

# ... Risk Management ...

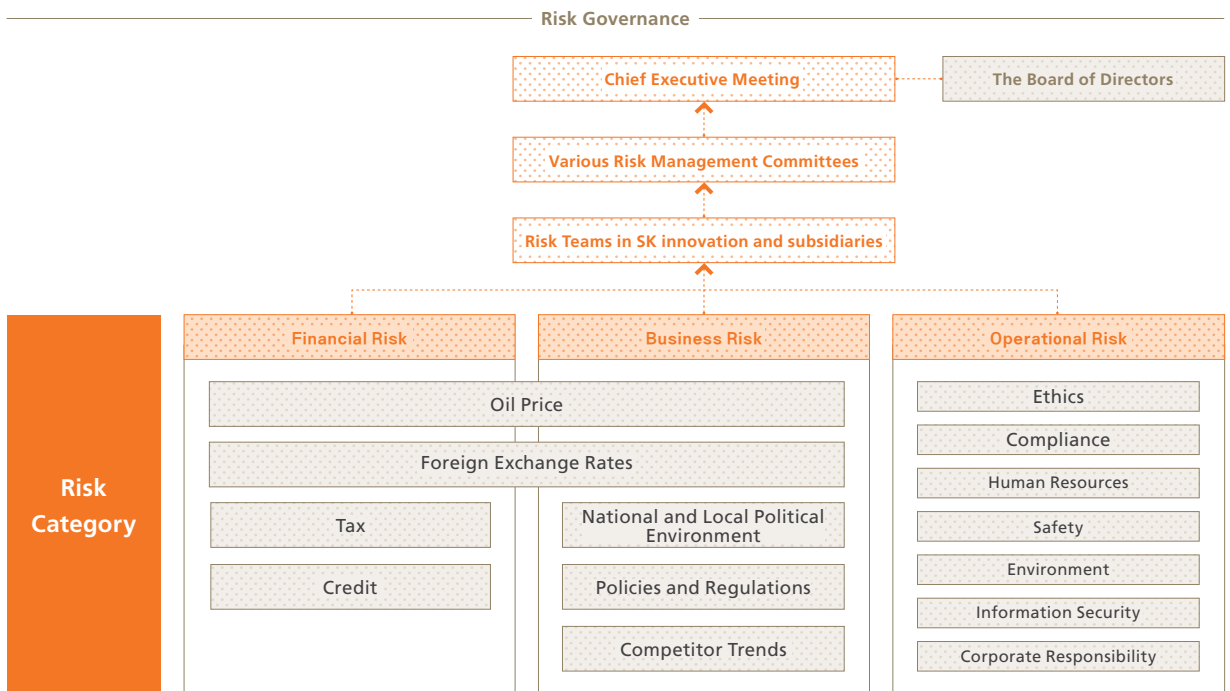
The global energy industry faces various risks amid a rapidly changing business environment. On one side, investors require conventional oil and gas producers and refiners to respond to the risks related to climate change, while on the other, increasing social interest and improved technology related to renewable energy and other forms of eco-friendly energy are in a position to significantly impact the future profit model of the conventional energy industry. SK innovation takes an organized approach to the key risks that it may face to develop the best approach to monitor and respond to each risk.

## Risk Reporting and Governance

SK innovation categorizes its risks into three categories—financial risk, business risk, and operational risk. Business risk is managed by the Risk Teams at SK innovation and its subsidiaries. Any issues that require a decision by senior management are discussed at the Risk Committee, in which the CEOs and senior executives of the relevant departments participate. Operational risk, including subsidiary risk, is managed comprehensively by reach of the relevant departments at SK innovation. In the event of a decision is required from SK innovation senior management or its subsidiaries, the issue will be discussed at the Chief Executive Meeting held each month based on the type or risk. In addition, due to the close business relevance between SK innovation and its affiliates, certain key risks will be discussed at the Chief Executive Meeting(held third times a month) under the presence of SK innovation’s CEO and the five affiliate CEOs. If necessary, some risk agenda may be reported to the Board of Directors.

## Analysis and Monitoring

SK innovation performs analysis and monitoring optimized for each type of risk. For financial risks such as oil price and foreign exchange movement, which have an immediate impact on business performance, we analyze short-term direction and mid-term trends for SK innovation and each subsidiary based on various economic indicators. Based on the conclusion, risk thresholds are set and managed. In the case of business and operational risk, the company monitors relevant laws and regulations, policy trends, and key stakeholder opinions on a daily basis. This information is shared through newsletters and the company’s intranet to ensure all employees are aware of key trends and engaged in their own risk prevention measures.



**Mid- and Long-Term Risk Identification and Response**

SK innovation regularly analyzes changes in society and environment to identify long-term risk factors that may impact the overall business, and to form and implement strategies to effectively respond to these risks.

