

# CORPORATE GOVERNANCE REPORT

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## Letter from the Chairman of the Board of Directors and the Company Secretary

Dear Shareholder

On behalf of the Board, we are pleased to present the corporate governance report for the year ended 30 June 2015.

The purpose of this report is to explain how Diageo is directed and controlled by your Board and to summarise the corporate governance activity that has taken place during the year.

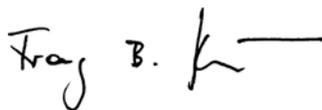
In addition to its overall responsibility for corporate governance, the Board's duties include setting the company's strategy and values and overseeing and supporting management in their day to day running of the business. We continue to believe that your Board demonstrates the appropriate behaviours and has the diversity, skills, independence and knowledge of the business to enable it to successfully discharge its duties.

The principal corporate governance rules applying to Diageo (as a UK company listed on the London Stock Exchange (LSE)) for the year ended 30 June 2015 are contained in The UK Corporate Governance Code as updated and published by the Financial Reporting Council (FRC) in September 2012 (the Code) and the UK Financial Conduct Authority (FCA) Listing Rules, which require us to describe, in our Annual Report, our corporate governance from two points of view: the first dealing generally with our application of the Code's main principles and the second dealing specifically with non-compliance with any of the Code's provisions. The two descriptions together are designed to give shareholders a picture of governance arrangements in relation to the Code as a criterion of good practice.

Throughout the year, Diageo has complied with all relevant provisions set out in the Code, which is publicly available under the heading 'Corporate Governance' at the website of the FRC, [www.frc.org.uk](http://www.frc.org.uk).

Diageo must also comply with corporate governance rules contained in the FCA Disclosure and Transparency Rules as well as certain related provisions in the Companies Act 2006 (the Act).

As well as being subject to UK legislation and practice, as a company listed on the New York Stock Exchange (NYSE), Diageo is subject to the listing requirements of the NYSE and the rules of the Securities and Exchange Commission (SEC). Compliance with the provisions of the US Sarbanes-Oxley Act of 2002 (SOX), as it applies to foreign private issuers, is continually monitored. As Diageo follows UK corporate governance practice, differences from the NYSE corporate governance standards are summarised in Diageo's 20-F filing and on our website at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).



Dr Franz B Humer  
Chairman



Paul D Tunnacliffe  
Company Secretary

# BOARD OF DIRECTORS

## Membership of the Board and Board Committees

The Chairman, Senior Non-Executive Director and other members of the Board, Audit Committee, Nomination Committee and Remuneration Committee are as set out in this Annual Report in the biographies of Directors and members of the Executive Committee.

There is a clear separation of the roles of the Chairman and the Chief Executive. The Chairman, Dr Franz B Humer, is responsible for the running of the Board and for ensuring all Directors are fully informed of matters, sufficient to make informed judgements. As Chief Executive, Ivan Menezes has responsibility for implementing the strategy agreed by the Board and for managing the company and the group. He is supported in this role by the Executive Committee.

The Non-Executive Directors, all of whom the Board has determined are independent, are experienced and influential individuals from a range of industries, backgrounds and countries. No individual or group dominates the Board's decision-making processes.

 A summary of the terms and conditions of appointment of the Non-Executive Directors is available at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

## Activities and duties of the Board

The Board manages overall control of the company's affairs with reference to the formal schedule of matters reserved for the Board for decision. The schedule was last reviewed in July 2015 and is available at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

The Board has agreed an approach and adopted guidelines for dealing with conflicts of interest and responsibility for authorising conflicts of interest is included in the schedule of matters reserved for the Board. The Board confirmed that it was aware of no situations that may or did give rise to conflicts with the interests of the company other than those that may arise from Directors' other appointments as disclosed in their biographies.

In order to fulfil their duties, procedures are in place for Directors to seek both independent advice and the advice and services of the Company Secretary who is responsible for advising the Board, through the Chairman, on all governance matters. The Non-Executive Directors meet without the Chairman present, and also meet with the Chairman without management present, on a regular basis.

