


<b>ENCE ENERGÍA Y CELULOSA</b>			
NAME	<b>RISK MANAGEMENT AND CONTROL POLICY</b>		
DEPARTMENT	INTERNAL AUDIT		
PROCEDURE:	DAI-02	DATE	February 2016
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VERSION CONTROL		
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## 1.- Objective

The objective of this document is to formalize the risk management and control Policy applied at Ence Energía y Celulosa, S.A. and in all the companies that are part of its Group (hereinafter Ence).

By applying this Policy, Ence undertakes to develop all its capacities so that all the risks, irrespective of the nature, faced by the aforementioned to achieve its objectives are duly managed; in other words, identified, assessed, reviewed, prioritized and addressed. This commitment is made by the Board of Directors and is under its direct responsibility, as is stipulated in the Rules of this Board.

This Policy defines the contribution of risk management to the Corporate Governance structure of Ence and includes the definition of competence, functions and responsibilities concerning the various members of the organisation who are involved in the risk management of the Group.

The Risk Management System defined in this Policy is complemented by the Risk Management and Control Procedure, by the System of Internal Control over Financial Reporting (ICFR) and the System of Internal Control over Non-Financial Reporting (ICNFR) implemented at Ence, in accordance with the requirements established by the National Securities Market Commission (CNMV) in these matters.

The methodology of this risk management and control Policy is based on the framework defined by COSO (Committee of Sponsoring Organizations of the Tradeway Commission) in the ERM (Enterprise Risk Management 2017) model for Risk Management *“Integrating with Strategy and Performance”*.

## 2.-Regulatory Framework

The two rules that govern and establish the key points for risk management of companies are the Capital Company Act and the Good Governance Code of the National Securities Market Commission for listed companies. Both references are aligned with their general provisions regarding risk management.

Article 529 (3) of the Capital Company Act states the non-delegable powers of the Board of Directors of a Company, comprising “determination of the risk management and control Policy, including risks of a fiscal nature, and the supervision of internal reporting and control systems”.

Likewise, Article 529 (14) states the minimum functions that that Audit Committee must have assigned, which include “supervise the effectiveness of the internal control of the company, the internal audit and the risk management systems, including risks of a fiscal nature, as well as discuss any significant weaknesses with the auditor concerning the internal control system which are detected when the audit is conducted”.

The Good Governance Code of listed companies (the Good Governance Code), approved by Agreement of the Board of the National Securities Market Commission on 18 February 2015, includes recommendations concerning risk management in listed companies:

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- The risk management and control Policy should identify at least:
  - ✓ The different types of financial and non-financial risk the company is exposed to (including operational, technological, financial, legal, social, environmental, political and reputational risks), with the inclusion under financial or economic risks of contingent liabilities and other off-balance-sheet risks.
  - ✓ The determination of the risk level the company sees as acceptable.
  - ✓ The measures in place to mitigate the impact of identified risk events should they occur.
  - ✓ The internal reporting and control systems to be used to control and manage the above risks, including contingent liabilities and off-balance-sheet risks.
  
- Companies should establish a risk management and control function in the charge of one of the company's internal department or units and under the direct supervision of the Audit Committee or some other dedicated Board of Directors committee. This function should be expressly charged with the following responsibilities:
  - ✓ Ensure that risk control and management systems are functioning correctly and, specifically, that major risks the company is exposed to are correctly identified, managed and quantified.
  - ✓ Participate actively in the preparation of risk strategies and in key decisions about their management.
  - ✓ Ensure that risk control and management systems are mitigating risks effectively within the framework of the Policy drawn up by the Board of Directors.

### 3.- Scope and application

This risk management and control Policy is applicable to all the companies and businesses that are part of the Ence Group, with these being understood as each and every one of the businesses in whose share capital the company Ence Energía y Celulosa, S.A. has, directly or indirectly, the majority of the shares, interest or voting rights, or in whose governing or administrative body it has appointed, or it has the power to appoint, the majority of its members, in such a way that it effectively controls the company.

