)

Date: August 7, 2018 By: /s/ Dennis M. Loughran
Dennis M. Loughran
Senior Vice President and Chief Financial Officer
(principal accounting officer)

21

ble Note may terminate the automatic extension for less than all of its Renewable Notes only if the terms of the Renewable Note specifically permit partial termination. An election to terminate the automatic extension of any portion of the Renewable Note is not revocable and will be binding on the holder of the Renewable Note. If the holder elects to terminate the automatic extension of the maturity of the Note, the holder will become entitled to the principal and interest accrued up to the Renewal Date. The applicable prospectus supplement or term sheet will identify a final stated maturity.

If a Renewable Note is represented by a global security, DTC or its nominee will be the holder of the Renewable Note and therefore will be the only entity that can exercise a right to terminate the automatic extension of such Renewable Note. In order to ensure that DTC or its nominee will exercise a right to terminate the automatic extension provisions of a particular Renewable Note, the beneficial owner of the Renewable Note must instruct the broker or other DTC participant through which it holds an interest in the Renewable Note to notify DTC of its desire to terminate the automatic extension of the Renewable Note. Different firms have different cut-off times for accepting instructions from their customers and, accordingly, each beneficial owner should consult the broker or other participant through which it holds an interest in a Renewable Note to ascertain the cut-off time by which an instruction must be given for delivery of timely notice to DTC or its nominee. Specific information pertaining to United States federal tax considerations for Renewable Notes will be described in an applicable prospectus supplement or term sheet.

Extendible Notes

We may issue debt securities, which we call Extendible Notes, whose maturity may be extended at our option for one or more whole-year periods (each, an Extension Period), up to but not beyond a final stated maturity described in the applicable prospectus supplement or term sheet.

Table of Contents

We may exercise our option to extend the Extendible Note by notifying the trustee (or any duly appointed paying agent) at least 45 but not more than 60 days prior to the then effective date of maturity. If we elect to extend the Extendible Note, the trustee (or paying agent) will deliver (at least 40 days prior to the then effective date of maturity) to the holder of the Extendible Note a notice (an Extension Notice) informing the holder of our election, the new date of maturity and any updated terms. Upon the mailing of the Extension Notice, the maturity of that Extendible Note will be extended automatically as set forth in the Extension Notice.

However, we may, not later than 20 days prior to the then effective date of maturity of an Extendible Note (or, if that date is not a Business Day, prior to the next Business Day), at our option, establish a higher interest rate, in the case of a Fixed Rate Note, or a higher spread and/or spread multiplier, in the case of a Floating Rate Note, for the Extension Period by delivering or causing the trustee (or paying agent) to deliver notice of such higher interest rate or higher spread and/or spread multiplier to the holder of the Fixed Rate Note or Floating Rate Note, as applicable. The notice will be irrevocable.

If we elect to extend the maturity of an Extendible Note, the holder of the Extendible Note will have the option to instead elect repayment of the Extendible Note by us on the then effective date of maturity. In order for an Extendible Note to be so repaid on the date of maturity, we must receive, at least 15 days but not more than 30 days prior to such date of maturity:

- (1) the Extendible Note with the form Option to Elect Repayment on the reverse of the Extendible Note duly completed; or
- (2) a facsimile transmission, telex or letter from a member of a national securities exchange or the Financial Industry Regulatory Authority (FINRA) or a commercial bank or trust company in the United States setting forth the name of the holder of the Extendible Note, the principal amount of the Extendible Note, the principal amount of the Extendible Note to be repaid, the certificate number or a description of the tenor and terms of the Extendible Note, a statement that the option to elect repayment is being exercised thereby and a guarantee that the Extendible Note be repaid, together with the duly completed form entitled Option to Elect Repayment on the reverse of the Extendible Note, will be received by the trustee (or paying agent) not later than the fifth Business Day after the date of the facsimile transmission, telex or letter; *provided, however*, that the facsimile transmission, telex or letter will only be effective if the Extendible Note and form duly completed are received by the trustee (or paying agent) by that fifth Business Day. The option may be exercised by the holder of an Extendible Note for less than the aggregate principal amount of the Extendible Note then outstanding if the principal amount of the Extendible Note remaining outstanding after repayment is an authorized denomination.

If an Extendible Note is represented by a global security, DTC or its nominee will be the holder of that Extendible Note and therefore will be the only entity that can exercise a right to repayment. To ensure that DTC or its nominee timely exercises a right to repayment with respect to a particular Extendible Note, the beneficial owner of that Extendible Note must instruct the broker or other participant through which it holds an interest in the Extendible Note to notify DTC of its desire to exercise a right of repayment. Different firms have different cut-off times for accepting instructions from their customers and, accordingly, each beneficial owner should consult the broker or other participant through which it holds an interest in an Extendible Note to determine the cut-off time by which an instruction must be given for timely notice to be delivered to DTC or its nominee. Specific information pertaining to United States federal tax considerations for the Extendible Notes will be described in an applicable prospectus supplement or term sheet.

Global Securities

What Is a Global Security? As noted above, we usually will issue debt securities as registered securities in book-entry form only. A global security represents one or any other number of individual debt securities. Generally, all debt securities represented by the same global securities will have the same terms.

Each debt security issued in book-entry form will be represented by a global security that we deposit with, or on behalf of, and register in the name of a financial institution or its nominee that we select. The financial institution

Table of Contents

that we select for this purpose is called the depositary. Unless we specify otherwise in the applicable prospectus supplement or term sheet, The Depositary Trust Company, New York, New York, known as DTC, will be the depositary for all debt securities issued in book-entry form.

A global security may not be transferred to or registered in the name of anyone other than the depositary or its nominee, unless special termination situations arise. We describe those situations below under *Special Situations when a Global Security Will Be Terminated*. As a result of these arrangements, the depositary, or its nominee, will be the sole registered owner and holder of all debt securities represented by a global security, and investors will be permitted to own only beneficial interests in a global security. Beneficial interests must be held by means of an account with a broker, bank or other financial institution that in turn has an account with the depositary or with another institution that has an account with the depositary. Thus, an investor whose security is represented by a global security will not be a holder of the debt security, but only an indirect owner of a beneficial interest in the global security.

Special Considerations for Global Securities. As an indirect holder, an investor's rights relating to a global security will be governed by the account rules of the investor's financial institution and of the depositary, as well as general laws relating to securities transfers. The depositary that holds the global security will be considered the holder of the debt securities represented by the global security.

If debt securities are issued only in the form of a global security, an investor should be aware of the following:

An investor cannot cause the debt securities to be registered in his or her name, and cannot obtain certificates for his or her interest in the debt securities, except in the special situations we describe below.

An investor will be an indirect holder and must look to his or her own bank or broker for payments on the debt securities and protection of his or her legal rights relating to the debt securities, as we describe under *Issuance of Securities in Registered Form* below.

An investor may not be able to sell interests in the debt securities to some insurance companies and other institutions that are required by law to own their securities in non-book-entry form.

An investor may not be able to pledge his or her interest in a global security in circumstances where certificates representing the debt securities must be delivered to the lender or other beneficiary of the pledge in order for the pledge to be effective.

The depositary's policies, which may change from time to time, will govern payments, transfers, exchanges and other matters relating to an investor's interest in a global security. We and the trustee have no responsibility for any aspect of the depositary's actions or for its records of ownership interests in a global security. We and the trustee also do not supervise the depositary in any way.

If we redeem less than all the debt securities of a particular series being redeemed, DTC's practice is to determine by lot the amount to be redeemed from each of its participants holding that series.

An investor is required to give notice of exercise of any option to elect repayment of its debt securities, through its participant, to the trustee and to deliver the related debt securities by causing its participant to transfer its interest in those debt securities, on DTC's records, to the trustee.

DTC requires that those who purchase and sell interests in a global security deposited in its book-entry system use immediately available funds. Your broker or bank may also require you to use immediately available funds when purchasing or selling interests in a global security.

Financial institutions that participate in the depository's book-entry system, and through which an investor holds its interest in a global security, may also have their own policies affecting payments, notices and other matters relating to the debt securities. There may be more than one financial intermediary in the chain of ownership for an investor. We do not monitor and are not responsible for the actions of any of those intermediaries.

Table of Contents

Special Situations When a Global Security Will Be Terminated. In a few special situations described below, a global security will be terminated and interests in it will be exchanged for debt securities of the same series in non-book-entry form (certificated debt securities). After that exchange, the choice of whether to hold the certificated debt securities directly or in street name will be up to the investor. Investors must consult their own banks or brokers to find out how to have their interests in a global security transferred on termination to their own names, so that they will be holders. We have described the rights of holders and street name investors under Issuance of Securities in Registered Form above.

The special situations for termination of a global security are as follows:

if the depositary notifies us that it is unwilling, unable or no longer qualified to continue as depositary for that global security, and we do not appoint another institution to act as depositary within 90 days,

if we notify the trustee that we wish to terminate that global security, or

if an event of default has occurred with regard to the debt securities represented by that global security and has not been cured or waived; we discuss events of defaults later under Events of Default.

The prospectus supplement or term sheet may list situations for terminating a global security that would apply only to the particular series of debt securities covered by the prospectus supplement or term sheet. If a global security is terminated, only the depositary, and neither we nor the trustee, will be responsible for deciding the names of the institutions in whose names the debt securities represented by the global security will be registered and, therefore, who will be the holders of those debt securities.

Payment and Paying Agents

We will pay interest to the person listed in the trustee's records as the owner of the debt security at the close of business on a particular day in advance of each regularly scheduled date for interest, even if that person no longer owns the debt security on the interest due date. That day, typically set at a date approximately two weeks prior to the interest due date, is called the record date. Because we will pay all the interest for an interest period to the holders on the record date, holders buying and selling debt securities must work out between themselves the appropriate purchase price. The most common manner is to adjust the sales price of the debt securities to prorate interest fairly between buyer and seller based on their respective ownership periods within the particular interest period. This prorated interest amount is called accrued interest.

Payments on Global Securities. We will make payments on a global security in accordance with the applicable policies of the depositary as in effect from time to time. Under those policies, we will make payments directly to the depositary, or its nominee, and not to any indirect holders who own beneficial interests in the global security. An indirect holder's right to those payments will be governed by the rules and practices of the depositary and its participants, as described under What Is a Global Security?

Payments on Certificated Debt Securities. We will make payments on a certificated debt security as follows. We will pay interest that is due on an interest payment date by check mailed on the interest payment date to the holder at his or her address shown on the trustee's records as of the close of business on the regular record date. We will make payments of principal and premium, if any, duly and punctually to the office of the trustee.

Alternatively, if the holder asks us to do so, we may pay any amount that becomes due on the debt security by wire transfer of immediately available funds to an account at a bank in New York City, on the due date. To request payment by wire, the holder must give the trustee or other paying agent appropriate transfer instructions at least 15 calendar days before the requested wire payment is due. In the case of any interest payment due on an interest payment date, the instructions must be given by the person who is the holder on the relevant regular record date. Any wire instructions, once properly given, will remain in effect unless and until new instructions are given in the manner described above. In addition, see the description under Interest and Interest Rates.

Table of Contents

Covenant

Consolidation, Merger, Sale or Conveyance. The indenture provides that Legg Mason may not consolidate with or merge into any other entity or convey, transfer or lease its properties and assets as an entirety or substantially as an entirety to any entity, unless:

the successor or transferee entity, if other than Legg Mason, is a corporation organized and existing under the laws of the United States, any state or territory thereof or the District of Columbia and expressly assumes by a supplemental indenture executed and delivered to the trustee, in form reasonably satisfactory to the trustee, the due and punctual payment of the principal of, any premium on and any interest on, all the outstanding debt securities of Legg Mason and the performance of every covenant and obligation in the indenture to be performed or observed by Legg Mason;

immediately after giving effect to the transaction, no Event of Default, as defined in the indenture, and no event which, after notice or lapse of time or both, would become an Event of Default, has happened and is continuing; and

Legg Mason has delivered to the trustee an officer's certificate and an opinion of counsel, each in the form required by the indenture and stating that such consolidation, merger, conveyance, transfer or lease and, if a supplemental indenture is required in connection with such transaction, such supplemental indenture comply with the foregoing provisions relating to such transaction.

In case of any such consolidation, merger, conveyance, transfer or lease, the successor entity will succeed to and be substituted for Legg Mason as obligor on the debt securities with the same effect as if it had been named in the indenture as Legg Mason.