 The terms of reference of Board Committees are available at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

## Induction, training and business engagement

There is a formal induction programme for new Directors, which was followed during the year for Nicola Mendelsohn and Alan Stewart. This included meeting with Executive Committee members and other senior executives individually and visiting the Supply operations in Scotland and the customer collaboration centre in the UK.

Following the initial induction for Non-Executive Directors, a continuing understanding of the business is developed through appropriate business engagements. Visits to customers, engagements with employees, and brand events were arranged during the year.

In addition, Executive Committee members and other senior executives are invited, as appropriate, to Board and strategy meetings to make presentations on their areas of responsibility.

All Directors are also provided with the opportunity, and encouraged, to attend regular training to ensure they are kept up to date on relevant legal developments or changes and best practice and changing commercial and other risks.

## Performance evaluation

As reported last year, an externally facilitated evaluation of the Board's effectiveness, including the effectiveness of the Audit, the Remuneration and the Nomination Committees, continued into the subsequent financial year. The external facilitator, Wickland Westcott, has no other connection with the company.

A report was prepared and presented, with the conclusion that the Board and its Committees continued to operate effectively, meeting the requirements and spirit of the Code. The climate within the Board, its capability and the diversity of Board members, were seen as significant factors which contributed to the Board's effectiveness during the year.

There were, nevertheless, areas identified as being of a particular focus: the relationship between the Board and the new executive team, with an aim for the Board to continue to support and mentor the team; ensuring sufficient time was allocated to undertake scenario planning, to generate insight and advantage; the understanding of and the deepening of the Board's relationships with the Company's shareholders; and on emerging market volatility, particularly the markets where there is the potential of significant external volatility or risks.

Without being complacent, the Board was considered to be in good shape to deal with these and support management in its aspirations to deliver the Performance Ambition.

A similar, internal, exercise building on this evaluation and covering the evaluation of the Board and its Committees started during the year and has continued into the subsequent financial year. A report will be prepared for the Board for consideration at its next meeting. The results of the evaluation will be reported in next year's report.

The Chairman has confirmed that the Non-Executive Directors standing for re-election at this year's AGM continue to perform effectively, both individually and collectively as a Board, and that each demonstrate commitment to their roles. The senior Non-Executive Director led a performance evaluation of the Chairman. Feedback was discussed in a meeting with the Executive and Non-Executive Directors and then privately with the Chairman.

It is the Board's intention to continue to review annually its performance and that of its committees and individual directors.

## Nomination Committee

### Role of the Nomination Committee

The Nomination Committee is responsible for keeping under review the composition of the Board and succession to it, and succession planning for senior leadership positions. It makes recommendations to the Board concerning appointments to the Board.

Any new Directors are appointed by the Board and, in accordance with the company's articles of association, they must be elected at the next AGM to continue in office. All existing Directors retire by rotation every year.

### Activities of the Nomination Committee

The principal activities of the Nomination Committee during the year were: the consideration of potential new Non-Executive Directors, in light of the review of the structure and composition of the Board; the review of individual Director performance; a review of the Executive Committee membership and succession planning for it and for senior leadership positions, in addition to a review of diversity within the group.

In respect of the appointment of Emma Walmsley the recruitment process included the development of a candidate profile and the engagement of a professional search agency (which has no other connection with the Company) specialising in the recruitment of high calibre Non-Executive Directors. Reports on potential appointees were provided to the committee, which, after careful consideration, made a recommendation to the Board.

## Diversity

Diageo supports diversity within its Board of Directors, including gender diversity. Further information is given in the section of this Annual Report on sustainability & responsibility, our people.

## Remuneration Committee

### Role of the Remuneration Committee

The role of the Remuneration Committee and details of how the company applies the principles of the Code in respect of Directors' remuneration are set out in the directors' remuneration report.

The Chairman and the Chief Executive may, by invitation, attend Remuneration Committee meetings, except when their own remuneration is discussed. No Director is involved in determining his or her own remuneration.

# EXECUTIVE DIRECTION AND CONTROL

## Executive Committee

The Executive Committee, appointed and chaired by the Chief Executive, supports him in discharging his responsibility for implementing the strategy agreed by the Board and for managing the company and the group.

It consists of the individuals responsible for the key components of the business: North America, Europe, Africa, Latin America and Caribbean, Asia Pacific, International Supply Centre and the global functions.