The risk management and control Policy is applicable to all direct and indirect participants in the Ence Risk Management Process.

This process covers all types of risk that may threaten the achievement of the objectives defined by Ence.

All employees, managers, administrators and collaborators of Ence have a responsibility to contribute to the risk management process in an efficient and effective way.

### 4.- Risk management

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Risk management is a continuous process carried out by the organisation applied in the definition and execution of the strategy and designed to identify, assess and address risks which, in the event that they emerge, may have a negative effect on the achievement of the objectives of the Group, keeping them within a risk appetite which is considered acceptable.

Each one of the parties involved in the risk management process has specific responsibilities and functions defined and assigned in accordance with the “COSO Enterprise Risk Management —Integrating with Strategy and Performance” model.

Ence is aware of the importance of risk management in order to comply with the expectations of its “stakeholders”, considering the risk/profitability relationship, hence this is an organisation which does not oppose risk.

Ence firmly believes that risks must be suitably managed and not just eliminated. The Ence risk management and control Policy therefore involves suitable and effective risk management, which will allow the company to:

- From an outside perspective:
  - ✓ Create and protect value for shareholders.
  - ✓ Build trust among its stakeholders (shareholders and investors, providers, customers, regulators, employees, forest owners, suppliers, public administrations, neighbours, NGOs, etc.).
  - ✓ Ensure that the laws and recommendations concerning Corporate Governance are observed.
- From an inside perspective:
  - ✓ Achieve its goals and objectives.
  - ✓ Offer support in the decision-making process.
  - ✓ Strengthen the internal control environment.
  - ✓ Improve supervision.

Furthermore, Ence considers that, for suitable risk management, it is essential for the highest level of transparency to be maintained as regards the information provided, both inside and outside the organisation. In this respect, Ence staff must bear in mind that the information provided on risk management must meet the following requirements:

- ✓ It is complete, ensuring that all relevant information is transmitted for suitable risk management.
- ✓ It is correct and accurate, ensuring that the information transmitted does not contain any errors or bias.
- ✓ It provides value, as it encourages the development of a risk control and management culture.
- ✓ It is appropriate, in other words, it must be transmitted on time; at the time at which is known and it is relevant for suitable risk management.

## 5.- Risk management objectives

The main risk management objective is to integrate the information from different companies, functions,

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areas or departments to give an overall view and, therefore, be able to work with the risks in an efficient way, once the strategy and the objectives of the Organisation have been established, in accordance with the methodology defined in “COSO Enterprise Risk Management —Integrating with Strategy and Performance”.

In particular, the tasks associated with risk management are intended to achieve the following objectives:

- **Be part of and support decision-making processes.**

The activities carried out are focused on supporting managers of the organisation in the decision-making process in a qualified way and in accordance with a certain methodology.

Likewise, it is an additional objective to that of risk management to improve the degree of efficiency of information available for decision-making and its use in the processes which are planned within the organisation, taking into account the context of the limitations brought about by any possible risk situations that may arise.

- **Obtain reasonable assurance regarding the achievement of objectives.**

The objective of risk management at Ence is to process the aspects of decision-making which are considered to be uncertain, in order to:

- ✓ Increase the likelihood of achieving the objectives of the company.
- ✓ Improve knowledge transfer skills concerning risk management aimed at improving management of the other units of the organisation.
- ✓ Avoid unexpected situations, minimizing the occurrence of unexpected events.
- ✓ Offer an alert system which makes it possible to anticipate potential problems.

- **Define risk profile.**

The objective of risk management at Ence is to ensure that the activities of the different areas of business are in line with the risk level considered suitable by the Group, in accordance with the objectives and priorities of the organisation.

- **Facilitate a common language and methodology concerning risks.**

The objective of risk management at Ence is to ensure a common and unique understanding of risk, documented in a set of solid and consistent measurement rules, procedures and methodologies.

