Permal Group Holdings Ltd

EnTrustPermal Ltd

Pillar III

Base date of PILLAR III:	31 March, 2018
Period of PILLAR III:	1 May 2017 to 31 March 2018

INTRODUCTION

In 2007 and 2008, the UK Financial Conduct Authority's ("FCA") new General Prudential Sourcebook and Prudential Sourcebook for Banks, Building Societies and Investment Firms ("BIPRU") rules came into effect, implementing the Capital Requirements Directive, which is the common framework for implementing Basel II in the European Union. These rules are built on three pillars:

- Pillar 1 – minimum capital requirements;
- Pillar 2 – rules for the Supervisory Review Process, including the Internal Capital Adequacy Assessment Process ("ICAAP");
- Pillar 3 – rules for the disclosure of risk and capital management, including capital adequacy.

The following is the Permal Group Holdings Ltd ("PGHL") and its subsidiaries' Pillar 3 disclosure in accordance with the requirements of the FCA's Rules.

Among PGHL's subsidiaries, EnTrustPermal Ltd ("EPL"), a UK-regulated Subsidiary of Permal Group Holdings Ltd ("PGHL"), accounts for the majority of the consolidated turnover of PGHL and is, therefore, deemed to be a significant Subsidiary. As a result, information is also presented in respect of EPL on an individual basis.

PGHL is part of the EnTrustPermal Group ("ETP Group"). ETP Group is a combined entity of EnTrust Capital and Permal Group formed on 2 May 2016 and is a leading global alternative asset manager specializing in providing investment solutions to public, corporate and multi-employer pension funds, foundations, endowments, sovereign wealth funds, insurance companies, private banks, family offices and high net worth individuals.

Risk is inherent in the businesses and activities of the ETP Group. PGHL and its subsidiaries follow an approach to risk management, which involves identifying and assessing the risks to which the ETP Group is exposed, and monitoring and managing such risks.

The following sections describe the approach of PGHL and its subsidiaries to risk management:

- Section 1 – Risk governance structure, strategy and process
- Section 2 – Categorisations of risk and the principal factors that drive each type of risk faced by the Group
- Section 3 – Monitoring and Reporting of Risk
- Section 4 – Consolidation principles for regulatory capital
- Section 5 – Capital resources

SECTION 1. RISK GOVERNANCE STRUCTURE, STRATEGY AND PROCESS

Risk Governance Structure and Process

The ETP Group's Management Committee has overall responsibility for the effectiveness of the control environment of PGHL and its subsidiaries. They are responsible for establishing internal policy. The operational risk management framework is reviewed on an ongoing basis, both formally and informally. ETP Group's Co-Chief Compliance Officers are responsible for ensuring the compliance with internal policies and procedures.

ETP Group's Risk Committee has the ultimate responsibility for deciding on limits for and monitoring of the risk exposure, as well as for setting the targets for the capital ratios and risk appetite. The Risk Committee decides on policies for risk management as well as the internal capital adequacy assessment. All policies are reviewed annually.

The ETP Group's Risk Committee has independent oversight of portfolio risks and is ultimately responsible for addressing inherent and exogenous risk factors in each portfolio and risk mitigation methodologies. The Risk Committee meets formally on a bi-weekly basis.

The Risk Committee reviews, considers, and focuses on such matters that relate to the ongoing operation of the business that impact or could have an impact on our clients. Given the broad nature of the Risk Committee's remit, it is not appropriate to exhaustively list the areas within its scope. However, areas of focus include but are not be limited to: conflicts of interest, valuation risk, counterparty risk, compliance and regulatory risk, reputational risk, trade execution risk, service provider risk, personnel related risk.

The ETP Group's Audit Committee, whose members include the Chairman and Chief Executive Officer, the Chief Financial Officer, the Chief Risk Officer and Chief Operating Officer, and the Global Head of International Business, meets on a quarterly basis and has responsibility for overseeing the overall risk infrastructure.

