RISK MANAGEMENT POLICY & FRAMEWORK

PURPOSE

STV is committed to maintaining a systematic strategy, framework and processes for the management of risk. The ability to identify, assess, monitor and manage each type of risk to which STV is exposed is an important factor in its financial soundness, performance, reputation and future success.

This document forms part of STV's internal control and governance arrangements and sets out the processes and activities employed in the management of risk.

The elements of the framework are:-

- an effective control environment;
- allocation of day to day responsibility for risk management;
- a risk assessment process;
- robust internal control procedures;
- performance monitoring and risk management activity;

The framework is designed to allow STV to manage its risk in accordance with its stated risk appetite.

RESPONSIBILITY FOR RISK

While the ultimate responsibility for risk management rests with the Board of Directors, it delegates the more detailed oversight of risk management and internal control principally to the Audit Committee which reports its findings to the Board.

RISK APPETITE

In pursuing its objectives, STV will generally accept a level of risk proportionate to the expected benefits to be gained and the scale or likelihood of loss.

STV has a very low appetite for risk where there is a likelihood of:-

- breach of any of its compliance obligations as regards its broadcasting licences;
- significant and lasting reputational damage;
- significant financial loss or significant negative variations to financial plans;
- loss of life or harm to its staff or visitors;
- illegal or unethical activity.

STV's risk appetite is set out in more detail in the attached spreadsheet.

RISK IDENTIFICATION

There are three categories of risk to STV:-

- Preventable risks
  These are internal risks which are controllable and ought to be eliminated or avoided. Eg risks from employees' unauthorised, illegal, unethical, incorrect or inappropriate actions and the risks from breakdowns in routine operational processes.

- Strategy risks
  These risks are not inherently undesirable and managing them is a key driver in capturing the potential gain. Eg a business strategy with high expected returns

generally requires significant risks to be taken on.

- External risks
  These risks arise from events outside STV and are beyond its influence or control. As they cannot be prevented, the focus is on their identification and the mitigation of their impact. Eg natural and political disasters and major macroeconomic shifts.

STV's approach to risk combines a top-down strategic view with a complementary bottom-up operational process. The strategic view involves an assessment of the external environment in which STV operates to evaluate the risks which it is comfortable being exposed to in pursuit of its performance objectives – its risk appetite. The bottom-up approach involves the identification, management and monitoring of risks in each area of the business thus ensuring that risk management is embedded in STV's everyday operations. Control of this process is provided through the risk register and operational risks are fully considered in determining the risk appetite and the corresponding strategy of the business.

STV's risk register has been developed in a way which allows the key risks facing STV to be summarised and actions taken to improve control to be tracked and monitored. The risk register was established through an in depth process, facilitated by the internal auditor, involving all areas of the business in order to ensure consensus on the key risks and the likelihood of their occurrence.

The risk register is helpful in identifying the actions required going forward to:

- ensure greater consistency of controls across the business;
- consider the need for additional controls or a change to the current process;
- protect the business from unexpected events; and
- improve the efficiency and effectiveness of financial and operational processes.

RISK MEASUREMENT

The risk register sets out the key risks that have been identified, allocating an owner to each, together with the risk impact, likelihood and score both on a gross and, after the current mitigating controls have been taken into account, a net basis.

The risk impact is graded 1 – 5 as follows:-

1. "Insignificant" with a potential impact of <£100k on profit
2. "Minor" with a potential impact of £100k - <£500k on profit
3. "Moderate" with a potential impact of £500k - <£1.5m on profit
4. "Major" with a potential impact of £1.5m - £5m on profit
5. "Disastrous" with a potential impact of >£5m on profit

The risk likelihood is graded 1 – 5 as follows:-

1. "Rare" - very unlikely during the next 20 yrs with a probability of <2%
2. "Unlikely" - may occur in the next 10–20 yrs with a probability of 2% - <10%
3. "Possible" - may arise at least once in a 1-10 yr period with a probability of 10% - <50%
4. "Likely" - highly likely it will occur once per yr with a probability of 50% -<80%

5. “Almost Certain” - likely it will occur more than once per yr with a probability of 80% or more.