- Furthermore, it is intended to establish action guidelines which are common in order to introduce the risk management process in the various companies of Ence. **Permit efficient allocation of resources.**

The objective of risk management at Ence is to reflect the risks that have a greater impact on the objectives of the Company, in such a way that allows for prioritization of the allocation of resources, focused on areas where risk is more critical.

- **Establish guidelines for Good Corporate Governance.**

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The goal of risk management is to provide a suitable base for integrating the risk management and internal control processes, as an essential part of effective principles of Good Corporate Governance.

- **Assign responsibilities to participants in the process.**

Lastly, the objective of risk management at Ence is to define the roles and responsibilities of the participants, guaranteeing a suitable segregation of functions between those who are directly responsible for risk management (risk owners) and those who are responsible for the development, implementation and maintenance of the risk management and control Model.

## 6.- Risk management principles

The Risk Management System at Ence is based on the following principles:

Risk Management:
<ul style="list-style-type: none"> <li>✓ Creates value for the organisation.</li> <li>✓ Is an integral part of all Ence processes.</li> <li>✓ Is part of decision-making processes.</li> <li>✓ Explicitly deals with uncertainty.</li> <li>✓ Is systematic, structured and suitable.</li> <li>✓ Must be based on the best information available.</li> <li>✓ Is tailored to the organisation.</li> <li>✓ Considers human and cultural aspects.</li> </ul>
<ul style="list-style-type: none"> <li>✓ Is transparent, effective and inclusive.</li> <li>✓ Is dynamic, repeatable and responds to change.</li> <li>✓ Facilitates the continuous improvement of Ence.</li> </ul>

Table 1: Risk Management Principles at Ence.

## 7.- Risk categories

Risk is considered as “any potential event that may have a negative effect on the achievement of the business objectives”. In this respect, Ence has identified the following types of risk:

- **Environmental risks:** situations that may involve possible losses in value or income derived from uncertainty linked to changes in the business scenario, competition and the market or changes in the legal and political framework (economic environment, customer behaviour, competitors, changes to laws, relationships with administrations, relationships with the local area, sale price).
- **Information integrity risks:** situations that may involve possible errors derived from an incorrect process of formulating information that may be useful for decision-making (strategic planning, environmental analysis, evaluation, financial and accounting information, fiscal and tax information).

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- **Legal risks:** situations derived from a breach of rules inside and outside the company, and from conflicts with third parties (formalization of contracts, regulatory compliance, arbitration and litigation, criminal risk, compliance with the System of Internal Control over Financial Reporting).
- **Financial and fiscal risks:** situations that may lead to possible losses in the income and net worth derived from variations in the interest rates, exchange rates, in liquidity, delinquency, capital availability, financing, fiscal risk and counterparty risk of trade transactions.
- **Operational risks:** arising from Ence operations (production, customers, providers, suppliers, technology and reporting systems, fraud, human capital, environment and surroundings).
- **Organisational risks:** situations that may lead to possible losses as a result of Human Capital management, fraud, Systems management, Business Continuity or Corporate Governance.
- **Climate change-related risks:** situations that may lead to possible losses as a result of the change in the global climate of the Earth due to natural causes and human action, and which occur on all climate variables (temperature, rainfall, cloudiness, etc.). These may be grouped into physical (damage to facilities), transitional (political and legal, market and reputation) and other risks, such as those in the supply chain and social phenomena.

For each of the risks identified, an additional classification is carried out by means of a category that identifies any risks with ESG-related conditions, which are those linked to environmental, social and governance events that may have an impact on an entity.

In this respect, Ence applies the principles and practices of the Enterprise Risk Management (ERM) Model to risks with ESG-related conditions by applying the “*COSO Enterprise Risk Management – Integrating with Strategy and Performance*” framework.

## 8.- Risk appetite

Risk Appetite is defined as the “risk level” that the company is willing to accept to achieve its objectives.