Events of Default

An Event of Default with respect to the debt securities of any series is defined in the indenture as:

(a) default in the payment of any interest on debt securities of that series when such interest becomes due and payable, and continuance of such default for a period of 30 days; or

(b) default in the payment of the principal of (or premium, if any, on) debt securities of that series at its maturity or upon redemption or repayment when the same becomes due and payable; or

(c) default in the performance, or breach, of any covenant or warranty of Legg Mason in respect of the debt securities of that series (other than a covenant or warranty a default in the performance of which or the breach of which is specifically dealt with elsewhere in clauses (a), (b), (d), (e) or (f) of this section), and continuance of such default or breach for a period of 60 days after there has been given, by registered or certified mail, to Legg Mason by the trustee or to Legg Mason and the trustee by the holders of at least 25% in aggregate principal amount of the outstanding debt securities of that series a written notice specifying such default or breach and requiring it to be remedied and stating that such notice is a Notice of Default under the indenture; or

(d) a default under any indebtedness for money borrowed by Legg Mason or any of its subsidiaries that results in the acceleration of the maturity of such indebtedness, or failure to pay any such indebtedness at maturity, in an aggregate amount of at least \$50.0 million or its foreign currency equivalent at the time and such acceleration has not been rescinded or annulled, or indebtedness paid, within 30 days after notice to Legg Mason by the trustee (to be provided by it promptly after a responsible officer of the trustee receives written notice of such default) or notice to Legg Mason and the trustee by holders of 25% or more of the then outstanding debt securities of that series; or

(e) certain events of bankruptcy, insolvency and reorganization of Legg Mason; or

(f) any other event of default provided in the prospectus supplement with respect to the debt securities of that series.

Table of Contents

The indenture provides that:

if an event of default described in clause (a), (b), (c), (d) or (f) above has occurred and is continuing, either the trustee or the holders of not less than 25% in aggregate principal amount of the debt securities of the applicable series may declare the principal amount of the debt securities then outstanding, and any accrued and unpaid interest through the date of such declaration, to be due and payable immediately;

upon certain conditions such declarations may be annulled and past defaults (except for defaults in the payment of principal of, or any premium or interest on, the debt securities and in compliance with certain covenants) may be waived by the holders of a majority in aggregate principal amount of the debt securities of the applicable series; and

if an event of default described in clause (e) occurs and is continuing, then the principal amount of all debt securities issued under the indenture, together with any accrued interest through the occurrence of such event, shall become and be due and payable immediately, without any declaration or other act by the trustee or any other holder.

Under the indenture, the trustee must give to the holders of debt securities of any series notice of all uncured defaults known to it with respect to the debt securities of such series within 90 days after such a default occurs (the term default to include the events specified above without notice or grace periods); *provided that*, except in the case of default in the payments of principal of, or any premium or interest on, any of the debt securities of such series, the trustee will be protected in withholding such notice if it in good faith determines that the withholding of such notice is in the best interest of the holders of such debt securities.

No holder of any debt securities of any series may institute any action under the indenture unless:

such holder has given the trustee written notice of a continuing event of default with respect to the debt securities of that series;

the holders of not less than 25% in aggregate principal amount of the outstanding debt securities of that series have requested the trustee to institute proceedings in respect of such event of default;

such holder or holders have offered the trustee such reasonable indemnity as the trustee may require;

the trustee has failed to institute an action for 60 days thereafter; and

no inconsistent direction has been given to the trustee during such 60-day period by the holders of a majority in aggregate principal amount of the debt securities of such series (or all series in the case of an event of default described in clause (e) above).

The holders of a majority in aggregate principal amount of the debt securities of any series will have the right, subject to certain limitations, to direct the time, method and place of conducting any proceeding for any remedy available to the trustee or exercising any trust or power conferred on the trustee with respect to the debt securities of such series. The indenture provides that, if an event of default occurs and is continuing, the trustee, in exercising its rights and powers under the indenture, will be required to use the degree of care of a prudent man in the conduct of his own affairs. The indenture further provides that the trustee shall not be required to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties under the indenture unless it has reasonable grounds for believing that repayment of such funds or adequate indemnity against such risk or liability is reasonably assured to it.

Legg Mason must furnish to the trustee within 120 days after the end of each fiscal year a statement signed by an officer thereof to the effect that a review of our activities during such year and our performance under the indenture and the terms of the debt securities has been made, and, to the knowledge of the signatories based on such review, we have complied with all conditions and covenants of the indenture or, if we are in default, specifying such default.

Table of Contents

Modification of the Indenture

We and the trustee may, without the consent of the holders of the debt securities issued under the indenture, enter into supplemental indentures for, among others, one or more of the following purposes:

to evidence the succession of another person to Legg Mason and the assumption by any such successor of the covenants of Legg Mason contained in the indenture and in the debt securities in accordance with the provisions described above under Covenant Consolidation, Merger, Sale or Conveyance ; or

to add to the covenants of Legg Mason for the benefit of the holders of all or any series of debt securities (and if such covenants are to be for the benefit of less than all series of debt securities, stating that such covenants are being included solely for the benefit of such series) or to surrender any right or power in the indenture conferred upon Legg Mason; or

to add any additional events of default for the benefit of the holders of all or any series of debt securities (and if such events of default are to be for the benefit of less than all series of debt securities, stating that such events of default are being included solely for the benefit of such series); or

to change or eliminate any of the provisions of the indenture; *provided* that any such change or elimination shall become effective only when there is no debt security outstanding of any series created prior to the execution of such supplemental indenture which is entitled to the benefit of any such provision; or

to establish the form or terms of debt securities of any series as permitted by the indenture, including the provisions and procedures relating to debt securities convertible into or exchangeable for any securities of any person (including Legg Mason); or

to evidence and provide for the acceptance of appointment under the indenture by a successor trustee with respect to the debt securities of one or more series and to add to or change any of the provisions of the indenture as shall be necessary to provide for or facilitate the administration of the trusts hereunder by more than one trustee, pursuant to the requirements of the indenture; or

to cure any ambiguity, to correct or supplement any provision in the indenture which may be inconsistent with any other provision in the indenture, or to make any other provisions with respect to matters or questions arising under the indenture, *provided* such action shall not adversely affect the interests of the holders of debt securities of any series in any material respect; or

to supplement any of the provisions of the indenture to such extent as shall be necessary to permit or facilitate the defeasance and discharge of any series of debt securities pursuant to the provisions described under Defeasance ; *provided* that any such action shall not adversely affect the interests of the holders of debt

securities of such series or any other series of debt securities in any material respect.

With certain exceptions, the indenture or the rights of the holders of the debt securities may be modified by us and the trustee with the consent of the holders of a majority in aggregate principal amount of the debt securities then outstanding affected thereby, but no such modification may be made without the consent of the holder of each outstanding note affected thereby that would:

change the maturity of the principal of, or any premium on, or any installment of principal of or interest on any debt securities, or reduce the principal amount or any premium or the rate or manner of calculating interest or any premium payable upon redemption or repayment of any debt securities, or change the dates or periods for any redemption or repayment or change any place of payment where, or the coin or currency in which, any principal, premium or interest is payable, or impair the right to institute suit for the enforcement of any such payment on or after the maturity thereof (or, in the case of redemption or repayment, on or after the redemption or repayment date);

Table of Contents

reduce the percentage in principal amount of the outstanding debt securities, the consent of whose holders is required for any such modification, or the consent of whose holders is required for any waiver of compliance with certain provisions of the indenture or certain defaults thereunder and their consequences provided for in the indenture; or

modify any of the provisions of certain sections of the indenture, including the provisions summarized in this paragraph, except to increase any such percentage or to provide that certain other provisions of the indenture cannot be modified or waived without the consent of the holder of each of the outstanding debt securities affected thereby.

Defeasance

The following provisions will be applicable to each series of debt securities unless we state in the applicable prospectus supplement or term sheet that the provisions of covenant defeasance and full defeasance will not be applicable to that series.

Covenant Defeasance. Under current United States federal tax law, Legg Mason can make the deposit described below and be released from some of the restrictive covenants in the indenture under which the particular series was issued. This is called covenant defeasance. In that event, you would lose the protection of those restrictive covenants but would gain the protection of having money and government securities set aside in trust to repay your debt securities. In order to achieve covenant defeasance, we must do the following:

Deposit in trust for the benefit of all holders of such debt securities a combination of money and government or government agency debt securities or bonds in the relevant currency that will generate enough cash to make interest, principal and any other payments on the debt securities of such series in the relevant currency on their various due dates.

Deliver to the trustee a legal opinion of our counsel confirming that, under current United States federal income tax law, we may make the above deposit without causing you to be taxed on the debt securities of such series any differently than if we did not make the deposit and just repaid such debt securities ourselves at maturity.

If we accomplish covenant defeasance, you can still look to us for repayment of the debt securities if there were a shortfall in the trust deposit or the trustee is prevented from making payment. In fact, if one of the remaining Events of Default occurred (such as our bankruptcy) and the debt securities became immediately due and payable, there might be a shortfall. Depending on the event causing the default, you may not be able to obtain payment of the shortfall.

Full Defeasance. If there is a change in United States federal tax law, as described below, we can legally release ourselves from all payment and other obligations on the debt securities of a particular series (called full defeasance) if we put in place the following other arrangements for you to be repaid:

We must deposit in trust for the benefit of all holders of the debt securities of such series a combination of money and government or government agency debt securities or bonds in the relevant currency that will generate enough cash to make interest, principal and any other payments on the debt securities of such series

in the relevant currency on their various due dates.

We must deliver to the trustee a legal opinion confirming that there has been a change in current United States federal tax law or an Internal Revenue Service ruling that allows us to make the above deposit without causing you to be taxed on the debt securities of such series any differently than if we did not make the deposit and just repaid such debt securities ourselves at maturity. Under current United States federal tax law, the deposit and our legal release from the debt securities of such series would be treated as though we paid you your share of the cash and debt securities or bonds at the time the cash and debt securities or bonds were deposited in trust in exchange for your debt securities and you would recognize gain or loss on your debt securities at the time of the deposit.

Table of Contents

If we ever did accomplish full defeasance, as described above, you would have to rely solely on the trust deposit for repayment of the debt securities of such series. You could not look to us for repayment in the unlikely event of any shortfall. Conversely, the trust deposit would most likely be protected from claims of our lenders and other creditors if we ever became bankrupt or insolvent.

Covenant defeasance and full defeasance are both subject to certain conditions, such as no default or Event of Default occurring and continuing, and that such defeasance does not result in a breach or violation of, constitute a default under, any material agreement or instrument (other than the indenture) to which Legg Mason or any of its subsidiaries is a party or is bound.

Discharge of the Indenture

We may satisfy and discharge our obligations under the indenture by delivering to the trustee for cancellation all outstanding debt securities or by depositing with the trustee or the paying agent after the debt securities have become due and payable, whether at stated maturity, or any redemption or repayment date, or otherwise, cash sufficient to pay all of the outstanding debt securities and paying all other sums payable under the indenture.

Form, Exchange and Transfer of Certificated Debt Securities

If registered debt securities cease to be issued in book-entry form, they will be issued:

only in fully registered certificated form,

without interest coupons, and

unless we indicate otherwise in the prospectus supplement or term sheet, in a minimum denomination of \$2,000 and amounts above the minimum denomination that are integral multiples of \$1,000.

Holders may exchange their certificated debt securities for smaller denominations or combined into fewer debt securities of larger denominations, as long as the total principal amount is not changed.

Holders may exchange or transfer their certificated debt securities at the office of the trustee. We have appointed the trustee to act as our agent for registering debt securities in the names of holders transferring debt securities. We may appoint another entity to perform these functions or perform them ourselves.

Holders will not be required to pay a service charge to transfer or exchange their certificated securities, but they may be required to pay any tax or other governmental charge associated with the transfer or exchange. The transfer or exchange will be made only if our transfer agent is satisfied with the holder's proof of legal ownership.

If we have designated additional transfer agents for your debt security, they will be named in the applicable prospectus supplement or term sheet. We may appoint additional transfer agents or cancel the appointment of any particular transfer agent. We may also approve a change in the office through which any transfer agent acts.

If any certificated debt securities of a particular series are redeemable and we redeem less than all the debt securities of that series, we may block the transfer or exchange of those debt securities during the period beginning 15 days

before the day we deliver the notice of redemption and ending on the day of that delivery, in order to freeze the list of holders to prepare the delivery. We may also refuse to register transfers or exchanges of any certificated debt securities selected for redemption, except that we will continue to permit transfers and exchanges of the unredeemed portion of any debt security that will be partially redeemed.

If a registered debt security is issued in book-entry form, only the depositary will be entitled to transfer and exchange the debt security as described in this subsection, since it will be the sole holder of the debt security.

Table of Contents

Resignation of Trustee

The trustee may resign or be removed at any time with respect to one or more series of indenture securities; *provided* that a successor trustee is appointed to act with respect to such series. In the event that two or more persons are acting as trustee with respect to different series of indenture securities under the indenture, each of the trustees will be a trustee of a trust separate and apart from the trust administered by any other trustee.

The Trustee Under the Indenture

The Bank of New York Mellon may be one of a number of banks with which we maintain ordinary banking relationships and from which we may obtain credit facilities and lines of credit in the future. The Bank of New York Mellon may also serve as trustee under other indentures under which we are the obligor in the future (including the junior subordinated note indenture). The trustee shall be under no obligation to exercise any of the rights or powers vested in it by the indenture at the request or direction of any of the holders of debt securities of any series pursuant to the indenture, unless such holders shall have offered to the trustee security or indemnity reasonably satisfactory to the trustee against the costs, expenses and liabilities which might be incurred by it in compliance with such request or direction.

