GREATER COMPETITIVENESS THROUGH A RESPONSIBLE VALUE CHAIN

Context

This Report discloses SK Telecom's supply chain sustainability management policies and processes, and its purpose is to inform stakeholders about responsibility and assurance for the products and services value chain. In the process of its business operation, SK Telecom depends upon a variety of suppliers for the development and spread of network devices, building and operating the network infrastructure as well as providing and developing platform content. This Report contains information regarding SK Telecom's efforts to review and resolve significant risk factors involving suppliers in the supply chain as well as support the ability to discover possible opportunities.

Supplier ESG Code of Conduct

SK Telecom defines its social responsibility compliance requirements for suppliers through the Supplier ESG Code of Conduct. The Supplier Code of Conduct covers 1) anti-corruption, 2) fair trade compliance, 3) data privacy and protection, 4) financial transparency, 5) appropriate participation in public policies, 6) respect for customer value, 7) environmental protection, 8) employees' welfare and safety, 9) community involvement, and 10) human rights. For more details about SK Telecom's supply chain policy, please refer to its homepage (http://www.sktelecom.com/supplychain.)

Through the 'Supplier ESG Code of Conduct' and 'Fair Trade/Transparent Transactions & CSR Practice Agreement,' which are based upon the company's supply chain policy, SK Telecom is improving the specificity of suppliers' social responsibility requirements as well as their ability to put them into practice. As a representative company of UNGC LEAD, SK Telecom reflects the UNGC principles in its supply chain guidelines, on the foundation of its UNGC LEAD activities. SK Telecom's supply chain guidelines refer to the global e-sustainability initiative e-Gesi's JAC (Joint Audit Cooperation) Guidelines. During the contract process, SK Telecom requires its suppliers to comply with these principles and through a monitoring process, the company makes use of a number of measures such as requesting corrective measures and terminating transactions.

SK Telecom's Supply Chain Status

SK Telecom has designated a 'critical supplier' group after having comprehensively considered the degree of the company's reliance upon the transactions as well as the impact on the company's continued operations. SK Telecom's critical suppliers are comprehensively considered, categorized and managed according to their 1) relevance to the company's core businesses and reliability, 2) high level of transaction amounts, 3) possession of proprietary technology for which substitution is not possible. Accordingly, as of 2016, 318 companies are categorized into the Tier 1 critical supplier group out of a total 1,881 registered partners.

Advance Screening of Supply Chain Sustainability

In 2016, 100% of newly registered partner companies were screened according to the Fair Trade/Transparent Transactions & CSR Practice Agreement and were requested to comply with the supply chain policy through Open2U, SK Telecom's electronic contract system. The Fair Trade/Transparent Transactions & CSR Practice Agreement is an official document that requests compliance and agreement with the Supply Chain ESG Policy. According to the screening results of the newly registered partner companies, those that do not satisfy the set standards (credit rating of B- or higher, a score of 70 points or higher on the contract execution ability evaluation) cannot, by regulation, become a supplier for SK Telecom. In addition, newly registered partner companies are evaluated for having cash payment and support programs for sub-suppliers, environmental policies and human rights/labor policies, etc. and those that do can receive up to 10 extra points.