Emerging Risks	Business Context
 <p><b>Unstable Oil Price and Financial Risk</b></p>	<ul style="list-style-type: none"> <li>• A volatility in oil price can impact the refining and petrochemical industry via various channels, including refining complex margins and petrochemical cash margins. Following the steep fall in oil prices triggered by US oversupply in late June 2014, oil prices have started to recover from the first half of 2015, but uncertainties still remain.</li> <li>• In particular, at the current time the company is increasingly sensitive toward global economic trends, due to its large portion of overseas exports. In China, which is one of the largest sources of demand, there is a prolonging trend of economic slowdown and increasing localization.</li> </ul>
 <p><b>Environment and Climate Change</b></p>	<ul style="list-style-type: none"> <li>• In the petrochemical industry, the topic of carbon emissions and climate change is a core agenda. The influence on business has increased since COP 21.</li> <li>• In addition to government’s regulations on GHG emissions, more investment in new renewable energy and GHG emission reduction R&amp;D is expected to initiate and accelerate change in the energy paradigm.</li> </ul>
 <p><b>Product Sales and Business Relations (Fair Trade)</b></p>	<ul style="list-style-type: none"> <li>• More transparent and fair business activities are required, due to tighter legal regulations on ethical management, and increasing demands from direct and indirect stakeholders, including agents, for broader transparency.</li> <li>• In addition, gasoline supply prices include a mix of different cost factors, such as international gasoline prices, international crude oil prices, and changes in oil import prices. However, lower crude oil prices have been not fully reflected in oil supply prices, which have led to consumers questioning whether companies are exploiting the situation, which is emerging as a potential risk.</li> </ul>
 <p><b>Personal Information Protection</b></p>	<ul style="list-style-type: none"> <li>• Negative incidents, such as customer personal information being leaked by employees of certain financial institutions in Korea, have led to growing interest in the topic of personal information protection.</li> <li>• More legal and regulatory requirements have been put in place, such as stronger Information Security Management System(ISMS) certification obligations and requirements to notify customers about personal information collection and use. Supervision and monitoring by government bodies is also increasing.</li> </ul>

Risk Impacts	Mitigation Action
<ul style="list-style-type: none"> <li>• Feedstock crude oil and petroleum products entail the risk of P&amp;L and cash flow profiles changing according to international price trends, which could result in unstable margins.</li> <li>• Global oil prices are driven by various economic, legal, political and climate conditions. Oil imported from locations like the Middle East require long-distance shipping, which creates a risk due to the difference in the oil price in the month of loading vs. in the month of arrival. Oil price expectations may directly influence financial performance.</li> <li>• Unexpected moves in fx rates can impact sales volume, prices, and crude oil prices, which ultimately can result in direct gains or losses in profitability.</li> </ul>	<ul style="list-style-type: none"> <li>• Using our deep industry knowledge, the company will apply optimization to the oil refining process, to distinguish the difference in oil by region, and pursue oil diversification optimized to the production of petroleum products.</li> <li>• SK innovation has created and executed a fx<sup>1)</sup> risk management policy to hedge any expected loss from fx volatility. The company has defined an acceptable fx risk ceiling and hedges any excess foreign currency positions to minimize the risk from fx movement.</li> </ul> <p><sup>1)</sup> foreign exchange</p>
<ul style="list-style-type: none"> <li>• There is a risk that the company may need to purchase carbon credit under emission trading, and manufacturing costs may increase due to investments needed to cut GHG emissions.</li> <li>• We expect demand for petroleum products to decrease on the back of the government's energy consumption mitigation policy.</li> </ul>	<ul style="list-style-type: none"> <li>• SK innovation manages GHG emissions at all worksites and mitigates carbon emissions through facility investment.</li> <li>• In addition, the company will establish a mid- to long-term response strategy to adapt to a paradigm shift in energy sector, and concentrate on investing in new businesses and developing technology for sustainable growth and development.</li> </ul>
<ul style="list-style-type: none"> <li>• Fair trade related legal and regulatory violations can have serious risk implications from various fines to damaging a company's reputation.</li> <li>• In addition, changes in sales price due to oil price movements may have a negative impact on consumer and brand confidence.</li> </ul>	<ul style="list-style-type: none"> <li>• Fair trade risk is mitigated by creating a fair trade voluntary compliance framework, such as introducing a Fair Trade Voluntary Compliance program. In addition, the company is increasing internal monitoring and enhancing fair trade awareness within the organization.</li> <li>• In addition to engaging in R&amp;D activities to provide customers with differentiated products and services, the company has continuously enhanced the value of its gas station network by analyzing the commercial district of each gas station and identifying and positioning the best complimentary business for the gas station to strengthen its competitiveness.</li> </ul>
<ul style="list-style-type: none"> <li>• The gas station business requires strong bonds with our customers, therefore, proper management of customer information is a key issue to growth. An absence of an information management system may lead to serious negative influences on customer communication and marketing.</li> <li>• In light of stronger government regulations, the company's brand can be dealt a serious blow from single incident, such as a criminal prosecution against an executive. There have been actual cases where executives of a major telecom operator in Korea were charged for negligent management of personal information, resulting in damaging the company's reputation.</li> </ul>	<ul style="list-style-type: none"> <li>• With the aim of improving its customer information protection framework and responding to government regulations, SK innovation has strengthened its Personal Information Management System(PIMS) certification maintenance and management. Through these efforts, the company can take preemptive action to respond to possible personal information leaks.</li> <li>• SK innovation is implementing a tighter internal control process, including continuous implementation monitoring and strict control on access to customer information. In addition to internal control, the company conducts regular and non-regular inspections on outsourced service providers regarding customer information management, and provides training on improvement measures to prevent events.</li> </ul>