



### Dear Shareholder

On behalf of the Audit Committee, I am pleased to present its report for the year ended 30 June 2020.

The purpose of this report is to describe how the Committee has carried out its responsibilities during the year. In overview, the role of the Audit Committee is to monitor and review: the integrity of the company's financial statements and reporting; internal control and risk management; audit and risk programmes; business conduct and integrity; 'whistleblowing'; and the appointment of the external auditor.

During the year, the Committee gave attention to all elements of its remit with continued focus on particular topics within the company's risk management programme and emerging trends, including product quality risk management, cyber security and data access risks, internal and third-party data management and migration risks, pensions funding status and governance, and controls testing. During the year, the Committee also reviewed external analyses relating to the effectiveness of the company's internal audit and controls, compliance and ethics functions, as well as internal reports on the steps being taken to address internal audit findings, controls issues and investigations.

As part of the annual Board evaluation, all members of the Audit Committee completed an evaluation of the Committee. This concluded that members were very satisfied with the performance of the Committee. In order to ensure that adequate time is given to enable the Committee to continue to carry out its duties to a high standard, it was decided to increase the number of meetings which it ordinarily holds each year. Further details of the evaluation can be found on pages 78 and 79.

In discharging its duties, the Audit Committee seeks to balance independent oversight of the matters within its remit with providing support and guidance to management. I am confident that the Committee, supported by members of senior management and the external auditor, has carried out its duties in the year under review effectively and to a high standard.

**Alan Stewart**  
Chairman of the Audit Committee

### Role of the Audit Committee

The formal role of the Audit Committee is set out in its terms of reference, which are available at <https://www.diageo.com/en/our-business/corporate-governance>. Key elements of the role of the Committee and work carried out during the year are set out as follows.

### Composition of the Audit Committee

The members of the Audit Committee are independent non-executive directors and it comprises Alan Stewart (Committee Chairman), Melissa Bethell, Susan Kilsby, Ho KwonPing and Lady Mendelsohn. The Board has satisfied itself that the membership of the Audit Committee includes at least one Director with recent and relevant financial experience and has competence in accounting and/or auditing and in the sector which the company operates, and that all members are financially literate and have experience of corporate financial matters.

### Financial statements

During the year, the Audit Committee met five times (and a subcommittee met twice) and reviewed both the interim results announcement, which included the interim financial statements, and the annual reports and associated preliminary results announcement, focusing on key areas of judgement and complexity, critical accounting policies, provisioning and any changes required in these areas or policies.

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 the preparation of consolidated accounts. A review of the consolidated financial statements is completed by the Filings Assurance Committee (FAC) to ensure that the financial position and results of the group are appropriately reflected therein. In addition to reviewing draft financial statements for publication at the half and full year, the FAC is responsible for examining the company's financial information and processes, the effectiveness of internal controls relating to financial reporting and disclosures, legal and compliance issues and, determining whether the company's disclosures are accurate and adequate. The FAC comprises the Chief Executive, the Chief Financial Officer, the General Counsel & Company Secretary, the General Counsel Corporate, the Group Controller, the Chief Accountant, the Head of Investor Relations, the Head of Global Audit & Risk, the Controls Assurance Director, the Chief Business Integrity Officer and the company's external auditor. The Audit Committee reviewed the work of the FAC and a report on the conclusions of the FAC process was provided to the Audit Committee by the Chief Financial Officer.

Significant issues and judgements that were considered in respect of the 2020 financial statements were as follows. These include the matters relating to risks disclosed in the UK external auditor's report.

- Disclosure on the quality of the earnings (material items of income or expense) and one-off items included in cash flow. The Audit Committee agreed that sufficient disclosure was made in the financial statements.
- The Audit Committee determined that exceptional items are appropriately classified considering their size and nature, and sufficient disclosure is provided in the financial statements (see note 4).
- Review of carrying value of assets, in particular intangible assets. The Audit Committee assessed the impairment charge recognised and agreed that, at 30 June 2020, the recoverable amount of the company's assets was in excess of their carrying value (see notes 6, 9 and 10).
- Exchange rate used to translate operations in Venezuela. The Audit Committee agreed that the rate is reasonable for the year ended 30 June 2020 for consolidation purposes, that represents the best estimation of the rate at which capital and dividend repatriations are expected to be realised (see note 1).
- Disclosure on taxation. The Audit Committee agreed that the separate presentation of the tax risk appropriately addresses the significant change in the international tax environment and sufficient and transparent disclosures are provided for the ongoing tax discussions (see page 40 and note 7).
- Review of legal cases. The Audit Committee agreed that adequate provision and/or disclosure has been made for all material litigation and disputes, based on the current most likely outcomes, including the litigation summarised in note 18.

## Audit Committee report *continued*

- Assumptions used in respect of post employment plans. Having considered advice from external actuaries and assumptions used by companies with comparator plans, the Audit Committee agreed that the assumptions used to calculate the income statement and balance sheet assets and liabilities for post employment plans were appropriate (see note 13).
- Viability statement. The Audit Committee noted that severe but plausible risk scenarios had been identified; a robust risk assessment had been carried out; and the group's viability and going concern consideration proved with stress testing. Taking into account the company's balance sheet position, the Audit Committee expected the group to be able to meet its liabilities as they fell due over the three-year period ending 30 June 2023. The risk that the group would become insolvent during this timeframe was considered remote. The Audit Committee recommended to the Board that the Viability statement on page 41 be approved.