The Executive Committee focuses its time and agenda to align with the Performance Ambition and how to achieve the performance imperatives. Performance metrics have been developed to measure progress and a further designated focus is on the company's reputation. In support, monthly performance delivery calls, involving the senior leadership group, focus on progress against the six performance drivers.

To support the market visits made by the presidents in the ordinary course of their business, a small group led by the Chief Executive makes regular market visits focused on the execution of strategy and designed to assist in continuing the development of strategy and in the delivery of performance against the Performance Ambition.

Committees appointed by the Chief Executive and intended to have an ongoing remit, including the Audit & Risk Committee, Finance Committee and Filings Assurance Committee are shown (with their remits) at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

## Additional information

### Internal control and risk management

An ongoing process has been established for identifying, evaluating and managing risks faced by the group. This process, which complies with the requirements of the Code, has been in place for the full financial year and up to the date the financial statements were approved and accords with the guidance issued by the Financial Reporting Council in October 2005, 'Internal Control: Revised Guidance for Directors on the Combined Code', also known as the Turnbull guidance (as amended by the Flint review).

The Board acknowledges that it is responsible for the company's systems of internal control and risk management and for reviewing their effectiveness. The Board confirms that, through the activities of the Audit Committee described below, it has reviewed the effectiveness of the company's systems of internal control and risk management.

During the year, in line with the Code, the Board considered the nature and extent of the risks it was willing to take to achieve its strategic goals and reviewed the existing internal statement of risk appetite (which was considered and recommended to the Board by both the Audit & Risk Committee and the Audit Committee).

The company has in place internal control and risk management systems in relation to the company's financial reporting process and the group's process for preparation of consolidated accounts. Further, a review of the consolidated financial statements is completed by management to ensure that the financial position and results of the group are appropriately reflected therein.

## Compliance and ethics programme

Diageo is committed to conducting its business responsibly and in accordance with all laws and regulations to which its business activities are subject. We hold ourselves to the principles in our Code of Business Conduct, which is embedded through a comprehensive training and education programme for all employees.

Our Code of Business Conduct, which was reviewed and updated during the year in preparation for launch in the next financial year, and other Diageo global policies are available at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

In accordance with the requirements of SOX (and related SEC rules), Diageo has adopted a code of ethics covering its Chief Executive, Chief Financial Officer, presidents and other identifiable persons in the group, including those performing senior accounting and controller functions. No amendments to, or waivers in respect of, the code of ethics were made during the year.

The full text of the code of ethics is available at [www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance](http://www.diageo.com/en-row/ourbusiness/aboutus/corporategovernance).

Both the Audit & Risk Committee and the Audit Committee regularly review the strategy and operation of the compliance and ethics programme through the year.

Further information is given in the section of this Annual Report on sustainability & responsibility, governance & ethics.

## Relations with shareholders

The Board's primary contact with institutional shareholders is through the Chief Executive and Chief Financial Officer. The Chief Executive and Chief Financial Officer are supported by the investor relations department, who are in regular contact with institutional shareholders and sell-side analysts. A monthly investor relations report, including coverage of the company by sell-side analysts, is circulated to the Board.

The Board also ensures that all Directors develop an understanding of the views of major institutional shareholders through an independent survey of shareholder opinion. In addition, major shareholders are invited to raise any company matters of interest to them at meetings with the chairman and the chairman of the Remuneration Committee. Reports on any meetings are made to the Board.

Private shareholders are invited to write to the chairman or any other Director and express their views on any issues of concern at any time and the AGM provides an opportunity for private shareholders to put their questions in person.

## Political donations

The group has not given any money for political purposes in the United Kingdom and made no donations to EU political organisations and incurred no EU political expenditure during the year. The group made contributions to non-EU political parties totalling £0.5 million during the year (2014 – £0.4 million).

These contributions were made, almost exclusively, to federal and state candidates and committees in North America (consistent with applicable laws), where it is common practice to make political contributions. No particular political persuasion was supported and contributions were made with the aim of promoting a better understanding of the group and its views on commercial matters, as well as a generally improved business environment.