Identification and Analysis of Key Supply Chain Risks

SK Telecom comprehensively reflects the risk factors discovered through internal risk processes including business partner surveys such as the biannual Win-Win Growth Satisfaction Survey, partner company meetings, listening to the voice of partners and risk management working groups, and reviews the results of the risk gap analysis of each supplier group and risk mapping by supplier at the monthly 'procurement performance analysis and improvement meeting.' SK Telecom defines the main risks that may occur in the supply chain as follows, and reflects these in the supply chain sustainability process.
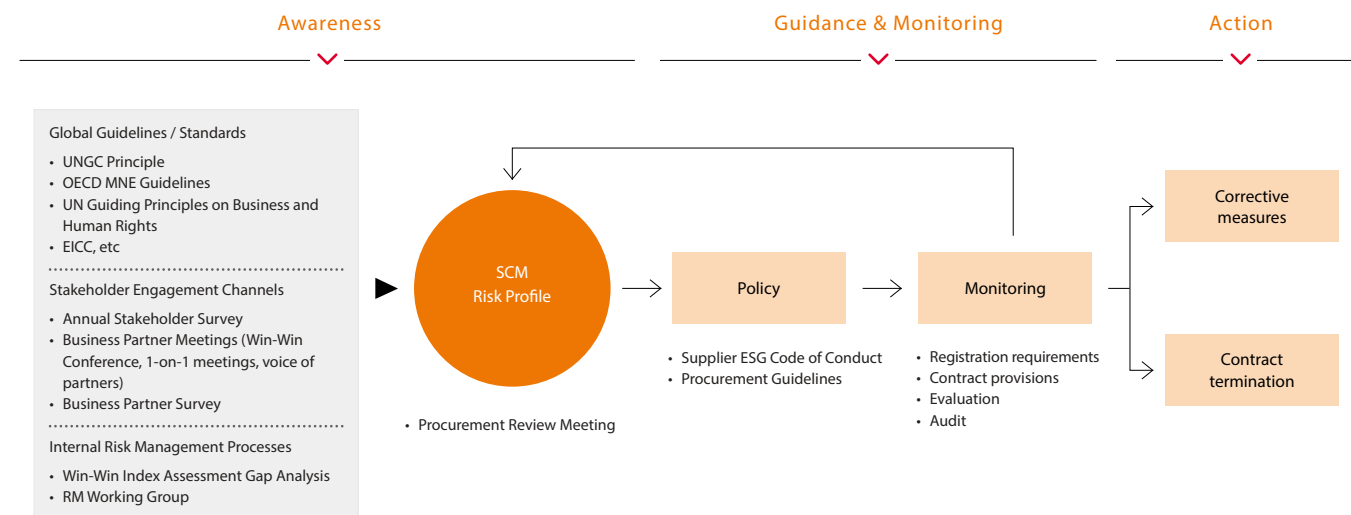
SUPPLY CHAIN SPEND ANALYSIS

Partner Category		Number of Partners	Proportion of Procurement
Tier 1	Total Number of Registered Suppliers	1,881	100%
	Equipment (Network and Infrastructure)	275	26.2%
	Services (Software and Solution Development)	1,123	50.3%
	Goods	249	3.5%
	Construction	234	20%
	Critical Suppliers	318	87%
Non-Tier 1	Critical Suppliers	35	-

SUPPLY CHAIN ESG ASSESSMENT (ADVANCE SCREENING)

	2014	2015	2016	2020 Target	Notes
Total Number of Newly Registered Suppliers	712	706	725	750	
Human Rights - Environment - Ethics - Social Screening	712	706	725	750	Service/Construction/Equipment/Goods Suppliers
Rate of Advance Assessments	100	100	100	100	

SK TELECOM'S PROCESS FOR A RESPONSIBLE SUPPLY CHAIN

Awareness → **Guidance & Monitoring** → **Action**

Global Guidelines / Standards
- UNGC Principle
- OECD MNE Guidelines
- UN Guiding Principles on Business and Human Rights
- EICC, etc

Stakeholder Engagement Channels
- Annual Stakeholder Survey
- Business Partner Meetings (Win-Win Conference, 1-on-1 meetings, voice of partners)
- Business Partner Survey

Internal Risk Management Processes
- Win-Win Index Assessment Gap Analysis
- RM Working Group

SCM Risk Profile → Policy → Monitoring

- Procurement Review Meeting

Policy
- Supplier ESG Code of Conduct
- Procurement Guidelines

Monitoring
- Registration requirements
- Contract provisions
- Evaluation
- Audit