Certain Considerations Relating to Foreign Currencies

Debt securities denominated or payable in foreign currencies may entail significant risks. These risks include the possibility of significant fluctuations in the foreign currency markets, the imposition or modification of foreign exchange controls and potential illiquidity in the secondary market. These risks will vary depending upon the currency or currencies involved and will be more fully described in the applicable prospectus supplement or term sheet.

Junior Subordinated Debt Securities

Set forth below is a description of the general terms of the junior subordinated debt securities (the "junior subordinated notes"). The following description does not purport to be complete and is subject to, and is qualified in its entirety by reference to, the junior subordinated note indenture to be entered into between Legg Mason, as issuer and The Bank of New York Mellon, as trustee (the "junior subordinated note trustee") as supplemented from time to time, the "junior subordinated note indenture", a form of which is filed herewith as Exhibit 4.2. The terms of the junior subordinated notes will include those stated in the junior subordinated note indenture and those made a part of the junior subordinated note indenture by reference to the TIA. Certain capitalized terms used in this prospectus and not defined in this prospectus are defined in the junior subordinated note indenture.

The junior subordinated note indenture is subject to and governed by the TIA. The terms "we", "our" and "us", when used to refer to an issuer of junior subordinated notes, means Legg Mason.

General

The junior subordinated notes will be issued as unsecured junior subordinated notes under the junior subordinated note indenture. The junior subordinated note indenture does not limit the aggregate principal amount of junior subordinated notes that may be issued under the junior subordinated note indenture and provides that junior subordinated notes may be issued from time to time in one or more series pursuant to an indenture supplemental to the junior subordinated note indenture. The junior subordinated note indenture gives Legg Mason the ability to reopen a previous issue of junior subordinated notes and issue additional junior subordinated notes of such series, unless otherwise provided.

Table of Contents

Reference is made to the prospectus supplement and the term sheet that will accompany this prospectus for the following terms of the series of junior subordinated notes being offered by such prospectus supplement or term sheet:

the title of such junior subordinated notes;

any limit on the aggregate principal amount of such junior subordinated notes;

the date or dates on which the principal of such junior subordinated notes is payable;

the rate or rates at which such junior subordinated notes shall bear interest, if any, or any method by which such rate or rates will be determined, the date or dates from which such interest will accrue, the interest payment dates on which such interest shall be payable, and the regular record date for the interest payable on any interest payment date;

the place or places where the principal of, premium, if any, on and interest, if any, on such junior subordinated notes shall be payable;

the period or periods within which, the price or prices at which and the terms and conditions on which such junior subordinated notes may be redeemed, in whole or in part, at the option of Legg Mason or at the option of the holder prior to their maturity;

the obligation, if any, of Legg Mason to redeem or purchase such junior subordinated notes;

the date or dates, if any, after which such junior subordinated notes may be converted or exchanged at the option of the holder into or for shares of common stock of Legg Mason and the terms for any such conversion or exchange;

the denominations in which such junior subordinated notes shall be issuable;

if other than the principal amount of the junior subordinated notes, the portion of the principal amount of such junior subordinated notes which shall be payable upon declaration of acceleration of the maturity of such junior subordinated notes;

any deletions from, modifications of or additions to the Events of Default or covenants of Legg Mason as provided in the junior subordinated note indenture pertaining to such junior subordinated notes;

whether such junior subordinated notes shall be issued in whole or in part in the form of a Global Security;

the right, if any, of Legg Mason to extend the interest payment periods of such junior subordinated notes;
and

any other terms of such junior subordinated notes.

The junior subordinated note indenture does not contain provisions that afford holders of junior subordinated notes protection in the event of a highly leveraged transaction involving Legg Mason.

Subordination

The junior subordinated notes are subordinated and junior in right of payment to all Senior Indebtedness (as defined below) of Legg Mason. No payment of principal of (including redemption payments, if any), premium, if any, on or interest on (including Additional Interest (as defined below)) the junior subordinated notes may be made if (a) any Senior Indebtedness is not paid when due and any applicable grace period with respect to such default has ended with such default not being cured or waived or otherwise ceasing to exist, or (b) the maturity of any Senior Indebtedness has been accelerated because of a default, or (c) notice has been given of the exercise of an option to require repayment, mandatory payment or prepayment or otherwise of the Senior Indebtedness. Upon any payment or distribution of assets of Legg Mason to creditors upon any liquidation, dissolution, winding-up, reorganization, assignment for the benefit of creditors, marshalling of assets or liabilities, or any

Table of Contents

bankruptcy, insolvency or similar proceedings of Legg Mason, the holders of Senior Indebtedness shall be entitled to receive payment in full of all amounts due or to become due on or in respect of all Senior Indebtedness before the holders of the junior subordinated notes are entitled to receive or retain any payment or distribution. Subject to the prior payment of all Senior Indebtedness, the rights of the holders of the junior subordinated notes will be subrogated to the rights of the holders of Senior Indebtedness to receive payments and distributions applicable to such Senior Indebtedness until all amounts owing on the junior subordinated notes are paid in full.

The term **Senior Indebtedness** means, with respect to Legg Mason, (i) any payment due in respect of indebtedness of Legg Mason, whether outstanding at the date of execution of the junior subordinated note indenture or incurred, created or assumed after such date, (a) in respect of money borrowed (including any financial derivative, hedging or futures contract or similar instrument) and (b) evidenced by securities, debentures, bonds, notes or other similar instruments issued by Legg Mason that, by their terms, are senior or senior subordinated debt securities including, without limitation, all such obligations under its indentures with various trustees; (ii) all capital lease obligations; (iii) all obligations issued or assumed as the deferred purchase price of property, all conditional sale obligations and all obligations of Legg Mason under any title retention agreement (but excluding trade accounts payable arising in the ordinary course of business and long-term purchase obligations); (iv) all obligations for the reimbursement of any letter of credit, banker's acceptance, security purchase facility or similar credit transaction; (v) all obligations of the type referred to in clauses (i) through (iv) above of other persons the payment of which Legg Mason is responsible or liable as obligor, guarantor or otherwise; and (vi) all obligations of the type referred to in clauses (i) through (v) above of other persons secured by any lien on any property or asset of Legg Mason (whether or not such obligation is assumed by Legg Mason), except for (1) any such indebtedness that is by its terms subordinated to or that ranks equally with the junior subordinated notes and (2) any unsecured indebtedness between or among Legg Mason or its affiliates. Such Senior Indebtedness shall continue to be Senior Indebtedness and be entitled to the benefits of the subordination provisions contained in the junior subordinated note indenture irrespective of any amendment, modification or waiver of any term of such Senior Indebtedness.

The junior subordinated note indenture does not limit the aggregate amount of Senior Indebtedness that may be issued by Legg Mason. As of December 31, 2015, Senior Indebtedness of Legg Mason aggregated to approximately \$1.1 billion. Since Legg Mason is a holding company, the right of Legg Mason and, hence, the right of creditors of Legg Mason (including holders of senior debt securities and junior subordinated notes) to participate in any distribution of the assets of any subsidiary of Legg Mason, whether upon liquidation, reorganization or otherwise, is subject to prior claims of creditors and preferred and preferences stockholders of each subsidiary. As of December 31, 2015, on a consolidated basis, Legg Mason had approximately \$1.1 billion of outstanding long-term debt (including securities due within one year), of which none was long-term debt of Legg Mason's subsidiaries (including securities due within one year).

Additional Interest

Additional Interest is defined in the junior subordinated note indenture as (i) such additional amounts as may be required so that the net amounts received and retained by the holder (if the holder is a securities trust) after paying taxes, duties, assessments or governmental charges of whatever nature (other than withholding taxes) imposed by the United States or any other taxing authority will not be less than the amounts the holder would have received had no such taxes, duties, assessments, or other governmental charges been imposed; and (ii) any interest not paid on an interest payment date (whether by virtue of deferral or extension, or otherwise), together with interest thereon from such interest payment date to the date of payment, compounded quarterly (or, if specified in the prospectus supplement or term sheet for an offering of a particular series of junior subordinated notes, semi-annually), on each interest payment date.

Table of Contents

Events of Default

The junior subordinated note indenture provides that any one or more of the following described events with respect to the junior subordinated notes of any series, which has occurred and is continuing, constitutes an Event of Default with respect to the junior subordinated notes of such series:

default in the payment of any interest upon any junior subordinated note of that series when it becomes due and payable on an interest payment date other than at maturity, including Additional Interest (as defined in clause (ii) of the definition thereof) in respect thereof, and continuance of such default for a period of thirty (30) days; provided, however, that (i) a valid extension of the interest payment period by Legg Mason pursuant to the terms of a supplemental indenture authorizing the junior subordinated notes of that series shall not constitute a default in the payment of interest for this purpose and (ii) no such default shall be deemed to exist if, on or prior to the date on which such interest became due, Legg Mason shall have made a payment sufficient to pay such interest pursuant to the guarantee related to the trust securities of the securities trust owning such series of junior subordinated notes, and shall have delivered a notice to the trustee to that effect; or

default in payment of Additional Interest (as defined in clause (i) of the definition thereof) and the continuance of such default for a period of thirty (30) days; or

default in the payment of the principal of (or premium, if any), or interest (including Additional Interest defined in clause (ii) of the definition thereof) on, any junior subordinated note of that series at its maturity; provided, however, that no such default in the payment of principal (or premium, if any) or interest (including Additional Interest as defined in clause (ii) of the definition thereof) shall be deemed to exist if, on or prior to the date such principal (and premium, if any) or interest (including Additional Interest as defined in clause (ii) of the definition thereof) became due, Legg Mason shall have made a payment sufficient to pay such principal (and premium, if any) or interest (including Additional Interest as defined in clause (ii) of the definition thereof) pursuant to the guarantee related to the trust securities of the securities trust owning such series of junior subordinated notes, and shall have delivered a notice to the trustee to that effect; or

default in the deposit of any sinking fund payment, when and as due by the terms of a junior subordinated note of that series and continuance of such default for a period of three business days; or

default in the performance or breach of any covenant or warranty of Legg Mason in the junior subordinated note indenture (other than a covenant or warranty a default in whose performance or whose breach is elsewhere in this paragraph specifically dealt with or which has expressly been included in the junior subordinated note indenture solely for the benefit of one or more series of junior subordinated notes other than that series), and continuance of such default or breach for a period of 60 days after there has been given, by registered or certified mail, to Legg Mason by the trustee, or to Legg Mason and the trustee by the holders of at least 25% in principal amount of the outstanding junior subordinated notes of that series, a written notice specifying such default or breach and requiring it to be remedied and stating that such notice is a

Notice of Default under the junior subordinated note indenture; or

certain events of bankruptcy, insolvency or reorganization of Legg Mason; or

any other event of default provided with respect to junior subordinated notes of that series in the supplemental indenture authorizing such series.

The holders of not less than a majority in aggregate outstanding principal amount of the junior subordinated notes of any series have the right to direct the time, method and place of conducting any proceeding for any remedy available to the junior subordinated note trustee with respect to the junior subordinated notes of such series. If a junior subordinated note indenture Event of Default occurs and is continuing with respect to the junior subordinated notes of any series, then the junior subordinated note trustee or the holders of not less than 25% in aggregate outstanding principal amount of the junior subordinated notes of such series may declare the principal

Table of Contents

amount of the junior subordinated notes due and payable immediately by notice in writing to Legg Mason (and to the junior subordinated note trustee if given by the holders), and upon any such declaration such principal amount shall become immediately due and payable. At any time after such a declaration of acceleration with respect to the junior subordinated notes of any series has been made and before a judgment or decree for payment of the money due has been obtained as provided in Article Five of the junior subordinated note indenture, the holders of not less than a majority in aggregate outstanding principal amount of the junior subordinated notes of such series may, by written notice to Legg Mason and the junior subordinated note trustee, rescind and annul such declaration and its consequences if the default has been cured or waived and Legg Mason has paid or deposited with the junior subordinated note trustee a sum sufficient to pay all matured installments of interest (including any Additional Interest) and principal due otherwise than by acceleration and all sums paid or advanced by the junior subordinated note trustee, including reasonable compensation and expenses of the junior subordinated note trustee.

The holders of not less than a majority in aggregate outstanding principal amount of the junior subordinated notes of any series may, on behalf of the holders of all the junior subordinated notes of such series, waive any past default with respect to such series, except (i) a default in the payment of principal or interest or (ii) a default in respect of a covenant or provision which under Article Nine of the junior subordinated note indenture cannot be modified or amended without the consent of the holder of each outstanding junior subordinated note of such series affected.

Defeasance

The following provisions will be applicable to each series of junior subordinated notes unless we state in the applicable prospectus supplement or term sheet that the provisions of covenant defeasance and full defeasance will not be applicable to that series.