Ence recognises that its risk appetite varies according to the activities carried out and that its degree of risk acceptance is contingent on ensuring that the potential benefits and risks are fully understood prior to decision-making and, where appropriate, reasonable measures are put in place to manage such situations.

Based on the relationship between risk and profitability, Ence analyses each situation to assess how willing the organisation is to deal with these types of situations. In this respect, the analysis involves factors such as strategy, stakeholder expectations, current legislation, the environment, and relationships with third parties. Accordingly:

- Ence adopts a **zero risk appetite** for all situations in which the health and safety of employees and collaborators could be compromised, a priority in its actions.
- Ence adopts a **zero risk position** for all situations in which the operation or execution of any activity may cause damage to the surroundings and environment.

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- Ence has an **approach for minimising its exposure** to situations that are related to compliance with the laws and regulations that affect the company.
- Ence has a team of external advisors as well as specialised internal staff who have set internal guidelines for **tax compliance and zero risk assumption** in this area.
- Ence adopts a **moderate risk appetite** for situations related to the research, development and innovation of its products, aimed at providing solutions that fully meet the needs of its customers and becoming a benchmark in the cellulose market.
- Likewise, aware of the current difficulties in relation to the economic environment in which it operates, Ence is committed to establishing financial discipline that will enable it to keep the organisation's total debt under control and provide it with sufficient liquidity to meet its payments and priority investments. In this respect, **Ence adopts a low risk appetite** for financial transactions.
- However, a large volume of Ence's operations are associated with the exchange rate between the US Dollar and the Euro. Ence, aware of the situation of the economic environment and the evolution of the exchange rate between the two currencies, adopts a **low risk appetite** in this area through rigorous management in accordance with the guidelines set by the Board of Directors Executive Committee and, where appropriate, the Finance Department.

## 9.- Risk management framework at Ence

### 9.1 Risk management framework.

The Ence risk management framework is based on the COSO-ERM model for enterprise risk management and it can be summed up by the fact that Ence, as an organisation that has a vision, a mission, a purpose and certain values, endeavours to achieve its goals by adopting and implementing a global strategy which brings together specific objectives from four different perspectives; strategic objectives, operational objectives, compliance objectives and financial reporting objectives.

In order to achieve these objectives and therefore fulfil its mission, things must go as devised and planned. Nonetheless, the internal characteristics of the organisation, that is, its people, processes and systems, together with the nature outside the business presented by its environment (market, standards, regulations, environment, etc.) do not provide absolute assurance about whether Ence will achieve its objectives and, if it can achieve these, about how it will be capable of doing so.

This uncertainty manifests itself in specific situations that threaten the Ence objectives (at all levels), and a risk management process is therefore created within the organisation in order to identify, assess, prioritize and respond to this uncertainty. This is done by bringing together methodologies, providing information channels and flows and reporting and assigning specific roles and responsibilities to the people involved in this process, in order to try to offer a reasonable level of assurance as regards the organisation achieving its goals.

The risk management framework provides an infrastructure of a systematic and common nature to establish, maintain and improve the main standards and guidelines that make up the process in order to address risks throughout the Group. This is implemented by means of a process aimed at continuous improvement, in which the participants and main responsibilities associated with the aforementioned are identified.

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The Internal Audit Department, in accordance with the framework of responsibilities and functions recommended by the Institute of Internal Auditors and with the Internal Audit Charter approved by the Board of Directors, carries out the risk management function throughout the Ence Group.