The Audit Groups, which are comprised of the internal audit department of Legg Mason Inc., the ETP Group's external auditors and Compliance, may periodically undertake relevant monitoring checks to confirm that risk policies and procedures are being implemented satisfactorily.

Risk Governance Strategy

As part of its strategy, PGHL and its subsidiaries accept calculated Group risks that it deems can result in positive consequences while attempting to mitigate as far as possible those risks that can have a negative impact.

SECTION 2. RISK TYPES

The different risks that could impact directly or indirectly its financial position are identified. PGHL and its subsidiaries aim to mitigate the impact of material risks noted below by implementing control policies and procedures. Other risks (counterparty, credit, market, concentration, interest rate, pension obligation and group risk, etc) are not deemed material enough to rise to the level of requiring inclusion in the list below.

- **Operational Risk** is the risk of loss resulting from inadequate or failed processes, people and systems. Due to the importance of maintaining effective operational controls in respect of its business activities, PGHL and its subsidiaries will usually only regard "low degree" as an acceptable level of post control operational risk. Major services are outsourced to specialist providers to reduce risks associated with back office functions necessary in connection with our asset management services (i.e. hedging services, administration services).

- **Liquidity Risk** is the risk from loss of mismatch of assets and liabilities maturities and risk of not being able maintain adequate capital in the foreseeable future. PGHL and its subsidiaries actively monitors its financial position to verify that it has sufficient capital to meet its requirements at all times and to take action where necessary. PGHL and its subsidiaries' liquidity needs do not require significant capital on a daily basis and based on the business model capital requirements do not unexpectedly vary.

- **Business Risk** is the risk of loss from business activities. This would include earnings volatility inherent in all business due to the uncertainty of revenues and costs as a result of changes in the economic, regulatory and competitive environment. PGHL and its subsidiaries exposure to business risk is reduced by means of the diversity inherent in our business model. All investment mandates look to protect investor capital in down markets via diversification. To mitigate business risk, ETP Group has a disciplined and rigorous investment selection process, including a Global Investment Committee that unanimously approves all investments and an Investment Risk Team that reviews investment returns and consequent risk by quantitative and qualitative analysis. Further, the client base is diversified across regions and client segment (e.g. institutional, High Net Worth).

SECTION 3. MONITORING AND REPORTING

The risk governance structure is designed to provide independent and objective assessments and monitoring of risks. The focus of the risk monitoring is two-fold: (i) Individual manager monitoring and (ii) Overall portfolio risk monitoring.

The risk monitoring and reporting processes involves risk and policy reviews which are conducted generally annually or on an as-needed basis as risks, assessments and controls and other mitigating factors change.

SECTION 4. CONSOLIDATION PRINCIPLES FOR REGULATORY CAPITAL

PGHL and its subsidiaries do not prepare consolidated statutory accounts, on the grounds that they are consolidated into the accounts of the ETP Group, then to Legg Mason, Inc., ETP Group's ultimate parent company.

PGHL is subject to consolidated supervision under the FCA rules. The following table sets out the Subsidiaries which are consolidated for the purpose of regulatory capital.

PGHL undertakings included in the capital base:

Name	Ownership %	Country	Consolidation method
LM Cayco Ltd	100%	Cayman	Fully consolidated
EnTrustPermal Ltd	100%	UK	Fully consolidated
Permal (Isle of Man) Limited	100%	Isle of Man	Fully consolidated
The St James Bank & Trust Company Ltd	100%	Bahamas	Fully consolidated
W&P Fund Services Ltd	100%	Bahamas	Fully consolidated
SaintCo Ltd	100%	Bahamas	Fully consolidated
SJBTC Ltd	100%	Bahamas	Fully consolidated
EnTrustPermal (Hong Kong) Limited	100%	HK	Fully consolidated
Permal Investment Consulting (Shanghai) Limited	100%	China	Fully consolidated (liquidating)
EnTrustPermal Business Consulting (Beijing) Company Limited	100%	China	Fully consolidated
EnTrustPermal SAS	100%	France	Fully consolidated

SECTION 5. CAPITAL RESOURCES

A. EPL's financial position and capital requirement (Pillar 1)

EPL's turnover for the financial year 17/18 was USD 72.2 million (FY16/17: USD 115.2 million). The total assets under management were USD 3.8 billion as of March 31st, 2018 (31 March 2017: USD 8.4 million).