As part of its review of the Annual Report, the Audit Committee considered whether the report is 'fair, balanced and understandable' (noting the Code's reference to 'position' as well as 'performance, business model and strategy'). On the basis of this work, the Audit Committee recommended to the Board that it could make the required statement that the Annual Report is 'fair, balanced and understandable'.

### **Internal control and risk management; audit and risk programme; business conduct and ethics (including 'whistleblowing')**

At its meetings, the Audit Committee reviewed reports from the Head of the Global Audit & Risk (GAR) team, the Controls Assurance Director and the Chief Business Integrity Officer (including coverage of the areas mentioned in the title of this section) and had sight of the minutes of meetings of management's Audit & Risk Committee. The work and reporting to the Committee of these functions during the year included focus on cyber security and data access risks, internal and third-party data management and migration risks, controls testing and steps being taken to address internal audit findings, controls issues and investigations. The Committee also reviewed reports prepared by external advisors relating to the effectiveness of the GAR team as well as the company's compliance and ethics framework and function, and implemented various changes as a result of recommendations in those reports. The Committee also received regular updates from the General Counsel on significant litigation and from the Head of Tax on the group's tax profile and key issues.

The Committee also considered key risks and related mitigations, including those set out in the section of this Annual Report dealing with principal risks. Based on this activity during the year, the Audit Committee made a recommendation to the Board covering the nature and extent of the risks it was willing to take to achieve its strategic goals and its internal statement of risk appetite (which was considered also by management's Audit & Risk Committee). The Board agreed this recommendation.

Through the activities of the Audit Committee described in this report and its related recommendations to the Board, the Board confirms that it has reviewed the effectiveness of the company's systems of internal control and risk management and that there were no material failings identified and no significant failings identified which require disclosure in this Annual Report.

### **External auditor**

During the year, the Audit Committee reviewed the external audit strategy and the findings of the external auditor from its review of the interim results and its audit of the consolidated financial statements.

The Audit Committee reviews annually the appointment of the auditor (taking into account the auditor's effectiveness and independence and all appropriate guidelines) and makes a recommendation to the Board accordingly. Any decision to open the external audit to tender is taken on the recommendation of the Audit Committee. There are no contractual obligations that restrict the company's current choice of external auditor. Following the last tender process, PwC was appointed as auditor of the company in 2015. The audit partner for the year ended 30 June 2020

was Ian Chambers and Richard Oldfield is the audit partner from the year ending 30 June 2021 onwards. The company is required to have a mandatory audit tender after 10 years and, as the Audit Committee considers the relationship with the auditors to be working well and remains satisfied with their effectiveness, the Audit Committee does not currently anticipate that it will conduct an audit tender before it is required to do so. The Audit Committee considers this to be in the best interests of the company's shareholders for the reasons outlined above and will continue to monitor this annually to ensure the timing for the audit tender remains appropriate, taking into account the effectiveness and independence of the auditor.

The company has complied with the provisions of The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 (CMA Order) for the year ended 30 June 2020.

The Audit Committee assesses the ongoing effectiveness and quality of the external auditor and audit process on the basis of meetings and a questionnaire-based internal review with the finance team and other senior executives. The group has a policy on auditor independence and on the use of the external auditor for non-audit services, which is reviewed annually, most recently in July 2020. The review takes into consideration effectiveness and upcoming expected changes to UK FRC regulation on non-audit services. Effective from 1 July 2020, any member of the PwC global network shall provide to the company, its subsidiaries or any related entity only permissible services, subject to the approval of the Audit Committee after it has properly assessed through its governance process the threats to independence and the safeguards applied in accordance with the FRC Ethical Standard. Any FRC permissible service to be provided by the auditor, regardless of the size of the engagement, must be specifically approved by the Audit Committee or its nominated delegate. The policy explicitly specifies the auditor independence review and approval mechanism process for permissible engagements costing more than £250,000. Fees paid to the auditor for audit, audit-related and other services are analysed in note 3(b) to the consolidated financial statements. The nature and level of all services provided by the external auditor are factors taken into account by the Audit Committee when it reviews annually the independence of the external auditor.

### **'Financial expert', composition and other attendees**

For the purposes of the Code and the relevant rule under SOX, section 407, the Board has determined that Alan Stewart is independent and may be regarded as an Audit Committee financial expert, having recent and relevant financial experience, and that all members of the Audit Committee are independent Non-Executive Directors with relevant financial and sectoral competence. The Chairman, the Chief Financial Officer, the General Counsel & Company Secretary, the Group Controller, the Head of GAR, the Chief Business Integrity Officer, the General Counsel Corporate, the Controls Assurance Director, the Chief Accountant and the external auditor regularly attend meetings of the Committee. The Audit Committee met privately with the external auditor, the Chief Business Integrity Officer, the Controls Assurance Director and the Head of GAR regularly during the year.

### **FRC correspondence**

The Committee reviewed correspondence between the company and the FRC following their review of the company's annual report and accounts for the year ended 30 June 2019, including in respect of certain distributions and transactions related to the company's employee share schemes undertaken between 10 May 2019 and 9 August 2019 which were contrary to applicable provisions of the Companies Act 2006 as further detailed on page 107. The Committee has overseen the incorporation of reporting and controls improvements following the FRC's review and have incorporated those improvements into the company's annual report and accounts for the year ended 30 June 2020. In June 2020, the FRC confirmed that the matters raised by their review are closed. The Committee notes that the FRC's review does not provide assurance that the annual report and accounts are correct in all material respects as the FRC's role is to consider compliance with reporting requirements.