The parts that make up the risk management Framework are incorporated into the whole organisation, as they are based on a strategic approach in which all areas, departments and functions are aligned:

- 1) The **Governance** of the organisation establishes the responsibilities and the control environment for risk management. The **Culture** of the organisation defines the desired behaviour and risk understanding.
- 2) **Development of the strategy and objective-setting:** risk management is connected to establishing the strategy and setting objectives. A risk appetite is established and aligned with the strategy.
- 3) **Performance:** Any risks that may affect the achievement of strategic objectives are identified and assessed. Mitigating actions are prioritized and established.
- 4) **Review and monitoring:** upon examining the performance of the organisation, it may be determined how the components of enterprise risk management work in a dynamic way and if there are any aspects likely to be changed.
- 5) **Information, Communication and Reporting:** in order to be effective, enterprise risk management requires a continuous process to obtain and exchange necessary information from both internal and external sources, with fluency in all departments and throughout the organisation.

This framework is in line with the best practices in Internal Control and Enterprise Risk Management (COSO ERM<sup>1</sup> and ISO 31000 standards relating to Risk Management<sup>2</sup>) and is shown in the outline below, although it is explained in detail in the risk management Procedure of Ence.

## 9.2 Risk management process.

The risk management process is based on the risk management Framework defined in the point above backed by the COSO-ERM model for enterprise risk management, and consists of the following elements:

### a) Governance and Culture.

The organisation establishes the responsibilities and the control environment for risk management. The culture of the organisation defines the desired behaviour and risk understanding.

### b) Strategy and objective-setting.

Ence defines its objectives and the environment in which it operates from an inside and outside perspective, taking into account the interests of its stakeholders, which affects the way in which it manages risks, allowing

<sup>1</sup> COSO: *Committee of Sponsoring Organizations of the Treadway Commission*, voluntary private-sector organisation dedicated to improving the quality of financial reporting through business ethics, effective internal controls and corporate governance. The COSO I Report, which establishes the 5 basic components of the Internal Control Framework. was published in 1992. In 2004, COSO published “*ERM- Integrated Framework*” (COSO II), expanding the initial Internal Control Framework. In 2017 it published “*ERM-Integrating with Strategy and Performance*”, updating the Internal Control Framework to the current business environment.

<sup>2</sup> *ISO 31000:2009 – Risk Management – Principles and guidelines on implementation, ISO 31010:2009 – Risk Management – Risk Assessment Techniques and ISO Guide 73:2009 – Risk Management – Vocabulary.*

**c) Performance:****1) Risk evaluation.**

- Detection of risks: identify potential events that may threaten the objectives.
- Risk analysis: determine their causes, areas of impact and possible consequences.
- Risk assessment: consider the consequences and likelihood of occurrence in order to prioritize the most concerning situations, in accordance with **the** risk classification scale.

**2) Addressing and responding to risks.**

This involves selecting and applying the best risk response, in accordance with the situation concerned. Once implemented, a new control is provided or an existing control is modified. The risk response may be to assume, transfer, mitigate or eliminate.

Risk Managers select and implement the control measures for each one of the risks identified in their area, and the aforementioned are responsible for ensuring that these are correctly applied as risk mitigating factors. As owners of the Ence processes, their activities create or manage risks that may contribute to or prevent objectives set by the Organisation from being achieved.

On a regular basis, in accordance with the methodology defined in the “*Risk Management and Control Procedure*”, the effectiveness of the control measures defined as mitigating factors for critical and significant risks are reviewed.

**d) Process control and review.**

The risk management process is monitored and continuously reviewed in order to identify, propose and make any improvements that are necessary.

**e) Information, Communication and Reporting.**

We must provide relevant **information** on risks from and to all levels involved in Ence risk management, by means of tools such as **risk registers** and **risk maps**.

For **communication**, we have a suitable environment and a risk management philosophy by means of specific communications of the Audit Committee which are aimed at expectations of behaviour and responsibilities of the staff.

Furthermore, Ence adopts an internal communication programme designed to support the integration of its risk management philosophy based on the following points, inter alia:

- The Department discusses the risks and associated risk responses in regular informative sessions with its employees at all levels.
- Employees are provided with the risk management policies, standards and procedures, together with clear statements regarding compliance with the aforementioned.
- New employee orientation sessions include information and documentation about the methodology of the risk management and control Policy.