The regulatory capital base of EPL, calculated based on the FCA rules applicable to Investment Firms, is as follows:

In USD'000s

	2018	2017
Tier 1 capital		
Paid up share capital	13,544	13,544
Share premium	0	0
Reserves	23,913	15,639
Tier 1 capital before deductions	37,457	29,183
Deductions from tier 1 capital		
Tier 1 capital after deductions	37,457	29,183
Tier 2 capital		
Perpetual subordinated debt	0	0
Tier 2 capital before deductions	0	0
Deductions from tier 2 capital	(1,143)	(2,148)
Tier 2 capital after deductions	(1,143)	(2,148)
Total capital base	**36,314**	**27,035**

Based upon its regulatory permissions and scope of activities, EPL is subject to the capital requirements for an Investment Firm. Its capital resources requirement is calculated as the higher of:

- The sum of the credit and market risk charges; and
- The fixed overheads requirement (FOR).

The FOR is calculated as 13 weeks' expenditure (excluding certain discretionary expenses) based on the most recent accounts.

The capital resources requirement of EPL as at 31 March 2018 is USD 8,182,000 (2017: USD 12,824,000).

As such, the regulatory capital base of EPL is in excess of the capital resources requirement.

B. PGHL and its subsidiaries' financial position and capital requirement (Pillar 1)

PGHL and its subsidiaries forms a UK consolidation Group and because the subsidiaries include The St James Bank and Trust Company Ltd. it must apply the FCA's Prudential Rules that apply to Banks. The following table sets out the calculations of PGHL and its subsidiaries regulatory capital base, as at 31 March 2017 and 2018:

In USD'000s

	2018	2017
Tier 1 capital		
Paid up share capital	27,681	27,681
Share premium	959,818	947,894
Reserves	-931,405	-932,781
Tier 1 capital before deductions	56,094	42,794
Deductions from tier 1 capital	0	0

Tier 1 capital after deductions	56,094	42,794
Tier 2 capital		
Upper tier two capital instruments	0	0
Tier 2 capital before deductions	0	0
Deductions from tier 2 capital	0	0
Tier 2 capital after deductions	0	0
Tier 3 capital		
Short term subordinated debt	0	0
Total capital base	**59,094**	**42,794**

PGHL has the ability to transfer capital within its subsidiaries and other affiliates within the Group without material restrictions.

The capital requirement for PGHL and its subsidiaries is comprised of the sum of credit risk, market risk and operational risk requirements according to the FCA Rules applied to Banks. The following table summarizes these as at 31 March 2017 and 2018:

In USD'000s

	2018	**2017**
Credit Risk	6,663	5,955
Market Risk	2,956	2,606
Operational Risk	6,065	7,228
Total	**15,684**	**15,789**

As such, the capital base of the UK consolidated Group is in excess of the regulatory capital requirement.

The detail of above 3 risk requirements are listed below:

- Credit risk capital requirement

PGHL and its subsidiaries uses the standardised approach to credit risk, under which the capital requirement is calculated as 8% of the risk weighted exposure amounts. Risk weighted exposures are obtained by multiplying the exposures by the risk weights set out in the FCA rules.