Corrective measures

Contract termination

SUPPLY CHAIN RISK IDENTIFICATION & ANALYSIS RESULTS

				Assessed Sourcing Group		Rate at High Risk (*)
Main Risk Factors			Risk Level	Assessed Group	Rate (No. of companies)	Rate (No. of companies)
Tier 1	Overall	Overall Risks	-	-	100% (1,881)	2.7% (52)
	Economic Risks	Ethical and Anti-Corruption Principle Violations in the Contract Process	High	All Suppliers	100% (1,881)	0.2% (3)
			High	All Suppliers	100% (1,881)	0% (0)
		Collusion and Other Unfair Trade Practices	High	All Suppliers	100% (1,881)	0% (0)
		Delayed Payment to Subcontractors	High	All Suppliers	100% (1,881)	0.9% (17)
	Social Risks	Unsound Financial Structure (low credit rating)	Moderate	Service Suppliers / Construction Suppliers	72.1% (1,357)	0.9% (12)
		Violation of ILO Labor Regulations and Reasonable Labor Practices (compliance with work hours, wage payment, and other labor rights)	Low	Equipment Suppliers	14.6% (275)	0.4% (1)
	Environmental Risks	Conflict Minerals	Moderate	Equipment Suppliers	14.6% (275)	0.7% (2)
		Violations of Environmental Regulations	Moderate	Equipment Suppliers	14.6% (275)	0.7% (2)
		High GHG Emissions	Low	Construction Suppliers/ Equipment Suppliers	27.1% (509)	2.9% (15)
		Failure to Adopt an Environmental Management System				
Non-Tier 1	Overall	Interim Contract Suppliers	-		100% (35)	2.9% (1)
		Overall Risks		(**)		

(*)The rate of suppliers determined to have a high risk level according to the risk analysis results.

(**)Calculation limited to cases when an interim contract instead of a direct contract is made with the small and medium sized suppliers for N/W facilities construction or the supply of general goods (SK E&C, Happynarae)

Supply Chain ESG Assessments

SK Telecom is confirming the proportion of registered partners that have undergone written surveys and on-site surveys as the key indicator of supply chain ESG risk assessment activities. In 2016, among the 1,881 tier 1 suppliers, 1,351 have done written surveys, 225 have undergone on-site surveys (includes separate visits and meetings with partners and 1-on-1 meetings), which covers 91% of all registered partners. With regard to the third-party external review and diagnostic assessment for partners, the 376 partners that were candidates for mutual growth cooperation participated in a third-party external review conducted by the Korean Commission on Cooperative Partnership. SK Telecom is applying such policies and performance indicators to all domestic and international suppliers. In 2016, 100% of newly registered partner companies were screened according to the Fair Trade/Transparent Transactions & CSR Practice Agreement through Open2U, SK Telecom's electronic contract system. Due to the majority of SK Telecom's total procurement amount (KRW 3.6957 trillion) being made up of domestic suppliers, with international procurement making up about KRW 20.9 billion (0.56%), performance indicators are also managed with a focus on Korea.

During 2016, SK Telecom conducted written surveys of 1,351 suppliers among all tier 1 suppliers (1,881 companies) and on-site surveys of 225 companies (includes separate visits and meetings with partners and 1-on-1 meetings). Regarding the partners that were judged to be exposed to 'high risk' in the risk identification process, 100% of them received on-site surveys or supply chain audits through third-party surveys to prevent risks in advance.

SK Telecom offers programs for capability improvement and incentive programs for exemplary partners on an annual basis based on diagnostic and assessment results. Programs to improve capabilities include technological support such as technology transfer and Open Collaboration as well as security activities, and also include the SK Win-Win Academy, where partners can engage in CEO seminars, MBA courses and training support for reducing risk. Risk reduction training includes topics such as mutual growth partnerships and includes training regarding procurement policies and policy compliance. For outstanding partners, the incentive and support programs include unit price adjustment, funding (financial) assistance, technology and training support, and welfare.

SUPPLY CHAIN ESG ASSESSMENT (BY TYPE)

		2014	2015	2016	2020 Target	Notes
Tier 1	Total Number of Registered Suppliers (*)	1,510	2,346	1,881	2,100	
	Number of Suppliers Assessed	1,020	1,582	1,726	2,000	
	Number of Suppliers Surveyed in Writing (Audit)	815	1,270	1,351	1,400	
	Number of Suppliers Surveyed On-Site (Audit)	205	212	225	242	Includes separate discussions with Construction/Equipment Suppliers and 1-on-1 meetings
	Number of Suppliers Surveyed by 3rd Parties	-	100	150	150	Partner experience survey conducted by the Korean Commission for Corporate Partnership
	Assessment Rate of Suppliers	67	67	91	95	
Non-Tier 1	Total Number of Critical Suppliers (**)	-	20	35	40	
	Number of Critical Suppliers Assessed (***)	-	10	21	24	
	Rate of Critical Suppliers Assessed (%)	-	50	60	60	

(*) This number includes all suppliers including those with which SK Telecom did not have transactions in the past 3 years