Covenant Defeasance. Under current United States federal tax law, Legg Mason can make the deposit described below and be released from some of the restrictive covenants in the indenture under which the particular series was issued. This is called covenant defeasance. In that event, you would lose the protection of those restrictive covenants but would gain the protection of having money and government securities set aside in trust to repay your junior subordinated notes. In order to achieve covenant defeasance, we must do the following:

Deposit in trust for the benefit of all holders of such junior subordinated notes a combination of money and government or government agency debt securities or bonds in the relevant currency that will generate enough cash to make interest, principal and any other payments on the junior subordinated notes of such series in the relevant currency on their various due dates.

Deliver to the junior subordinated note trustee a legal opinion of our counsel confirming that, under current United States federal income tax law, we may make the above deposit without causing you to be taxed on the junior subordinated notes of such series any differently than if we did not make the deposit and just repaid such junior subordinated notes ourselves at maturity.

If we accomplish covenant defeasance, you can still look to us for repayment of the junior subordinated notes if there were a shortfall in the trust deposit or the junior subordinated note trustee is prevented from making payment. In fact, if one of the remaining Events of Default occurred (such as our bankruptcy) and the junior subordinated notes became immediately due and payable, there might be a shortfall. Depending on the event causing the default, you may not be able to obtain payment of the shortfall.

Full Defeasance. If there is a change in United States federal tax law, as described below, we can legally release ourselves from all payment and other obligations on the junior subordinated notes of a particular series (called full defeasance) if we put in place the following other arrangements for you to be repaid:

We must deposit in trust for the benefit of all holders of the junior subordinated notes of such series a combination of money and government or government agency debt securities or bonds in the relevant

Table of Contents

currency that will generate enough cash to make interest, principal and any other payments on the junior subordinated notes of such series in the relevant currency on their various due dates.

We must deliver to the junior subordinated note trustee a legal opinion confirming that there has been a change in current United States federal tax law or an Internal Revenue Service ruling that allows us to make the above deposit without causing you to be taxed on the junior subordinated notes of such series any differently than if we did not make the deposit and just repaid such junior subordinated notes ourselves at maturity. Under current United States federal tax law, the deposit and our legal release from the junior subordinated notes of such series would be treated as though we paid you your share of the cash and junior subordinated notes or bonds at the time the cash and junior subordinated notes or bonds were deposited in trust in exchange for your junior subordinated notes and you would recognize gain or loss on your junior subordinated notes at the time of the deposit.

If we ever did accomplish full defeasance, as described above, you would have to rely solely on the trust deposit for repayment of the junior subordinated notes of such series. You could not look to us for repayment in the unlikely event of any shortfall. Conversely, the trust deposit would most likely be protected from claims of our lenders and other creditors if we ever became bankrupt or insolvent.

Covenant defeasance and full defeasance are both subject to certain conditions, such as no default or Event of Default occurring and continuing, and that such defeasance does not result in a breach or violation of, constitute a default under, any material agreement or instrument (other than the junior subordinated note indenture) to which Legg Mason or any of its subsidiaries is a party or is bound.

Discharge of the Junior Subordinated Note Indenture

We may satisfy and discharge our obligations under the junior subordinated note indenture by delivering to the junior subordinated note trustee for cancellation all outstanding junior subordinated notes or by depositing with the junior subordinated note trustee or the paying agent after the junior subordinated notes have become due and payable, whether at stated maturity, or any redemption or repayment date, or otherwise, cash sufficient to pay all of the outstanding junior subordinated notes and paying all other sums payable under the junior subordinated note indenture.

Registration and Transfer

Legg Mason shall not be required to (i) issue, register the transfer of or exchange junior subordinated notes of any series during a period of 15 days immediately preceding the date notice is given identifying the junior subordinated notes of such series called for redemption or (ii) issue, register the transfer of or exchange any junior subordinated notes so selected for redemption, in whole or in part, except the unredeemed portion of any junior subordinated note being redeemed in part.

Payment and Paying Agent

Unless otherwise indicated in an applicable prospectus supplement, payment of principal of any junior subordinated notes will be made only against surrender to the Paying Agent of such junior subordinated notes. Principal of and interest on junior subordinated notes will be payable, subject to any applicable laws and regulations, at the office of such Paying Agent or Paying Agents as Legg Mason may designate from time to time, except that, at the option of Legg Mason, payment of any interest may be made by wire transfer or other electronic transfer or by check mailed to the address of the person entitled to an interest payment as such address shall appear in the Security Register with respect to the junior subordinated notes. Payment of interest on junior subordinated notes on any interest payment date

will be made to the person in whose name the junior subordinated notes (or predecessor security) are registered at the close of business on the record date for such interest payment.

Table of Contents

Unless otherwise indicated in an applicable prospectus supplement or term sheet, the junior subordinated note trustee will act as Paying Agent with respect to the junior subordinated notes. Legg Mason may at any time designate additional Paying Agents or rescind the designation of any Paying Agents or approve a change in the office through which any Paying Agent acts.

All moneys paid by Legg Mason to a Paying Agent for the payment of the principal of or interest on the junior subordinated notes of any series which remain unclaimed at the end of two years after such principal or interest shall have become due and payable will be repaid to Legg Mason, and the holder of such junior subordinated notes will from that time forward look only to Legg Mason for payment of such principal and interest.

Modification

The junior subordinated note indenture contains provisions permitting Legg Mason and the junior subordinated note trustee, with the consent of the holders of not less than a majority in principal amount of the outstanding junior subordinated notes of each series that is affected, to modify the junior subordinated note indenture or the rights of the holders of the junior subordinated notes of such series; *provided* that no such modification may, without the consent of the holder of each outstanding junior subordinated note that is affected, (i) change the stated maturity of the principal of, or any installment of principal of or interest on, any junior subordinated note, or reduce the principal amount of any junior subordinated note or the rate of interest (including Additional Interest) on any junior subordinated note or any premium payable upon the redemption of any junior subordinated note, or change the method of calculating the rate of interest on any junior subordinated note, or impair the right to institute suit for the enforcement of any such payment on or after the stated maturity of any junior subordinated note (or, in the case of redemption, on or after the redemption date), or (ii) reduce the percentage of principal amount of the outstanding junior subordinated notes of any series, the consent of whose holders is required for any such supplemental indenture, or the consent of whose holders is required for any waiver (of compliance with certain provisions of the junior subordinated note indenture or certain defaults under the junior subordinated note indenture and their consequences) provided for in the junior subordinated note indenture, or (iii) modify any of the provisions of the junior subordinated note indenture relating to supplemental indentures, waiver of past defaults or waiver of certain covenants, except to increase any such percentage or to provide that certain other provisions of the junior subordinated note indenture cannot be modified or waived without the consent of the holder of each outstanding junior subordinated note that is affected, or (iv) modify the provisions of the junior subordinated note indenture with respect to the subordination of the junior subordinated notes in a manner adverse to such holder.

In addition, Legg Mason and the junior subordinated note trustee may execute, without the consent of any holders of junior subordinated notes, any supplemental indenture for any of the following purposes:

to evidence the succession of another corporation to Legg Mason and the assumption by any such successor of the covenants of Legg Mason in the junior subordinated note indenture and in the junior subordinated notes; or

to add to the covenants of Legg Mason for the benefit of the holders of all or any series of junior subordinated notes (and if such covenants are to be for the benefit of less than all series of junior subordinated notes, stating that such covenants are expressly being included solely for the benefit of such series) or to surrender any right or power herein conferred upon Legg mason; or

to add any additional events of default; or

to add to or change any of the provisions of the junior subordinated note indenture, to change or eliminate any restrictions on the payment of principal (or premium, if any) on junior subordinated notes or to permit the issuance of junior subordinated notes in uncertificated form, provided any such action shall not adversely affect the interests of the holders of junior subordinated notes of any series in any material respect; or

Table of Contents

to change or eliminate any of the provisions of the junior subordinated note indenture with respect to any series of junior subordinated notes that have not yet been issued under the junior subordinated note indenture; or

to secure the junior subordinated notes; or

to establish the form or terms of junior subordinated notes of any series as permitted by the junior subordinated note indenture; or

to evidence and provide for the acceptance of appointment under the junior subordinated note indenture by a successor trustee with respect to the junior subordinated notes of one or more series and to add to or change any of the provisions of the junior subordinated indenture as shall be necessary to provide for or facilitate the administration of the trusts thereunder by more than one trustee, pursuant to the requirements of the junior subordinated note indenture; or

to cure any ambiguity, to correct or supplement any provision in the junior subordinated note indenture which may be inconsistent with a other provision therein, or to make provisions with respect to matters or questions arising under the junior subordinated note indenture, provided such action shall not adversely affect the interests of the holders of junior subordinated notes of any series or holders of outstanding trust securities in any material respect; or

subject to certain limitations, to make any change in the provisions described under this Modification section that would limit or terminate the benefits available to any holder of Senior Indebtedness; or

to modify, eliminate or add to the provisions of the junior subordinated note indenture to such extent as shall be necessary to the qualification of the junior subordinated note indenture under the Trust Indenture Act or under any similar federal statute hereafter enacted, and to add to the junior subordinated note indenture such other provisions as may be expressly required by the Trust Indenture Act.

Consolidation, Merger, Sale or Conveyance

The junior subordinated note indenture provides that Legg Mason may not consolidate with or merge into any other entity or convey, transfer or lease its properties and assets as an entirety or substantially as an entirety to any entity, unless:

the successor or transferee entity, if other than Legg Mason, is a corporation organized and existing under the laws of the United States, any state or territory thereof or the District of Columbia and expressly assumes by a supplemental indenture executed and delivered to the trustee, in form reasonably satisfactory to the trustee, the due and punctual payment of the principal of, any premium on and any interest (including Additional Interest) on, all the outstanding junior subordinated notes of Legg Mason and the performance of every covenant and obligation in the indenture to be performed or observed by Legg Mason;

immediately after giving effect to the transaction, no Event of Default and no event which, after notice or lapse of time or both, would become an Event of Default, has happened and is continuing; and

Legg Mason has delivered to the trustee an officer's certificate and an opinion of counsel, each in the form required by the junior subordinated note indenture and stating that such consolidation, merger, conveyance, transfer or lease and, if a supplemental indenture is required in connection with such transaction, such supplemental indenture comply with the foregoing provisions relating to such transaction.

In case of any such consolidation, merger, conveyance, transfer or lease, the successor entity will succeed to and be substituted for Legg Mason as obligor on the junior subordinated notes with the same effect as if it had been named in the junior subordinated note indenture as Legg Mason.

Table of Contents

Optional Redemption, Repayment and Repurchase

If specified in a prospectus supplement or term sheet, we may redeem the junior subordinated notes at our option by delivering a notice of any redemption at least 30 days, but not more than 60 days, before the date of redemption to each holder of the junior subordinated notes to be redeemed. If the junior subordinated notes are registered in the name of only one holder, any partial redemptions shall be pro rata; *provided* that, in the case of any such holder which is a depository or a nominee thereof, nothing in this sentence shall affect the right of such depository to select for redemption the positions held by its participants in accordance with the procedures of such depository. If the junior subordinated notes are held in definitive form by more than one holder and if less than all the junior subordinated notes of any series are to be redeemed, the particular junior subordinated notes to be redeemed shall be selected not more than 45 days prior to the redemption date by the junior subordinated note trustee, from the outstanding junior subordinated notes of such series not previously called for redemption, by lot or other such method as the junior subordinated note trustee shall deem fair and appropriate and which may provide for the selection for redemption of portions (equal to the minimum authorized denomination for junior subordinated notes of that series or any integral multiple thereof) of the principal amount of junior subordinated notes of such series of a denomination larger than the minimum authorized denomination for junior subordinated notes of that series. Unless we default in payment of the redemption price, on and after the date of redemption, interest will cease to accrue on the junior subordinated notes or portions thereof called for redemption.

We may at any time purchase junior subordinated notes at any price in the open market or otherwise, subject to applicable law. We may hold, resell or surrender for cancellation any junior subordinated notes that we purchase.

Information Concerning the Junior Subordinated Note Trustee

The junior subordinated note trustee, prior to an Event of Default with respect to junior subordinated notes of any series, undertakes to perform, with respect to junior subordinated notes of such series, only such duties as are specifically set forth in the junior subordinated note indenture and, in case an Event of Default with respect to junior subordinated notes of any series has occurred and is continuing, shall exercise, with respect to junior subordinated notes of such series, the same degree of care as a prudent individual would exercise in the conduct of his or her own affairs. Subject to such provision, the junior subordinated note trustee is under no obligation to exercise any of the powers vested in it by the junior subordinated note indenture at the request of any holder of junior subordinated notes of any series, unless offered reasonable indemnity by such holder against the costs, expenses and liabilities which might be incurred by the junior subordinated note trustee. The junior subordinated note trustee is not required to expend or risk its own funds or otherwise incur any financial liability in the performance of its duties if the junior subordinated note trustee reasonably believes that repayment or adequate indemnity is not reasonably assured to it.

The junior subordinated note trustee may be one of a number of banks with which we maintain ordinary banking relationships and from which we may obtain credit facilities and lines of credit in the future. The Bank of New York Mellon may also serve as trustee under other indentures under which we are the obligor in the future (including the senior note indenture). The trustee shall be under no obligation to exercise any of the rights or powers vested in it by this indenture at the request or direction of any of the holders of junior subordinated notes of any series pursuant to this indenture, unless such holders shall have offered to the trustee security or indemnity satisfactory to it against the costs, expenses and liabilities which might be incurred by it in compliance with such request or direction.