The following table analyses the calculation between the standardized credit risk exposure classes:

In USD'000s

	2018		**2017**	
	Exposure	**Capital requirement**	**Exposure**	**Capital requirement**
Local authorities	325	0	594	0
Financial institutions	29,404	470	28,083	449
Corporate	76,413	6,113	66,888	5,351
CIU	36	3	51	4
Other items	959	77	1,886	151
Total	**107,137**	**6,663**	**97,502**	**5,955**

- Market risk capital requirement

PGHL and its subsidiaries calculates its market risk capital requirement using the interest rate *position risk requirement*. ("PRR"), equity PRR, collective investment undertaking PRR and foreign currency PRR methods set out in the FCA rules. The following table analyses the market risk capital requirement:

In USD'000s

	2018	2017
Interest rate PRR	0	0
CIU PRR	0	0
Foreign currency PRR	2,956	2,606
Total	**2,956**	**2,606**

The capital requirements are calculated as a percentage of the exposure according to the FCA handbook. For example, the collective investment undertaking PRR is 32% and the foreign currency PRR is 8%.

- Operational risk capital requirement (ORCR)

PGHL and its subsidiaries calculates its operational risk capital requirement according to the basic indicator approach (BIA). Under this method, the ORCR is calculated by taking 15% of the 3-year average of the projected sum of net interest income and net non-interest income.

The capital requirement for operational risk amounts to USD 6,065,000 as of March 31, 2018.

Internal Capital Adequacy Assessment Process ("ICAAP")

Under Pillar 2 of the FCA's capital requirements, PGHL and its subsidiaries has undertaken an assessment of the adequacy of capital based upon all the risks to which the business is exposed ("ICAAP").

The Senior Management has determined that the following material risks are faced by PGHL and its subsidiaries and could potentially, in the case of them crystallizing, result in the need for additional capital:

- Operational risk: loss of key business members
- Business risk: poor client portfolio performance resulting, for example, from:
    - poor investment decisions
    - unanticipated changes in the markets and/or exchange rates
- Business risk: redemptions resulting, for example, from:
    - liquidity needs of investors
    - poor performance of client portfolios
    - lower fee paying products representing a large portion of the AUM
    - reputational issues relating to the industry or the ETP Group
    - bear market / market crash?

Methodology

Senior Management believes that in the case of one or all of the risks crystallising, the outcome would be the same: a decrease in assets under management due to either negative client investment performance and / or a dramatic increase in net redemptions from the clients. As a result, Senior Management has decided to perform a sensitivity analysis with respective to capital requirements based on the variation of the above two sensitivity factors over a 12-month period.

Results of sensitivity analysis

EPL has a positive working capital (i.e., it receives its revenues before having to pay its counterparties). This is due to the fact that most of the fee revenues are received monthly, whereas fee payments for third party distribution are paid quarterly. Additionally, EPL has a relatively small balance sheet structure to finance.

In summary, PGHL's business model automatically finances itself. Due to the decrease of AUM and relating fees in FY17-18, PGHL's capital requirement is sensitive to the fund performance and redemption with an unchanged operating fixed cost. As a result, a combined identical decrease in Funds' performance and an increase of net redemptions between 10% and 50% can vary PGHL's capital requirements from $5,754,000 to $17,988,000.

Conclusion of respective capital requirements

As at March 31st, 2018 on the basis of unchanged operating fixed costs, financial investments, off balance sheet investments and preferred share dividend:

- EPL's current capital structure would be sufficient, even in the event of risks crystallizing at the same time over a 12-month period as set out above in the Results section. EPL's excess of capital after consumption of capital required to finance operations for the next 12 months would be sufficient.

- Similarly, PGHL and its subsidiaries current capital structure would be sufficient even in the event of a combined identical variation over a 12-month period as set out above in the Results section. The Group's excess of capital after consumption of capital required to finance operations for the next 12 months would be sufficient.

A 12-month period is expected to provide Senior Management with sufficient time to take the appropriate action in terms of balance sheet and profit and loss restructuring (for example, liquidation of seed money investments, among other liquid asset sales and fixed cost reductions).

As a result of the above, Senior Management has assessed that EPL and PGHL and its subsidiaries are sufficiently capitalised for the risks to which they are exposed.