- The risk management methodology is reinforced by means of continuous internal and external communication programmes in order to consolidate the culture principles of the organisation.

## 10.- Internal reporting and control systems

Every year, Ence identifies and assesses new risks, monitors the development of risks that have been identified in previous years and determines whether any risks have ceased to exist during the period. It also updates the information relating to the controls and action plans associated with identified risks.

In order to do so, Ence uses the following management tools:

### a) Risk Register.

The Risk Register is the format used for the regular report of the main risks identified and assessed in the various business units.

The Risk Register is a tool that provides business units involved in the risk management process with strategic and operational information.

### b) Risk Map.

The Risk Map is the format used to graphically represent the likelihood and the impact associated with each risk, and to be able to immediately identify whether this must be addressed with the appropriate priority level.

In this regard, the risk Managers may focus on their risk management actions with more urgency and, at the same time, monitor the changes in situation registered in the other risks.

## 11.- Roles and responsibilities

The roles and responsibilities of each one of the members of the organisation involved in the process have been defined, taking into account the COSO-ERM methodology and the three lines model of the Institute of Internal Auditors (All), with these being assigned as follows:

### a) Board of Directors.

It takes on the roles attributed in the Rules, in particular:

- ✓ Establish the risk management and control Policy, including fiscal risks, and the supervision of internal reporting and control systems.
- ✓ Approve the corporate policies, and extension of the risk management and control Policy.

### b) Audit Committee.

This is the supervisory body for Risk Management. Its main functions are, inter alia:

- ✓ Supervise the Internal Audit services.
- ✓ Supervise and assess the adaptation, integrity and effectiveness of the internal control and financial and non-financial risk management systems relating to the Company, and where appropriate, the group,

including operational, technological, legal, social, environmental, climate, political, reputational, and corruption risks and discuss with the auditors or audit firms any significant weaknesses in the internal control system detected in the course of the audit.

- ✓ Supervise the correct management of the environmental aspects and occupational risk prevention audits.
- ✓ Supervise the risk map before it is approved by the Board of Directors.

**c) Internal Audit Department:**

This is responsible for:

- ✓ Developing the Group's risk management procedures and criteria and presenting them, via the Audit Committee, to the Board of Directors for their approval.
- ✓ Advising the Audit Committee of any identified risks to be approved by the aforementioned, as well as the plans and actions proposed by the risk manager.
- ✓ Developing and periodically updating the Ence risk map based on those previously approved.
- ✓ Informing the Board of Directors, via the Audit Committee, about risks that have emerged, underlining the circumstances that caused them and if the established control systems have worked.
- ✓ Ensuring that risk management systems are working correctly and, specifically, that any major risks to which Ence is exposed are correctly identified, managed and quantified.
- ✓ Ensuring that the risk management systems suitably mitigate risks in the framework of the risk management and control Policy, conducting a review on the effectiveness of the mitigating measures defined by the risk managers.
- ✓ Providing support and guidance for risk managers in all areas related to risk management.
- ✓ Developing and implementing the risk management and control processes of the organisation.
- ✓ Periodically monitoring the extent to which approved action plans are implemented.

**d) Risk managers.**

The directors and managers of the various Ence departments are the risk managers within their areas and perform, inter alia, the following functions:

- ✓ Use the risk management procedures and criteria approved by Ence. Specifically:
  - Identify situations of risk that effect the achievement of Ence objectives within their area of responsibility.
  - Assess identified risks according to the methodology available.
  - Inform of these risks by taking part in the established risk reporting process for this purpose and by using the tools made available for them.
- ✓ Follow the guidelines regularly outlined regarding risk management
- ✓ Inform the Internal Audit Department of the risks identified, the proposed plans and actions to mitigate these risks, as well as the level of progress or implementation of the aforementioned.
- ✓ Make decisions on risk responses and ensure implementation of the control measures.