Governing Law

The junior subordinated note indenture and the junior subordinated notes will be governed by, and construed in accordance with, the internal laws of the State of New York.

Table of Contents

Miscellaneous

Legg Mason will have the right at all times to assign any of its rights or obligations under the junior subordinated note indenture to a direct or indirect wholly-owned subsidiary of Legg Mason; *provided*, that, in the event of any such assignment, Legg Mason will remain primarily liable for all such obligations. Subject to the foregoing, the junior subordinated note indenture will be binding upon and inure to the benefit of the parties to the junior subordinated note indenture and their respective successors and assigns.

Senior Subordinated Debt Securities and Debt Securities of Other Ranking

We may from time to time offer senior subordinated debt securities and debt securities of other ranking. Each time we sell such debt securities pursuant to this prospectus, we will provide a supplement to this prospectus that contains specific information about the offering and the specific terms of the securities offered.

Table of Contents

DESCRIPTION OF DEBT WARRANTS

Each series of debt warrants will be issued by Legg Mason under a separate debt warrant agreement to be entered into between Legg Mason and a bank or trust company, as debt warrant agent, as set forth in the applicable prospectus supplement or term sheet. The forms of each of the debt warrant agreements will be filed as exhibits to the registration statement of which this prospectus forms a part or will be furnished to the Commission on a Form 8-K that is incorporated by reference into the registration statement of which this prospectus forms a part. This prospectus briefly outlines certain general terms and provisions of the debt warrants Legg Mason may issue. Further terms of the debt warrants and applicable debt warrant agreement will be set forth in the applicable prospectus supplement or term sheet. The specific terms of a debt warrant as described in the applicable prospectus supplement or term sheet will supplement and, if applicable, may modify or replace the general terms described in this section. If there are differences between the applicable prospectus supplement or term sheet and this prospectus, the applicable prospectus supplement or term sheet will control. See [Where To Find More Information](#) for information on how to locate the debt warrant agreement.

General

A prospectus supplement or term sheet relating to each series of debt warrants that may be offered will include specifications relating to the offering. These terms will include the following:

the title of such debt warrants;

the aggregate number of such debt warrants and whether such debt warrants may be settled in cash;

the price or prices at which such debt warrants will be issued;

the currency or currencies (including composite currencies) in which the price of such debt warrants may be payable;

the aggregate principal amount and terms of the Legg Mason debt securities purchasable upon exercise of such debt warrants and the procedures and conditions relating to the exercise of such debt warrants;

the designation and terms of any related Legg Mason debt securities with which such debt warrants are issued and the number of such debt warrants issued with each such Legg Mason debt security;

the date, if any, when such debt warrants and the related Legg Mason debt securities will be separately transferable;

the principal amount of Legg Mason debt securities purchasable upon exercise of each debt warrant and the exercise price;

the date when the right to exercise such debt warrants begins and ends or, if a holder may not continuously exercise the warrants throughout that period, the specific date or dates on which the holder may exercise the debt warrants;

a discussion of the material U.S. federal income tax considerations that are specific to the debt warrants being offered; and

any other terms of such debt warrants, including terms, procedures and limitations relating to the exchange or exercise of such debt warrants.

Debt warrant certificates will be exchangeable for new debt warrant certificates of different denominations and debt warrants may be exercised at the corporate trust office of the debt warrant agent or any other office indicated in the applicable prospectus supplement or term sheet. Prior to the exercise of their debt warrants, holders of debt warrants will not have any of the rights of holders of the Legg Mason debt securities purchasable upon such exercise and will not be entitled to payments of principal of (and premium, if any) or interest, if any, on the Legg Mason debt securities purchasable upon such exercise.

Table of Contents

Exercise of Debt Warrants

Each debt warrant will entitle the holder to purchase for cash such principal amount of Legg Mason debt securities at such exercise price as shall in each case be set forth in, or be determinable as set forth in, the applicable prospectus supplement or term sheet relating to the debt warrants offered thereby. Debt warrants may be exercised at any time up to the close of business on the expiration date set forth in the applicable prospectus supplement or term sheet relating to the debt warrants offered by such prospectus supplement or term sheet. After the close of business on the expiration date, unexercised debt warrants will become void.

Debt warrants may be exercised as described in the applicable prospectus supplement or term sheet. Upon receipt of payment and the debt warrant certificate properly completed and duly executed at the corporate trust office of the debt warrant agent or any other office indicated in the applicable prospectus supplement or term sheet, Legg Mason will, as soon as practicable, forward the Legg Mason debt securities purchasable upon such exercise. If fewer than all of the debt warrants represented by such debt warrant certificate are exercised, a new debt warrant certificate will be issued for the remaining amount of debt warrants.

Table of Contents

DESCRIPTION OF CURRENCY WARRANTS

Currency warrants may be in the form of either: (i) currency warrants giving holders the right to receive from Legg Mason the cash settlement value in U.S. dollars of the right to sell a specified amount of a specified foreign currency or currency units for a specified amount of U.S. dollars (the currency put warrants) or (ii) currency warrants giving the holders the right to receive from Legg Mason the cash settlement value in U.S. dollars of the right to purchase a specified amount of a specified foreign currency or units of two or more currencies for a specified amount of U.S. dollars (the currency call warrants). The spot exchange rate of the applicable base currency as compared to the U.S. dollar will determine whether the currency warrants have a cash settlement value on any given day prior to their expiration.

Each series of the currency warrants will be issued by Legg Mason under a currency warrant agreement between Legg Mason and a bank or trust company, as currency warrant agent, as set forth in the applicable prospectus supplement or term sheet. The forms of each of the currency warrant agreements will be filed as exhibits to the registration statement of which this prospectus forms a part or will be furnished to the Commission on a Form 8-K that is incorporated by reference in the registration statement of which this prospectus forms a part. This prospectus briefly outlines certain general terms and provisions of the currency warrants Legg Mason may issue. Further terms of the currency warrants and applicable currency warrant agreement will be set forth in the applicable prospectus supplement or term sheet. The specific terms of a currency warrant as described in the applicable prospectus supplement or term sheet will supplement and, if applicable, may modify or replace the general terms described in this section. If there are differences between the applicable prospectus supplement or term sheet and this prospectus, the applicable prospectus supplement or term sheet will control. See [Where To Find More Information](#) for information on how to locate the currency warrant agreement.

General

A prospectus supplement or term sheet related to each series of currency warrants that may be offered will include specific terms relating to the offering. These terms will include the following:

whether currency put warrants or currency call warrants will be offered;

the title of such currency warrants;

the aggregate number of such currency warrants;

the formula for determining the cash settlement value, if any, of each currency warrant;

the price or prices at which such currency warrants will be issued;

the procedures and conditions relating to the exercise of each series of currency warrants;

when the currency warrants will be deemed to be automatically exercised;

any minimum number of currency warrants which must be exercised at any one time;

the dates the right to exercise such currency warrants will begin and end or, if a holder may not continuously exercise the warrants throughout the period, the specific date or dates on which the holder may exercise the currency warrants;

a discussion of the material U.S. federal income tax considerations, if any, that are specific to the currency warrants being offered; and

any other terms of such currency warrants, including terms, procedures and limitations relating to the exchange or exercise of such warrants.

Book-Entry Procedures and Settlement

Except as may otherwise be provided in the applicable prospectus supplement or term sheet, the currency warrants will be issued in book-entry form represented by a global currency warrant certificate registered in the

Table of Contents

name of a depositary or its nominee. Holders will not be entitled to receive definitive certificates representing currency warrants. A holder's ownership of a currency warrant will be recorded on or through the records of the brokerage firm or other entity that maintains such holder's account. In turn, the total number of currency warrants held by an individual brokerage firm for its clients will be maintained on the records of the depositary in the name of such brokerage firm or its agent. Transfer of ownership of any currency warrant will be effected only through the selling holder's brokerage firm.

The cash settlement value will be paid by the currency warrant agent to the depositary. The depositary will be responsible for crediting the amount of such payments to the accounts of participants or indirect participants in accordance with its standard procedures. Each participant or indirect participant will be responsible for disbursing such payments to the holders that it represents and to each brokerage firm for which it acts as agent. Each such brokerage firm will be responsible for disbursing funds to the holders that it represents.

Exercise of Currency Warrants

Except as may otherwise be provided in the applicable prospectus supplement or term sheet, each currency warrant will entitle the holder to receive the cash settlement value of such currency warrant on the applicable exercise date, in each case as such terms will be defined in the applicable prospectus supplement or term sheet. If not exercised prior to 3:00 P.M., New York City time, on the fifth New York Banking Day preceding the expiration date, currency warrants will be deemed automatically exercised on the expiration date.

Listing

If provided in the applicable prospectus supplement or term sheet, each issue of currency warrants may be listed on a national securities exchange, subject to official notice of issuance, as a condition of sale of any such currency warrants. In the event that any listed currency warrants are delisted from, or permanently suspended from trading on, such exchange, the expiration date for such currency warrants will be the date such delisting or trading suspension becomes effective and currency warrants not previously exercised will be deemed automatically exercised on such expiration date. The applicable currency warrant agreement will contain a covenant of Legg Mason not to seek delisting of the currency warrants, or suspension of their trading, on such exchange.

Table of Contents

DESCRIPTION OF STOCK WARRANTS

General

Legg Mason may issue warrants to purchase common stock or preferred stock of Legg Mason (stock warrants). We will issue the stock warrants under warrant agreements (each, a stock warrant agreement) to be entered into between us and a bank or trust company, as warrant agent (the stock warrant agent), identified in the applicable prospectus supplement or term sheet.

The forms of each of the stock warrant agreements will be filed as exhibits to the registration statement of which this prospectus forms a part or will be furnished to the Commission on a Form 8-K that is incorporated by reference in the registration statement of which this prospectus forms a part. This prospectus briefly outlines certain general terms and provisions of the stock warrants Legg Mason may issue. Further terms of the stock warrants and applicable stock warrant agreement will be set forth in the applicable prospectus supplement or term sheet. The specific terms of a stock warrant as described in the applicable prospectus supplement or term sheet will supplement and, if applicable, may modify or replace the general terms described in this section. If there are differences between the applicable prospectus supplement or term sheet and this prospectus, the applicable prospectus supplement or term sheet will control. See [Where To Find More Information](#) for information on how to locate the stock warrant agreement.

Because this section is a summary, it does not describe every aspect of the stock warrants and stock warrant agreement.

You should read the applicable prospectus supplement or term sheet for the material terms of any stock warrants we may issue, including the following:

the title and aggregate number of the stock warrants;

the number of shares of common stock or preferred stock that may be purchased upon exercise of each stock warrant;

the price, or the manner of determining the price, at which the shares may be purchased upon exercise;

if other than cash, the property and manner in which the exercise price may be paid;

any minimum number of stock warrants that must be exercised at any one time;

the time or times at which, or period or periods in which, the stock warrants may be exercised and the expiration date of the stock warrants;

any optional redemption terms;

the terms of any right that we may have to accelerate the exercise of the stock warrants upon the occurrence of certain events;

whether the stock warrants will be sold with any other offered securities and, if so, the amount and terms of these other securities;

the date, if any, on and after which the stock warrants and any other offered securities will be separately transferable; and

any other terms of the stock warrants.

The prospectus supplement or term sheet will also contain a discussion of the United States federal income tax considerations relevant to the offering.

Certificates representing stock warrants will be exchangeable for new stock warrant certificates of different denominations. We will not impose a service charge for any permitted transfer or exchange of stock warrant

Table of Contents

certificates, but we may require payment of any tax or other governmental charge payable in connection therewith. Stock warrants may be exercised at the corporate trust office of the stock warrant agent or any other office indicated in the prospectus supplement or term sheet.

Exercise of Stock Warrants

Each stock warrant will entitle the holder thereof to purchase the number of shares of Legg Mason's common stock or preferred stock, as applicable, at the exercise price set forth in, or calculable from, the applicable prospectus supplement or term sheet relating to the stock warrants. After the close of business on the applicable expiration date, unexercised stock warrants will be void.

Stock warrants may be exercised by payment to the stock warrant agent of the exercise price and by delivery to the stock warrant agent of the related stock warrant certificate, with the reverse side thereof properly completed. Stock warrants will be deemed to have been exercised upon receipt of the exercise price and the stock warrant certificate or certificates. Upon receipt of the payment and the properly completed stock warrant certificates, we will, as soon as practicable, deliver the shares of common stock or preferred stock, as applicable, purchased upon the exercise.

If fewer than all of the stock warrants represented by any stock warrant certificate are exercised, a new stock warrant certificate will be issued for the unexercised offered stock warrants. The holder of an offered stock warrant will be required to pay any tax or other governmental charge that may be imposed in connection with any transfer involved in the issuance of common stock or preferred stock, as applicable, purchased upon exercise.