Pillar 3 remuneration disclosures for EnTrustPermal Ltd (the "Company")

April 2017 – March 2018

Decision making process for remuneration policy

The Company has a Compensation Committee which meets regularly to consider human resource issues relating to terms and conditions of employment, compensation and retirement benefits. Within the authority delegated by the Board, the Compensation Committee is responsible for:

- Reviewing and approving remuneration policy and structures for all employees designed to ensure alignment with the Company's business strategy, objectives, values, risk appetite and long-term interests.
- Overseeing implementation of the remuneration policy and an annual review of the implementation of remuneration policy is conducted.
- Reviewing and approving all remuneration decisions for Management Committee members, Code Staff and employees with remuneration over a pre-determined amount.
- Approving all individual bonus awards taking into account both current and future risks to the Company's prudential soundness.
- Remuneration of senior officers working in control functions designed to ensure that their remuneration aligns to remuneration policy.
- Variable remuneration decisions designed to ensure that decisions consider financial and non-financial metrics, and the performance of the individual and the Company.
- Review and approval of severance payments, guarantees and buyouts.
- Approval of any periodic disclosure to a regulator or any other relevant authority relating to the remuneration policy.

There were 3 resolutions passed by the Compensation Committee during the financial year ending 31 March 2018.

The members of the Compensation Committee for the period April 2017 to March 2018 were Gregg Hymowitz (Chairman and Chief Executive Officer), Jill Zelenko (Senior Managing Director, COO and CRO), François Becquaert (Senior Managing Director and Chief Financial Officer) and Omar Kodmani (Senior Executive Officer). Gregg Hymowitz was Chairman of the Committee throughout the period.

External consultants

Consultants are used from time to time to advise on specific issues.

During the year, François Becquaert (Senior Managing Director and Chief Financial Officer) provided regular briefings to the Committee and the Committee received advice on the implications of the remuneration policy on risk and risk management from the Jill Zelenko (Senior Managing Director, COO and CRO) Michael McDonough (Senior Managing Director, General Counsel and CCO – International) and Michelle Parfitt (Managing Director, Human Resources).

Role of the relevant stakeholders

The Compensation Committee takes full account of the Company's strategic objectives in setting remuneration policy and is mindful of its duties to its shareholder and other stakeholders. The Committee seeks to preserve shareholder value by ensuring the successful retention, recruitment and motivation of employees.

In line with the Financial Conduct Authority ("FCA") regulations, 11 employees were designated as "Code Staff", defined as SIFs, heads of significant business functions, heads of support and control functions and risk takers.

This group is defined with reference to managerial responsibility to influence the Company's overall risk profile. This does not include portfolio managers or sales staff without wider executive responsibilities, as these are not deemed to have a material impact on the Company's risk profile given the control structures in place and the agency nature of the Company's business.

The Code Staff list is reviewed annually or following a material change in personnel.

The link between pay and performance for Code Staff

The Management Committee and Compensation Committee take into account, when determining remuneration awards, the need to ensure an appropriate ratio between fixed and variable pay to ensure that the Company can operate a fully flexible incentive policy. This includes the potential non-award of bonuses should Company performance and/or the performance of specific individuals require it.

If all or part of the business has made a loss, or if an employee breaches accepted risk or compliance behaviour and the Compensation Committee believe it to be appropriate, the Company has the ability to not award a bonus.

The bonus pool is calculated in accordance with a percentage of consolidated run rate gross margin/profit approved by the Compensation Committee.

Legg Mason, Inc. may issue stock options to certain directors and key employees of the Company. Options under Legg Mason's employee stock plans have been granted at prices not less than 100% of the fair market value. Options are generally exercisable in equal increments over 3 to 5 years and expire within 5 to 10 years from the date of grant.

Aggregate remuneration cost for Code Staff

The aggregate remuneration expenditure in respect of Code Staff was £21.5 million for the period (all Code Staff being classified as senior management or risk takers).

There were 2 leavers during the period 1 April 2017 – 31 March 2018

Robert Kaplan	31 March 2018
Michelle Parfitt	31 March 2018