

Our approach to risk management

Because of the specific nature of the fuel sector, the LOTOS has a strategic approach to minimizing prospective risks likely to affect performance of our business objectives, as well as the social environment where we operate adversely. By identification, constant monitoring and strategic approach to management we reduce hazards day by day.

Throughout 2015, as part of the Enterprise Risk Management (ERM) system, we undertook a number of risk mitigation measures reducing the probability that specific risks may materialize. In the case of risks that did materialize, we applied the action plans prepared in advance, successfully limiting their adverse effects. We also defined new risks, mainly associated with projects of crucial importance to the LOTOS Group (such as [EFRA](#) or [B8 field](#) development). A number of measures were also being implemented to improve the risk management tools and risk identification, assessment and monitoring methodologies.

At the LOTOS Group, we identify a range of risks in all areas of our business. Many of them are interrelated, so we analyse their interactions and take steps to minimize their impact.

Key risk groups for the LOTOS Group



Risks are identified in reference to the strategic and operational objectives pursued by the organization. Risk assessment is performed based on a defined and approved risk matrix, and includes analysis of the likelihood of the risk materialization and possible financial and reputational consequences, where the latter are understood as damage to reputation, environment or people's health. All identified risks are monitored, and those considered as material are subject to more stringent control requirements.

Key elements of risk and opportunity management at the LOTOS Group



- **Risk identification** – risks are identified in reference to the strategic and operational objectives pursued by the organization.
 - **Risk assessment** – risks are assessed in the annual and long-term perspectives in terms of their potential consequences for the LOTOS Group’s financial standing and reputation (including adverse impact on the LOTOS Group’s image, the environment and people’s health).
 - **Risk analysis** – for each risk, we define the current management procedure as well as monitoring and protection measures, and if a risk is deemed material, detailed risk management charts are prepared. The charts specify how a given risk should be mitigated and what actions to take should it materialize. Key risk indicators (KRI) are defined, by means of which the risk and the level of exposure can be monitored in accordance with established guidelines. Risk owners are responsible for the above elements of risk analysis.
 - **Risk reviews** – all identified risks are periodically reviewed and updated, twice a year as a minimum.
 - **Process reporting** – appropriate standards have been implemented for communicating and reporting the results at each stage of the process.
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Roles in the risk management process:

- The Supervisory Board – monitors the effectiveness of the risk management system.
- The Board of Grupa LOTOS – makes key ERM decisions and approves risk maps.
- Segment heads – are responsible for overall monitoring and supervision of risk management in their segments.
- Enterprise Risk Management Committee – recommends ERM-related actions and monitors their progress. The Committee consists of representatives of each segment.
- Enterprise Risk Coordinator – coordinates and supports risk management activities within the LOTOS Group.
- Risk owners – manage individual risks, defining the course of action with respect to each risk and monitoring its levels.
- The LOTOS Group employees – implement risk mitigation activities and identify new risks.
- Internal Audit Office and Business Process Management Office – carry out audits at LOTOS Group companies to review the implemented controls and evaluate their effectiveness, identify and assess threats to the organization's operations, carry out annual evaluations of the risk management system's effectiveness as part of the organizational maturity assessment, and assess individual risk management procedures.

Enterprise risk management activities at the LOTOS Group are supported by a dedicated IT tool, the ERM Portal. The ERM Portal is used to record risks and risk assessment results and prepare risk maps, to monitor current risk indicators and the progress of planned actions, as well as for reporting purposes. Audit results are also recorded in the ERM Portal where the audit involves a review of the risk management procedures.

How is the system's effectiveness evaluated?

The ERM system's effectiveness is evaluated every year, as part of our [organizational maturity assessment](#), the conclusions and recommendations of which are used to further improve the system. A final assessment score is expressed as a percentage and reflects:

- The degree to which the system designed at the Company conforms with best practices and standards for a given area, and
- Conformity of the system's operation in practice with the system's design.

In the period from 2011 (when the system was launched at the organization) to 2015, the assessment score rose to 96%. Risk is inherent in Grupa LOTOS' business. The risk management system, being a strategic business process at the organization, is subject to constant improvement.

Implementation costs of hedging strategies

The costs of hedging strategies depend on the materiality of the risk and the potential benefits derived from hedging. Whenever possible, risk is reduced to a level considered economically acceptable. Furthermore, when preparing risk analyses or action plans, potential costs are among the factors considered in making the final decision. This approach enables us to deploy the financial resources required for risk management in the most efficient manner possible.

What are other manifestations of our precautionary approach?

- The [Code of Ethics](#): sets the standards of conduct in line with the LOTOS Group values.
- Agreements: include appropriate provisions governing cooperation with partners.
- Environmental protection and OHS standards: ensure the highest standard of people's and process safety.
- Project management: ensures proper project implementation and budget control.
- Controlling: supervision over the current budgets.