Modifications

There are three types of changes Legg Mason can make to a stock warrant agreement and the stock warrants issued thereunder.

Changes Requiring Your Approval. First, there are changes that cannot be made to your stock warrants without your specific approval. Those types of changes include modifications and amendments that:

accelerate the expiration date;

reduce the number of outstanding stock warrants, the consent of the holders of which is required for a modification or amendment; or

otherwise materially and adversely affect the rights of the holders of the stock warrants.

Changes Not Requiring Approval. The second type of change does not require any vote by holders of the stock warrants. This type of change is limited to clarifications and other changes that would not materially adversely affect the interests of the holders of the stock warrants.

Changes Requiring a Majority Vote. Any other change to the stock warrant agreement requires a vote in favor by holders of not fewer than a majority in number of the then outstanding unexercised stock warrants affected thereby. Most changes fall into this category.

Stock Warrant Adjustments

The terms and conditions on which the exercise price of and/or the number of shares of common stock or preferred stock, as applicable, covered by a stock warrant are subject to adjustment will be set forth in the stock warrant agreement and the applicable prospectus supplement or term sheet. The terms will include provisions for adjusting the exercise price and/or the number of shares of common stock or preferred stock, as applicable, covered by the stock warrant; the events requiring the adjustment; the events upon which we may, in lieu of

Table of Contents

making the adjustment, make proper provisions so that the holder of a stock warrant, upon exercise thereof, would be treated as if the holder had exercised the stock warrant prior to the occurrence of the events; and provisions affecting exercise in the event of certain events affecting the common stock or preferred stock, as applicable.

No Rights as Stockholders

Holders of stock warrants are not entitled, by virtue of being holders, to receive dividends or to vote, consent or receive notice as our stockholders in respect of any meeting of stockholders for the election of our directors or for any other matter, or exercise any other rights whatsoever as our stockholders.

Table of Contents

DESCRIPTION OF COMMON STOCK

The following summary describes elements of Legg Mason's Articles of Incorporation and Bylaws as well as relevant sections of The Maryland Business Combination Act (the "Business Combination Act"). Legg Mason's authorized capital stock consists of (i) 500,000,000 shares of common stock, par value \$.10 per share, of which 107,708,098 shares were issued and outstanding as of January 28, 2016 and (ii) 4,000,000 shares of preferred stock, par value \$10.00 per share of which no shares are issued and outstanding as of the date of this prospectus. The following summary is qualified in its entirety by reference to the Articles of Incorporation and the Bylaws, copies of which are on file with the SEC, and the Business Combination Act.

Common Stock

Holders of common stock are entitled to one vote per share on all matters to be voted upon by the stockholders. The holders of common stock do not have cumulative voting rights in the election of directors. Holders of common stock are entitled to receive dividends if, as and when dividends are declared from time to time by Legg Mason's Board of Directors out of funds legally available therefor, after payment of dividends required to be paid on outstanding preferred stock or series common stock (as described below), if any. In the event of liquidation, dissolution or winding up of Legg Mason, the holders of common stock are entitled as a class, share for share, to share ratably in all assets remaining after payment of debts and other liabilities of Legg Mason and the payment of the full preferential amounts to which the holders of preferred stock are entitled. The common stock has no preemptive or conversion rights and is not subject to further calls or assessment by Legg Mason. There are no redemption or sinking fund provisions applicable to the common stock. The common stock sold by Legg Mason in an offering pursuant to this prospectus, when sold to the underwriters of such offering in the manner described in this prospectus and the prospectus supplement or term sheet relating to such offering will be, and all currently outstanding common stock of Legg Mason is, duly authorized, validly issued, fully paid and non-assessable.

Authorized but Unissued Capital Stock

Maryland law does not require stockholder approval for any issuance of authorized shares. However, the listing requirements of the New York Stock Exchange, which would apply so long as the common stock remains listed on the New York Stock Exchange, require stockholder approval of certain issuances equal to or exceeding 20% of the then outstanding voting power or then outstanding number of shares of common stock. These additional shares may be used for a variety of corporate purposes, including future public offerings to raise additional capital or to facilitate acquisitions.

One of the effects of the existence of unissued and unreserved common stock and preferred stock may be to enable Legg Mason's Board of Directors to issue shares to persons friendly to current management, which issuance could render more difficult or discourage an attempt to obtain control of Legg Mason by means of a merger, tender offer, proxy contest or otherwise, and thereby protect the continuity of Legg Mason's management and possibly deprive the stockholders of opportunities to sell their shares at prices higher than prevailing market prices.

Two-Tier Business Combination Provisions

The Maryland Business Combination Act

Legg Mason is a Maryland corporation subject to the Business Combination Act. The Business Combination Act provides that "business combinations" between a Maryland corporation and an interested stockholder or an affiliate of an interested stockholder are prohibited for five years after the most recent date on which the interested stockholder

becomes an interested stockholder. These business combinations include a merger, consolidation, statutory share exchange or, in circumstances specified in the statute, an asset transfer or issuance or reclassification of equity securities. An interested stockholder is defined as:

any person who beneficially owns 10% or more of the voting power of the corporation's shares; or

Table of Contents

an affiliate or associate of the corporation who, at any time within the two-year period prior to the date in question, was the beneficial owner of 10% or more of the voting power of the then outstanding voting stock of the corporation.

A person is not an interested stockholder under this statute if the Board of Directors approved in advance the transaction by which such stockholder otherwise would have become an interested stockholder. However, in approving a transaction, the Board of Directors may provide that its approval is subject to compliance, at or after the time of approval, with any terms and conditions determined by the Board of Directors.

After the five-year prohibition, any business combination between the Maryland corporation and an interested stockholder generally must be recommended by the Board of Directors of the corporation and approved by the affirmative vote of at least:

80% of the votes entitled to be cast by holders of outstanding shares of voting stock of the corporation; and

two-thirds of the votes entitled to be cast by holders of voting stock of the corporation other than shares held by the interested stockholder with whom or with whose affiliate the business combination is to be effected or held by an affiliate or associate of the interested stockholder.

These super-majority vote requirements do not apply if the corporation's common stockholders receive a minimum price, as defined under Maryland law, for their shares in the form of cash or other consideration in the same form as previously paid by the interested stockholder for its shares.

The statute permits various exemptions from its provisions, including business combinations that are exempted by the Board of Directors before the time that the interested stockholder becomes an interested stockholder. These voting provisions do not apply if the stockholders receive a minimum price, as defined under Maryland law.

Articles of Incorporation

As permitted by the Business Combination Act, our Articles of Incorporation require the affirmative vote of not less than 70% of our then outstanding shares of voting stock to approve any business combination of us with any related person unless certain conditions have been met. In addition, the 70% vote must include the affirmative vote of at least 55% of the outstanding shares of voting stock held by stockholders other than the related person. Accordingly, the actual vote required to approve the business combination may be greater than the 70%, depending upon the number of shares controlled by the related person. A related person is defined to include any person or entity which is, directly or indirectly, the beneficial owner of 15% or more of the outstanding shares of our voting stock, including any affiliate or associate of such person or entity. The term business combination is defined to include a wide variety of transactions between us and a related person, including a merger, consolidation, share exchange or sale of assets having a fair market value greater than 10% of the book value of our consolidated assets.

However, if the related person pays a fair price to our stockholders in the transaction, the 70% requirement would not be applicable and the proposed business combination could be approved by a simple majority of the stockholders unless otherwise required by Maryland law, provided that such affirmative vote includes at least 55% of the voting stock held by persons other than the related person. Under our Articles of Incorporation, the fair price must be at least equal to the greater of:

the highest price paid or agreed to be paid by the related person to purchase shares of our common stock during the 24-month period prior to the taking of such vote; or

the highest market price of the common stock during the 24-month period prior to the taking of such vote; or

Table of Contents

the per share book value of our common stock at the end of the calendar quarter immediately preceding the taking of such vote.

In addition, the fair price consideration to be received by our stockholders must be of the same form and kind as the most favorable form and kind of consideration paid by the related person in acquiring any of its shares of our common stock.

The special voting provisions are not applicable to a business combination authorized by our Board of Directors by a vote which includes a majority of our disinterested directors. A disinterested director is defined to include any member of our Board of Directors who is not the related person (or an affiliate or associate of the related person) and who was a director prior to the time that the related person became a related person, and any successor of a disinterested director who is not the related person (or an affiliate or associate of the related person) and who is recommended to succeed a disinterested director by a majority of the disinterested directors then on our Board of Directors.

Our special voting provisions may not be amended, altered, changed or repealed except by the affirmative vote of at least 70% of the shares of stock entitled to vote at a meeting of the stockholders called for the consideration of such amendment, alteration, change or repeal, and at least 55% of the outstanding shares of stock entitled to vote thereon held by stockholders who are not related persons, unless such proposal was proposed by our Board of Directors by a vote which includes a majority of the disinterested directors.

The business combination provisions under our Articles of Incorporation could have the effect of delaying, deterring or preventing a change in control. Any possible change in control could also be affected by the applicability of certain Maryland anti-takeover statutes dealing with business combinations and acquisitions of controlling blocks of shares (including the Business Combination Act), as well as by our classified Board of Director provisions.

Articles of Incorporation; Bylaws

In addition to the provisions described above in Two-Tier Business Combination Provisions, the Articles of Incorporation and the Bylaws contain certain provisions that could make more difficult the acquisition of Legg Mason by means of a tender offer, a proxy contest or otherwise.

Non-Staggered Board. The Articles of Incorporation and the Bylaws provide that Legg Mason's Board of Directors will be non-staggered. All directors will be elected for terms expiring at the next annual meeting of stockholders. The Articles of Incorporation provide that the number of directors will be fixed in the manner provided in the Bylaws. The Articles of Incorporation and the Bylaws provide that the number of directors will be fixed from time to time pursuant to any regular meeting or any special meeting by a majority of the entire Board of Directors, but must consist of not less than six directors and not more than twenty directors. In addition, the Bylaws provide that any vacancies will not affect the Bylaws or the powers of the remaining Board of Directors under the Bylaws.

Removal of Directors. Under the Maryland General Corporation Law (the MGCL), unless otherwise provided in the Articles of Incorporation, directors serving on a classified board may be removed by the stockholders with or without cause. In addition, the Articles of Incorporation and the Bylaws provide that directors may be removed with or without cause and only upon the affirmative vote of holders of at least 70% of the voting power of all the then outstanding shares of stock entitled to vote generally in the election of directors.

Stockholder Action. The Articles of Incorporation and the Bylaws provide that stockholder action can be taken without a meeting (i) if a unanimous consent in writing or by electronic transmission is signed by all the stockholders entitled to vote on the subject matter and any other stockholders entitled to notice of a meeting of stockholders have waived in

writing any rights which they may have to dissent from such action, and such consent and waiver are filed with the minutes of proceedings of the stockholders or (ii) unless the Articles of

Table of Contents

Incorporation or the Bylaws require otherwise, by the holders of any class of stock, other than common stock entitled to vote generally in the election of directors, by delivering a consent in writing or by electronic transmission of the stockholders entitled to cast not less than the minimum number of votes that would be necessary to authorize or take the action at a stockholders meeting if Legg Mason gives notice of the action to each holder of the class of stock not later than ten days after the effective time of the action. The Articles of Incorporation and the Bylaws provide that special meetings of stockholders can be called by the chairman of the Board of Directors, Legg Mason's Chief Executive Officer, the president or a majority of the Board of Directors. Majority stockholders are permitted to call a special meeting through a written request to the secretary. Moreover, the business permitted to be conducted at any special meeting of stockholders is limited to the business brought before the meeting pursuant to the notice of meeting given by Legg Mason.

Advance Notice Procedures. Not less than ten nor more than 90 days before the date of every meeting of stockholders, the secretary must give to each stockholder entitled to vote at such meeting and to each stockholder not entitled to vote who is entitled to notice of the meeting, written or printed notice stating the time and place of the meeting. In the case of a special meeting or as otherwise may be required by any statute, such written notice must contain the purpose for which the meeting is called, either by mail, by presenting it to such stockholder personally, by leaving it at the stockholder's residence or usual place of business, by electronic transmission, or by any other means permitted by Maryland law. If mailed, such notice is deemed to be given when deposited in the United States mail addressed to the stockholder at the stockholder's address as it appears on the records of the corporation, with postage thereon prepaid. If transmitted electronically, such notice is deemed to be given when transmitted to the stockholder by an electronic transmission to any address or number of the stockholder at which the stockholder receives electronic transmissions. Legg Mason may give a single notice to all stockholders who share an address, which single notice will be effective as to any stockholder at such address, unless a stockholder objects to receiving such single notice or revokes a prior consent to receiving such single notice. Failure to give notice of any meeting to one or more stockholders, or any irregularity in such notice, will not affect the validity of any meeting fixed in accordance with this procedure or the validity of any proceedings at any such meeting.

Legg Mason may postpone or cancel a meeting of stockholders by making a public announcement through disclosure in a press release or in a document publicly filed with the Commission of such postponement or cancellation prior to the meeting. Notice of the date, time and place to which the meeting is postponed must be given not less than ten days prior to such date.