### Going concern

The Directors confirm that, after making appropriate enquiries, they have reasonable expectation that the group has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements. Further information on going concern is given in this Annual Report under note 1 Accounting information and policies – going concern.

### Management’s report on internal control over financial reporting

Management, under the supervision of the Chief Executive and Chief Financial Officer, is responsible for establishing and maintaining adequate control over the group’s financial reporting.

Management has assessed the effectiveness of Diageo’s internal control over financial reporting (as defined in Rules 13(a)-13(f) and 15(d)-15(f) under the US Securities Exchange Act of 1934) based on the framework in ‘Internal Control – Integrated Framework’, issued by the Committee of Sponsoring Organisations of the Treadway Commission (COSO) in 2013. Based on this assessment, management concluded that, as at 30 June 2015, internal control over financial reporting was effective.

During the period covered by this report, there were no changes in internal control over financial reporting that have materially affected or are reasonably likely to materially affect the effectiveness of internal control over financial reporting.

KPMG LLP, an independent registered public accounting firm, who also audit the group’s consolidated financial statements, has audited the effectiveness of the group’s internal control over financial reporting, and has issued an unqualified report thereon, which will be included in the company’s Form 20-F to be filed with the SEC.

### Directors’ responsibilities in respect of the Annual Report and financial statements

The Directors are responsible for preparing the Annual Report, the information filed with the SEC on Form 20-F and the group and parent company financial statements in accordance with applicable law and regulations.

### Responsibility statement

Each of the Directors, whose names are set out in the Board of Directors and Executive Committee section of this Annual Report, confirms that to the best of his or her knowledge:

- the Annual Report for the year ended 30 June 2015, taken as a whole, is fair, balanced and understandable, and provides the information necessary for shareholders to assess the group’s performance, business model and strategy;
- the consolidated financial statements contained in the Annual Report for the year ended 30 June 2015, which have been prepared in accordance with IFRS as issued by the IASB and as adopted for use in the EU, give a true and fair view of the assets, liabilities, financial position and profit of the group; and
- the management report represented by the Directors’ report contained in the Annual Report for the year ended 30 June 2015 includes a fair review of the development and performance of the business and the position of the group, together with a description of the principal risks and uncertainties that the group faces.

The responsibility statement was approved by the Board of Directors on 29 July 2015.

Directors’ attendance record at the AGM, scheduled Board meetings and Board committee meetings, for the year ended 30 June 2015 was as set out in the table below. For Board and Board committee meetings, attendance is expressed as the number of meetings attended out of the number that each Director was eligible to attend.

	Annual General Meeting 2014	Board (maximum 6) <sup>(ii)</sup>	Audit Committee (maximum 4)	Nomination Committee (maximum 3)	Remuneration Committee (maximum 6)
Dr Franz B Humer	✓	6/6	4/4 <sup>(i)</sup>	3/3	6/6 <sup>(i)</sup>
Ivan Menezes	✓	6/6	2/2 <sup>(ii)</sup>	3/3 <sup>(i)</sup>	6/6 <sup>(ii)</sup>
Deirdre Mahlan	✓	6/6	4/4 <sup>(i)</sup>	n/a	1/1 <sup>(ii)</sup>
Lord Davies	✓	6/6	4/4	3/3	6/6
Peggy Bruzelius	✓	5/6	3/4	3/3	5/6
Laurence Danon	✓	6/6	4/4	3/3	6/6
Betsy Holden	✓	6/6	4/4	3/3	6/6
Ho KwonPing	✓	6/6	4/4	3/3	5/6
Nicola Mendelsohn	✗	4/5	3/3	1/2	4/5
Philip Scott	✓	6/6	4/4	3/3	6/6
Alan Stewart	✓	4/5	2/3	2/2	4/5

(i) Attended by invitation.

(ii) Attended by invitation, for part only.

(iii) Two non-scheduled Board calls were held during the year, in relation to financial matters.

Where Non-Executive Directors were unable to attend a meeting they gave their views to the Chairman of the respective meetings ahead of the meetings being held. Nicola Mendelsohn was unable to attend the 2014 AGM as a result of another engagement which was arranged prior to her appointment.

Sub-Committee meetings of the Audit Committee were also held involving P G Scott, P B Bruzelius and A JH Stewart.