

9 October 2009

Chris Hodge  
Corporate Governance Unit  
Financial Reporting Council  
Fifth Floor  
Aldwych House  
71-91 Aldwych  
London WC2B 4HN

Dear Chris

## **Review of the effectiveness of The Combined Code (the “Code”) - second consultation**

Thank you for the opportunity to comment again on the Code; once more, we hope you find our views helpful.

We remain of the view that it is ultimately behaviours rather than process that produce good corporate governance. Accordingly, we are supportive of continuing the principles based approach of the Code, as opposed to putting in place further law and regulation.

We are pleased to note that the three principles set out in section 1 of your consultation (i.e. emphasis on non-binding guidance, non-boiler plate disclosure and avoidance of an increase in the overall level of prescription), which will guide you in the next phase of the review of the Code, are consistent with our views.

In general, our views are based on a belief that, currently our corporate governance arrangements (including risk management) at Diageo have worked demonstrably well and the Code and its related guidance continues to encourage us to develop our governance arrangements. In addition, we do not see any significant evidence that a greater volume of prescriptive rules produces better corporate governance behaviour. Indeed, our belief is that prescriptive rules will serve to provide more boiler-plate disclosure not less, and less openness and engagement, to the detriment of the level of governance assurance sought.

However, we understand that there is a need to reassure stakeholders, including the UK Government, that recommendations arising from the review are credible, workable and provide an evidential confirmation of improved governance.

In this regard, and consistent with our response to the original consultation, we think that there are a number of smaller but important areas which could help achieve this.

Firstly, provide some requirement to state in the corporate governance report the ways in which a company believes that its compliance with the Code is linked to the behaviours that boards (and non-executive directors in particular) wish to see in the management of companies. This might give investors a sense of what the Code is trying to achieve and compel companies to undergo the thought process necessary to identify these behaviours.

Secondly, more encouragement towards forward looking reporting (especially for risk management) as opposed to reporting on the past might help to steer corporate governance towards a more proactive rather than reactive position.

In general, we believe different businesses face different risk profiles, so we are not supportive of a wholesale lift of the Walker recommendations applying to non-financial companies, particularly in the areas of risk. Additionally, whilst not wanting to put a tick and cross against each provisional proposal made in the Code consultation, we are not supportive of the specific 'mandatory' related proposals.

We believe that the role of NEDs should remain one of strategy and oversight, not one of managing the business. We believe that the key is to appoint individuals of the required calibre to the roles of chairman and NED and then to allow them the scope to exercise their judgement on these and other issues on a case by case basis for each company. On NEDs, we support the relaxing of the nine year rule on NED tenure, as we believe that this would help continuity and retention of experience and benefit the pool of available NEDs as a whole.

One area that we think merits further discussion is the engagement between companies and large shareholders, in the sense that this should result in less "short-termism" and more focus on the long-term health of the company. Clearly, finding a way to achieve this is challenging but it may be a key driver of boards' behaviour.

We wholeheartedly support the FRC's project to reduce complexity in corporate reporting.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'J. Nicholls', with a stylized, cursive script.

John Nicholls  
Deputy Secretary