Liability of Directors; Indemnification. The Articles of Incorporation provide that a director will not be personally liable for monetary damages to Legg Mason or its stockholders, except to the extent such limitation of liability is not permitted under the MGCL. The Articles of Incorporation also provide that notwithstanding any contrary provision of law, no indemnification will be provided for any officer, director, employee or agent of any predecessor of Legg Mason unless the Bylaws otherwise provide. The Bylaws provide for indemnification of any person who is serving or has served as a director or officer of Legg Mason, against all liabilities and expenses incurred in connection with any action, suit or proceeding arising out of such service to the full extent permitted under Maryland law.

Amendment. The Articles of Incorporation provide that Legg Mason may amend its Articles of Incorporation, including any provision which alters the contract rights, as expressly set forth in its Articles of Incorporation, of any outstanding stock. However, no such amendment may change the terms of any class or series of any class of the outstanding stock unless such change of terms shall have been authorized by the holders of not less than two-thirds of all shares of such class or series of such class at the time outstanding.

The Bylaws provide that the Bylaws may be amended only by a majority of the entire Board of Directors at any regular meeting of the Board of Directors or at any special meeting called for that purpose.

The description set forth above is intended as a summary only and is qualified in its entirety by reference to the Articles of Incorporation and the Bylaws, copies of which are exhibits to the Registration Statement of which this prospectus is a part.

Table of Contents

Registrar and Transfer Agent

The registrar and transfer agent for the common stock is American Stock Transfer & Trust Company, LLC.

Listing

Legg Mason's common stock is listed on the New York Stock Exchange under the symbol LM.

Table of Contents

DESCRIPTION OF PREFERRED STOCK

Under Legg Mason's Articles of Incorporation, its Board of Directors is authorized to adopt resolutions providing for the issuance, in one or more series, of up to 4,000,000 shares of preferred stock, \$10.00 par value, with the powers, preferences and relative, participating, optional or other special rights and qualifications, limitations or restrictions thereof adopted by the Board of Directors or a duly authorized committee thereof.

Because this section is a summary, it does not describe every aspect of Legg Mason's preferred stock. We urge you to read Legg Mason's Articles of Incorporation and the certificate of designations creating your preferred stock because they, and not this description, define your rights as a holder of preferred stock. Legg Mason has filed the Articles of Incorporation and will file the certificate of designations with the SEC. See [Where To Find More Information](#) for information on how to obtain copies of these documents.

The specific material terms of any preferred stock proposed to be sold under this prospectus and an attached prospectus supplement or term sheet will be described in the prospectus supplement or term sheet. If so indicated in the prospectus supplement or term sheet, the terms of the offered preferred stock may differ from the terms set forth below.

General

Unless otherwise specified in the prospectus supplement or term sheet relating to the offered preferred stock, each series of preferred stock will rank on a parity as to dividends and distribution of assets upon liquidation and in all other respects with all other series of preferred stock. The preferred stock will, when issued, be fully paid and nonassessable and holders thereof will have no preemptive rights.

You should read the prospectus supplement or term sheet for the material terms of the preferred stock offered thereby, including the following:

The title and stated value of the preferred stock.

The number of shares of the preferred stock offered, the liquidation preference per share and the offering price of the preferred stock.

The dividend rate(s), period(s) and/or payment date(s) or method(s) of calculation thereof applicable to the preferred stock.

The date from which dividends on the preferred stock will accumulate, if applicable.

The liquidation rights of the preferred stock.

The procedures for any auction and remarketing, if any, of the preferred stock.

The sinking fund provisions, if applicable, for the preferred stock.

The redemption provisions, if applicable, for the preferred stock.

Whether the preferred stock will be convertible into or exchangeable for other securities and, if so, the terms and conditions of conversion or exchange, including the conversion price or exchange ratio and the conversion or exchange period (or the method of determining the same).

Whether the preferred stock will have voting rights and the terms thereof, if any.

Whether the preferred stock will be listed on any securities exchange.

Whether the preferred stock will be issued with any other securities and, if so, the amount and terms of these other securities.

Any other specific material terms, preferences or rights of, or limitations or restrictions on, the preferred stock.

Table of Contents

Subject to Legg Mason's Articles of Incorporation and to any limitations contained in its outstanding preferred stock, Legg Mason may issue additional series of preferred stock, at any time or from time to time, with the powers, preferences and relative, participating, optional or other special rights and qualifications, limitations or restrictions thereof, as the Board of Directors or any duly authorized committee thereof may determine, all without further action of its stockholders, including holders of its then outstanding preferred stock.

If applicable, the prospectus supplement or term sheet will also contain a discussion of the material United States federal income tax considerations relevant to the offering.

Dividends

Holders of preferred stock will be entitled to receive cash dividends, when, as and if declared by the Board of Directors, out of Legg Mason's assets legally available for payment, at the rate and on the dates set forth in the prospectus supplement or term sheet. Each dividend will be payable to holders of record as they appear on our books on the record date fixed by the Board of Directors. Dividends, if cumulative, will be cumulative from and after the date set forth in the applicable prospectus supplement or term sheet.

Conversion and Exchange

If the preferred stock will be convertible into or exchangeable for common stock or other securities, the prospectus supplement or term sheet will set forth the terms and conditions of that conversion or exchange, including the conversion price or exchange ratio (or the method of calculating the same), the conversion or exchange period (or the method of determining the same), whether conversion or exchange will be mandatory or at the option of the holder or us, the events requiring an adjustment of the conversion price or the exchange ratio and provisions affecting conversion or exchange in the event of the redemption of that preferred stock. These terms may also include provisions under which the number of shares of common stock or the number or amount of other securities to be received by the holders of that preferred stock upon conversion or exchange would be calculated according to the market price of the common stock or those other securities as of a time stated in the prospectus supplement or term sheet.

Liquidation Rights

In the event of Legg Mason's voluntary or involuntary liquidation, dissolution or winding up, the holders of each series of the preferred stock will be entitled to receive out of the assets that are available for distribution to stockholders, before any distribution of assets is made to holders of any stock that is junior as to dividends and liquidation rights to such series of preferred stock, liquidating distributions in the amount set forth in the applicable prospectus supplement or term sheet plus all accrued and unpaid dividends. If, upon Legg Mason's voluntary or involuntary liquidation, dissolution or winding up, the amounts payable with respect to the preferred stock are not paid in full, the holders of preferred stock of each series will share ratably in the distribution of assets in proportion to the full respective preferential amounts to which they are entitled. After payment of the full amount of the liquidating distribution to which they are entitled, the holders of the preferred stock will not be entitled to any further participation in any distribution of assets. Legg Mason's consolidation or merger with or into any other corporation or corporations or a sale of all or substantially all of its assets will not be deemed to be a liquidation, dissolution or winding up for purposes of these provisions.

Redemption

If so provided in the prospectus supplement or term sheet, the offered preferred stock may be redeemable in whole or in part at Legg Mason's option at the times and at the redemption prices set forth therein.

Voting Rights

Except as indicated below or in the prospectus supplement or term sheet, or except as expressly required by applicable law, the holders of the preferred stock will not be entitled to vote.

Table of Contents

DESCRIPTION OF DEPOSITARY SHARES

General

Legg Mason may, at its option, elect to offer fractional shares rather than full shares of the preferred stock of a series. In the event that Legg Mason determines to do so, it will issue receipts for depositary shares, each of which will represent a fraction (to be set forth in the prospectus supplement or term sheet relating to a particular series of preferred stock) of a share of a particular series of preferred stock as more fully described below.

The shares of any series of preferred stock represented by depositary shares will be deposited under one or more deposit agreements among Legg Mason, a depositary to be named in the applicable prospectus supplement or term sheet and the holders from time to time of depositary receipts issued thereunder. Subject to the terms of the applicable deposit agreement, each holder of a depositary share will be entitled, in proportion to the applicable fraction of a share of preferred stock represented by the depositary share, to all the rights and preferences of the preferred stock represented thereby (including, as applicable, dividend, redemption and liquidation rights).

The depositary shares will be evidenced by depositary receipts issued pursuant to the deposit agreement. Depositary receipts will be distributed to those persons purchasing the fractional shares of the related series of preferred stock.

The following description sets forth certain general terms and provisions of the depositary shares to which any prospectus supplement or term sheet may relate. The particular terms of the depositary shares to which any prospectus supplement or term sheet may relate and the extent, if any, to which such general provisions may apply to the depositary shares so offered will be described in the applicable prospectus supplement or term sheet. To the extent that any particular terms of the depositary shares or the deposit agreement described in a prospectus supplement or term sheet differ from any of the terms described below, then the terms described below will be deemed to have been superseded by that prospectus supplement or term sheet relating to such deposited shares.

The following summary of certain provisions of the depositary shares and deposit agreement does not purport to be complete and is subject to, and is qualified in its entirety by express reference to, all the provisions of the deposit agreement and the applicable prospectus supplement or term sheet, including the definitions.

Immediately following Legg Mason's issuance of shares of a series of preferred stock that will be offered as fractional shares, Legg Mason will deposit the shares with the depositary, which will then issue and deliver the depositary receipts to the purchasers thereof. Depositary receipts will only be issued evidencing whole depositary shares. A depositary receipt may evidence any number of whole depositary shares.

Pending the preparation of definitive depositary receipts, the depositary may, upon Legg Mason's written order, issue temporary depositary receipts substantially identical to (and entitling the holders thereof to all the rights pertaining to) the definitive depositary receipts but not in definitive form. Definitive depositary receipts will be prepared thereafter without unreasonable delay, and such temporary depositary receipts will be exchangeable for definitive depositary receipts at Legg Mason's expense.

Dividends and Other Distributions

The depositary will distribute all cash dividends or other cash distributions received in respect of the related series of preferred stock to the record holders of depositary shares relating to the series of preferred stock in proportion to the number of the depositary shares owned by the holders.

In the event of a distribution other than in cash, the depositary will distribute property received by it to the record holders of depositary shares entitled thereto in proportion to the number of depositary shares owned by the

Table of Contents

holders, unless the depositary determines that the distribution cannot be made proportionately among the holders or that it is not feasible to make the distributions, in which case the depositary may, with Legg Mason's approval, adopt any method as it deems equitable and practicable for the purpose of effecting the distribution, including the sale (at public or private sale) of the securities or property thus received, or any part thereof, at the place or places and upon those terms as it may deem proper.

The amount distributed in any of the foregoing cases will be reduced by any amounts required to be withheld by Legg Mason or the depositary on account of taxes or other governmental charges.

Redemption of Depositary Shares

If any series of the preferred stock underlying the depositary shares is subject to redemption, the depositary shares will be redeemed from the proceeds received by the depositary resulting from any redemption, in whole or in part, of the series of the preferred stock held by the depositary. The redemption price per depositary share will be equal to the applicable fraction of the redemption price per share payable with respect to the series of the preferred stock. If Legg Mason redeems shares of a series of preferred stock held by the depositary, the depositary will redeem as of the same redemption date the number of depositary shares representing the shares of preferred stock so redeemed. If less than all the depositary shares are to be redeemed, the depositary shares to be redeemed will be selected by lot or substantially equivalent method determined by the depositary.

After the date fixed for redemption, the depositary shares so called for redemption will no longer be deemed to be outstanding and all rights of the holders of the depositary shares will cease, except the right to receive the monies payable upon redemption and any money or other property to which the holders of the depositary shares were entitled upon such redemption, upon surrender to the depositary of the depositary receipts evidencing the depositary shares. Any funds deposited by Legg Mason with the depositary for any depositary shares that the holders thereof fail to redeem will be returned to Legg Mason after a period of two years from the date the funds are so deposited.

Voting the Underlying Preferred Stock

Upon receipt of notice of any meeting at which the holders of any series of the preferred stock underlying the depositary shares are entitled to vote, the depositary will mail the information contained in the notice of meeting to the record holders of the depositary shares relating to such series of preferred stock. Each record holder of the depositary shares on the record date (which will be the same date as the record date for the related series of preferred stock) will be entitled to instruct the depositary as to the exercise of the voting rights pertaining to the number of shares of the series of preferred stock represented by that holder's depositary shares. The depositary will endeavor, insofar as practicable, to vote or cause to be voted the number of shares of preferred stock represented by the depositary shares in accordance with the instructions, provided the depositary receives the instructions sufficiently in advance of the meeting to enable it to so vote or cause to be voted the shares of preferred stock, and Legg Mason will agree to take all reasonable action that may be deemed necessary by the depositary in order to enable the depositary to do so. The depositary will abstain from voting shares of the preferred stock to the extent it does not receive specific instructions from the holders of depositary shares representing the preferred stock.