MANAGING AND MONITORING RISK

Performance monitoring of risk management activity must ensure that the treatment of risks remains effective and that the benefits of implementing risk control measures outweigh the costs of doing so. Performance monitoring is a continual review not only of the whole process, but also of individual risks or projects and of the benefits gained from implementing risk control measures.

STV’s process for managing risks is:

(i) Identify all realistic risks
This involves looking at financial and business operations to establish what could cause an impact then at how serious it could be.

(ii) Analyse their probability and potential impact
The risks that have a greater consequence or impact upon business performance are determined together with what the likelihood of their occurrence is.

(iii) Evaluate risks to prioritise their management
The likelihood and impact of each risk on business performance is calculated in order to evaluate and prioritise the resources that would be required to treat these risks. The outcome of this step is a prioritised list of risks that require further action.

(iv) Treat risks to minimise their impact
The risks that are considered acceptable and those that need to be addressed are established. For unacceptable risks, strategies are developed for improving business performance and plans made so that the business is prepared to deal with these risks should they occur.

(v) Continually monitor the situation
The position is thereafter constantly checked for risks occurring, new risks emerging and changes in the assessment of existing risks in order that these can be reviewed and dealt with competently.

EMBEDDING RISK MANAGEMENT

Risk is an intrinsic part of the day to day activities of STV so risk management is integrated within the key business planning and decision making processes. STV’s system of internal control incorporates risk management and encompasses a number of elements that together facilitate an effective and efficient operation, enabling STV to respond to a variety of risks. These elements include:-

- Policies and Procedures
  Fundamental risks have a series of policies which underpin the internal control process.

- Business Planning and Budgeting
  The business planning and budgeting process is used to set objectives, agree action plans and allocate resources. Progress towards meeting business plan objectives is monitored regularly and risk management is built into this process.

- Risk Register
  The register is reviewed and updated on an ongoing basis both at an operational level and on a biannual basis by the Board, with the Audit Committee conducting an in-depth annual review.

- Audit Committee
  The Audit Committee oversees both internal and external audit and reports fully to the Board on a regular basis.

- Internal Audit
  The internal auditor attends all Audit Committee meetings to report on how well risks are being managed and how the business is being governed. It reviews the effectiveness of the internal control system including the risk management process and provides advice on how improvements can be made

- External Audit
  The external auditor attends all Audit Committee meetings to ensure the information contained within the financial statements is "true and fair" and to advise on the operation of the internal financial controls reviewed as part of the audit process.

RISK REPORTING

STV focuses on providing the following information when making its risk disclosures:

- Sufficient detail to enable shareholders to understand why these risks are important to STV
- Details of any significant changes to principal risks
- A description of the likelihood of the risk
- A high level explanation of how the principal risks and uncertainties are being managed
- An indication of the circumstances under which the risk might be most relevant to STV and its possible impact
- For a more generic risk or uncertainty, a description of how that risk or uncertainty might affect STV specifically.

RISK TESTING

Testing is used to evaluate the potential impact on the business of unlikely but plausible events in order to observe the results and measure the impact upon revenue, value, liquidity etc. It is an effective risk management tool as it explicitly links potential impacts to specific events. When testing, either a single or a combination of operational risk parameters can be changed in order to provide valuable data to senior management allowing further and better understanding of STV's operational risk profile.

By gaining a better understanding of STV's risks, controls, indicators and potential losses, effective testing of risks can clarify for management the interactions and causal relationships between them. It can also help evaluate the effectiveness of various mitigating options available to management and stimulate them to be prepared in case a disruptive event occurs.

Testing encourages managers to think differently, challenge their models, be better risk managers and ultimately be more accountable to stakeholders. While there is no certainty in risk, testing helps management address key issues, such as:-

- What is the P&L impact?
- What is the worst-case scenario and the associated loss?
- What level of loss is STV willing to take under specific scenarios?
- What action can management take to bring the exposure within an acceptable level?