(**) Calculation limited to cases when an interim contract instead of a direct contract is made with the small and medium sized suppliers for N/W facilities construction or the supply of general goods (SK E&C, Happynarae)

(***) SK Telecom's N/W facilities construction began in 2015 and an interim contract with Happynarae was implemented starting in 2016

RISK MONITORING AND ASSESSMENT (2016, BY TIER)

Category	No. of Companies	No. of Companies Assessed	Rate (%)	Notes
Critical Suppliers	353	321	91	Tier 1 & Critical Non-Tier 1 Suppliers
Suppliers at a High Risk Level	52	52	100	Tier 1 Suppliers

* SK Telecom conducts its supply chain ESG assessment on an annual basis and the above assessment rate has been calculated according to the suppliers that were assessed annually.

Corrective Measures

For partners whose diagnostic and assessment results demonstrate a need for improvement, SK Telecom creates a plan for corrective measures and requests that partner companies make efforts to improve their ESG performance. Despite these efforts, in 2016, a total of 3 companies received corrective measures according to the diagnosis and assessment results, and due to the seriousness of their policy violations including fair trade violations, and occurrence of unethical issues, a permanent suspension of transactions was implemented against two of the companies.

RISK-RELATED CORRECTIVE MEASURES FOR PARTNERS

	2014	2015	2016	2020 Target	Notes
Rate of High Risk Level Suppliers with Established Plans for Improvement (%)	-	100	100	100	
Rate of Suppliers with Improved ESG Performance within 12 months of Establishing Plans for Improvement (%)	-	83	90	100	
Number of Suppliers that Received Corrective Measures	2	2	3	-	Reviewed by the Procurement Review Committee
Banned Temporarily	1	0	1	-	1 year suspension
Banned Permanently	1	2	2	-	Permanent suspension

Procurement Strategy and Supply Chain Sustainability

SK Telecom's procurement strategy prioritizes 1) gaining competitiveness by improving the procurement structure through TCO (Total Cost Ownership), 2) revitalizing strategic integrated procurement through a 'procurement synergy consultative group' with SK subsidiaries and invested companies, 3) improving cost efficiency by checking the production cost structure from the zero-base perspective, 4) optimizing and improving business-friendly procurement processes, and 5) creating an environment for advance procurement risk management and fair trade compliance. Furthermore, SK Telecom continues to cooperatively develop sustainability management goals and expand support for overseas export while creating an environment conducive to fair trade.

By executing this procurement strategy and sustainability management goals in a connected manner across the company, SK Telecom helps its partners and the company to not only maximize resource-creation, but also removes inefficient practices, formalities and procedures from the procurement process so that it can be optimized through efficiency. The following business case will explain how SK Telecom achieves its procurement strategy by practicing responsible supply chain risk management.

CASE

BUSINESS CASE 1.

ENERGY EFFICIENCY JOINT VENTURE

SK Telecom's energy efficiency joint venture supports a business partner's optimized energy reduction solution that combines an energy platform (BEMS/FEMS) and lighting control technology. The Energy Management System (EMS) is a package comprised of a cloud server-based management platform and facilities to help manage energy use, and it is a solution that allows users to continuously reduce their energy use expenses through this business partner's optimized energy consulting. This solution helps businesses with high levels of energy consumption to respond to energy policies such as the Greenhouse Gas Target Management System and a yearly energy reduction of 5% is possible. Furthermore, through the natural air conditioning system and reduced vehicular fuel use by using the T map service, the business partner achieved KRW 82,759 million (314 cases) in energy expense savings.

Energy Savings Achieved by Business Partner

KRW 82,759 million

BUSINESS CASE 2.

JOINT DEVELOPMENT AND PREFERENTIAL PURCHASING OF NETWORK EQUIPMENT

SK Telecom has jointly developed and commercialized an optical repeater for mobile communications such as LTE with a partner company and made an import substitution for the foreign-made base station equipment that it normally purchased. SK Telecom has pursued joint development including patent grants for a savings-type optical repeater and relay base telecommunication cabinet and carried out import substitution. The company has also supported partnerships for productivity innovation as well as exports such as overseas sales of ICT solutions. Furthermore, SK Telecom has successfully exported cloud transmission equipment to the U.S. through patent grants and joint developments.

Joint development of N/W equipment

316 cases