Conversion and Exchange

Depositary shares are not convertible into or exchangeable for other shares of Legg Mason's stock or other securities. Nevertheless, if the preferred stock represented by depositary shares is convertible into or exchangeable for other shares of Legg Mason's stock or other securities, the depositary receipts evidencing the depositary shares may be surrendered by the holder thereof to the depositary with written instructions to convert or exchange the preferred stock

into whole shares of Legg Mason's other stock or other securities, as specified in the related prospectus supplement or term sheet. Upon receipt of these instructions and any amounts payable in

Table of Contents

respect thereof, Legg Mason will cause the conversion or exchange thereof and will deliver to the holder whole shares of Legg Mason's other stock or the whole number of other securities (and cash in lieu of any fractional share or security). In the case of a partial conversion or exchange, the holder will receive a new depositary receipt evidencing the unconverted or unexchanged balance.

Withdrawal of Stock

Upon surrender of the depositary receipts at the corporate trust office of the depositary and upon payment of the taxes, charges and fees provided for in the deposit agreement and subject to the terms thereof, the holder of the depositary shares evidenced thereby will be entitled to delivery at such office, to or upon his or her order, of the number of whole shares of the related series of preferred stock and any money or other property, if any, represented by the depositary shares. Holders of depositary shares will be entitled to receive whole shares of the related series of preferred stock, but holders of the whole shares of preferred stock will not thereafter be entitled to deposit the shares of preferred stock with the depositary or to receive depositary shares therefor. If the depositary receipts delivered by the holder evidence a number of depositary shares in excess of the number of depositary shares representing the number of whole shares of the related series of preferred stock to be withdrawn, the depositary will deliver to the holder or upon his or her order at the same time a new depositary receipt evidencing the excess number of depositary shares.

Amendment and Termination of a Deposit Agreement

The form of depositary receipt evidencing the depositary shares of any series and any provision of the applicable deposit agreement may at any time and from time to time be amended by agreement between Legg Mason and the depositary. However, any amendment that materially adversely alters the rights of the holders of depositary shares of any series will not be effective unless the amendment has been approved by the holders of at least a majority of the depositary shares of the series then outstanding. Every holder of a depositary receipt at the time the amendment becomes effective will be deemed, by continuing to hold the depositary receipt, to be bound by the deposit agreement as so amended. Notwithstanding the foregoing, in no event may any amendment impair the right of any holder of any depositary shares, upon surrender of the depositary receipts evidencing the depositary shares and subject to any conditions specified in the deposit agreement, to receive shares of the related series of preferred stock and any money or other property represented thereby, except in order to comply with mandatory provisions of applicable law. The deposit agreement may be terminated by Legg Mason at any time upon not less than 60 days' prior written notice to the depositary, in which case, on a date that is not later than 30 days after the date of the notice, the depositary shall deliver or make available for delivery to holders of depositary shares, upon surrender of the depositary receipts evidencing the depositary shares, the number of whole or fractional shares of the related series of preferred stock as are represented by the depositary shares. The deposit agreement shall automatically terminate after all outstanding depositary shares have been redeemed or there has been a final distribution in respect of the related series of preferred stock in connection with any liquidation, dissolution or winding up of Legg Mason and the distribution has been distributed to the holders of depositary shares.

Charges of Depositary

Except as provided in the prospectus supplement or term sheet, Legg Mason will pay the fees and expenses of the depositary, and the holders of depositary receipts will be required to pay any tax or other governmental charge that may be imposed in connection with the transfer, exercise, surrender or split-up of depositary receipts.

Resignation and Removal of Depositary

The depositary may resign at any time by delivering to Legg Mason written notice of its election to do so, and Legg Mason may at any time remove the depositary. Any resignation or removal will take effect upon the appointment of a successor depositary, which successor depositary must be appointed within 60 days after delivery of the notice of resignation or removal and must be a bank or trust company having its principal office in the United States and having a combined capital and surplus of at least \$50,000,000.

Table of Contents

Miscellaneous

The depositary will forward to the holders of depositary shares all reports and communications from Legg Mason that are delivered to the depositary and which Legg Mason is required to furnish to the holders of the related preferred stock.

The depositary's corporate trust office will be identified in the applicable prospectus supplement or term sheet. Unless otherwise set forth in the applicable prospectus supplement or term sheet, the depositary will act as transfer agent and registrar for depositary receipts and if shares of a series of preferred stock are redeemable, the depositary will also act as redemption agent for the corresponding depositary receipts.

Table of Contents

DESCRIPTION OF RIGHTS

This section describes the general terms of the rights that Legg Mason may offer and sell by this prospectus. This prospectus and any accompanying prospectus supplement or term sheet will contain the material terms and conditions for each right. The accompanying prospectus supplement or term sheet may add, update or change the terms and conditions of the rights as described in this prospectus. The particular terms of each issue of rights, the rights agent agreement relating to the rights and the rights certificates representing rights will be described in the applicable prospectus supplement or term sheet, including, as applicable:

the title of the rights;

the date of determining the stockholders entitled to the rights distribution;

the title, aggregate number of shares of common stock or preferred stock purchasable upon exercise of the rights;

the exercise price;

the aggregate number of rights issued;

the date, if any, on and after which the rights will be separately transferable;

if applicable, a discussion of United States federal income tax, accounting or other considerations applicable to the rights;

the date on which the right to exercise the rights will commence and the date on which the right will expire; and

any other terms of the rights, including terms, procedures and limitations relating to the distribution, exchange and exercise of the rights.

Exercise of Rights

Each right will entitle the holder of rights to purchase for cash the principal amount of shares of common stock or preferred stock at the exercise price provided in the applicable prospectus supplement or term sheet. Rights may be exercised at any time up to the close of business on the expiration date for the rights provided in the applicable prospectus supplement or term sheet. After the close of business on the expiration date, all unexercised rights will be void.

Holders may exercise rights as described in the applicable prospectus supplement or term sheet. Upon receipt of payment and the rights certificate properly completed and duly executed at the corporate trust office of the rights agent or any other office indicated in the prospectus supplement or term sheet, Legg Mason will, as soon as practicable, forward the shares of common stock or preferred stock purchasable upon exercise of the rights. If less than all of the rights issued in any rights offering are exercised, Legg Mason may offer any unsubscribed securities directly to persons other than stockholders, to or through agents, underwriters or dealers or through a combination of such methods, including pursuant to standby underwriting arrangements, as described in the applicable prospectus supplement or term sheet.

Table of Contents

DESCRIPTION OF PURCHASE CONTRACTS

Legg Mason may issue, from time to time, purchase contracts, including contracts obligating holders to purchase from Legg Mason and Legg Mason to sell to the holders, a specified principal amount of debt securities, debt warrants, currency warrants, stock warrants, common stock, preferred stock, depositary shares or other securities that Legg Mason may sell under this prospectus at a future date or dates. The consideration payable upon settlement of the purchase contracts may be fixed at the time the purchase contracts are issued or may be determined by a specific reference to a formula set forth in the purchase contracts. The purchase contracts may be issued separately or as part of units consisting of a purchase contract and other securities or obligations issued by Legg Mason or third parties, including United States treasury securities, securing the holders' obligations to purchase the relevant securities under the purchase contracts. The purchase contracts may require Legg Mason to make periodic payments to the holders of the purchase contracts or units or vice versa, and the payments may be unsecured or prefunded on some basis. The purchase contracts may require holders to secure their obligations under the purchase contracts.

The prospectus supplement or term sheet related to any particular purchase contracts will describe, among other things, the material terms of the purchase contracts and of the securities being sold pursuant to such purchase contracts, a discussion, if appropriate, of any special United States federal income tax considerations applicable to the purchase contracts and any material provisions governing the purchase contracts that differ from those described above. The description in the prospectus supplement or term sheet will not necessarily be complete and will be qualified in its entirety by reference to the purchase contracts, and, if applicable, collateral arrangements, relating to the purchase contracts.

Table of Contents

DESCRIPTION OF UNITS

Legg Mason may, from time to time, issue units comprised of one or more of certain other securities that may be offered under this prospectus, in any combination. Each unit may also include debt obligations of third parties, such as U.S. Treasury securities. Each unit will be issued so that the holder of the unit is also the holder of each security included in the unit. Thus, the holder of a unit will have the rights and obligations of a holder of each included security. The unit agreement under which a unit is issued may provide that the securities included in the unit may not be held or transferred separately at any time, or at any time before a specified date.

Any prospectus supplement or term sheet related to any particular units will describe, among other things:

the material terms of the units and of the securities comprising the units, including whether and under what circumstances those securities may be held or transferred separately;

any material provisions relating to the issuance, payment, settlement, transfer or exchange of the units or of the securities comprising the units;

if appropriate, any special United States federal income tax considerations applicable to the units; and

any material provisions of the governing unit agreement that differ from those described above.

Table of Contents

HOLDING COMPANY STRUCTURE

We are a holding company and our assets consist primarily of investments in our subsidiaries. A substantial portion of our consolidated liabilities have been incurred by our subsidiaries. Our rights and the rights of our creditors, including holders of our securities, to participate in the distribution of assets of any subsidiary upon liquidation or reorganization of a subsidiary or otherwise will be subject to prior claims of the subsidiary's creditors, including trade creditors, except to the extent that we may be a creditor with recognized claims against the subsidiary. Accordingly, the holders of our securities may be deemed to be effectively subordinated to such claims. As of December 31, 2015, our subsidiaries had a total of approximately \$1.0 billion of outstanding liabilities, including indebtedness.

Our ability to service our indebtedness and other obligations, including the securities offered hereby, is dependent primarily upon the earnings and cash flow of our subsidiaries and the distribution or other payment to us of such earnings and cash flow.

Table of Contents

PLAN OF DISTRIBUTION

Terms of Sale

We will describe the terms of a particular offering of securities in the applicable prospectus supplement or term sheet, including the following:

the name or names of any underwriters, dealers or agents;

the purchase price of the securities;

the proceeds to the issuer from sale;

any underwriting discounts and other items constituting underwriters' compensation;

any initial public offering price of the securities;

any concessions allowed or reallocated or paid to dealers; and

any securities exchanges on which such securities may be listed.

Any underwriters, dealers or agents participating in a sale of securities may be considered to be underwriters under the Securities Act. Furthermore, any discounts or commissions received by them may be considered to be underwriting discounts and commissions under the Securities Act. We may agree to indemnify any agents and underwriters against certain liabilities, including liabilities under the Securities Act. The agents and underwriters may also be entitled to contribution from us for payments they make relating to these liabilities.

Method of Sale

We may sell the securities in any of the following ways:

through underwriters or dealers;

directly to one or more purchasers;

through agents; or

through a combination of any of these methods of sale.

If underwriters are used in a sale, they will acquire the securities for their own account and may resell them in one or more transactions, including negotiated transactions, at a fixed public offering price or at varying prices determined at the time of sale. The securities may be offered to the public either through underwriting syndicates represented by managing underwriters or directly through underwriters. The obligations of the underwriters to purchase a particular offering of securities may be subject to conditions. The underwriters will also be obligated to purchase all the securities of an issue if any are purchased. Any initial public offering price or any concession allowed or reallocated or paid to dealers may be changed.

We may also sell the securities directly or through agents. Any agent will be named and any commissions payable to the agent will be set forth in the applicable prospectus supplement. Any agent will act on a reasonable best efforts basis for the period of its appointment unless the applicable prospectus supplement states otherwise.

We may authorize underwriters or dealers to solicit offers by certain institutions to purchase a particular offering of securities at the public offering price set forth in the applicable prospectus supplement or term sheet using delayed delivery contracts. These contracts provide for payment and delivery on one or more specified dates in the future. The applicable prospectus supplement or term sheet will describe the commission payable for solicitation and the terms and conditions of these contracts.

Table of Contents

The applicable prospectus supplement or term sheet will describe any restrictions on the sale of securities if and as appropriate.

Agents and underwriters may be customers of, engage in transactions with, or perform services for Legg Mason in the ordinary course of business.

Pursuant to a requirement by FINRA, the maximum commission or discount to be received by any FINRA member or independent broker/dealer may not be greater than eight percent of the gross proceeds received by us for the sale of any securities being registered pursuant to Rule 415 under the Securities Act.

Table of Contents

LEGAL MATTERS

The validity of the securities to be issued by Legg Mason will be passed upon by Thomas C. Merchant, Esq., our Executive Vice President and General Counsel, who as to matters of New York law may rely upon the opinion of Shearman & Sterling LLP, New York, New York. With respect to matters of New York law, the validity of the securities to be issued by Legg Mason will be passed upon for us by Shearman & Sterling LLP unless otherwise provided for in the applicable prospectus supplement. Mr. Merchant beneficially owns, or has rights to acquire under our employee benefit plans, less than one percent of our common stock.

Table of Contents

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in the Report of Management on Internal Control over Financial Reporting) incorporated in this prospectus by reference to the Annual Report on Form 10-K for the year ended March 31, 2015 have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

Table of Contents

\$450,000,000

4.750% Senior Notes due 2026

PROSPECTUS SUPPLEMENT

Joint Book-Running Managers

Citigroup

J.P. Morgan

Senior Co-Managers

HSBC

MUFG
Co-Managers

RBC Capital Markets

ANZ Securities
Morgan Stanley

BNY Mellon Capital Markets, LLC
Wells Fargo Securities

Credit Agricole CIB
UBS Investment Bank

March 17, 2016

