

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 64978 / July 27, 2011

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 3307 / July 27, 2011

ADMINISTRATIVE PROCEEDING
File No. 3-14490

<p>In the Matter of</p> <p>DIAGEO plc,</p> <p>Respondent.</p>
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ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER AND A CIVIL PENALTY

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Diageo plc (“Diageo” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (“Offer”), which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over the Respondent and the subject matter of these proceedings, which are admitted, the Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order and a Civil Penalty (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that:

Summary

This matter concerns multiple violations of the Foreign Corrupt Practices Act ("FCPA") by Respondent Diageo, one of the world's largest producers of premium alcoholic beverages. Over more than six years, Diageo, through its subsidiaries, paid over \$2.7 million to various government officials in India, Thailand, and South Korea in separate efforts to obtain lucrative sales and tax benefits.

In India, from 2003 through mid-2009 Diageo made over \$1.7 million in illicit payments to hundreds of Indian government officials responsible for purchasing or authorizing the sale of its beverages. Increased sales from these payments yielded more than \$11 million in ill-gotten gains. In Thailand, from 2004 through mid-2008, Diageo paid approximately \$12,000 per month – totaling nearly \$600,000 – to retain the consulting services of a Thai government and political party official. This official lobbied extensively on Diageo's behalf in connection with multi-million dollar pending tax and customs disputes, contributing to Diageo's receipt of certain favorable dispositions by the Thai government. With respect to South Korea, in 2004, Diageo paid 100 million won (KRW) (over \$86,000) to a customs official as a reward for his role in the government's decision to grant Diageo significant tax rebates. Diageo also paid over \$100,000 in travel and entertainment expenses for South Korean customs and other government officials involved in these tax negotiations. Separately, Diageo made hundreds of gift payments totaling over \$230,000 to South Korean military officials in order to obtain and retain liquor business.

Diageo and its subsidiaries failed to account accurately for these illicit payments in their books and records. Exercising lax oversight, Diageo also failed to devise and maintain internal accounting controls sufficient to detect and prevent the payments.

Respondent

Diageo, headquartered in London, United Kingdom, is a leading producer and/or distributor of premium branded spirits, beer, and wine, including Johnnie Walker, Smirnoff, J&B, Baileys, Captain Morgan, Tanqueray, and Guinness. Through its various direct and indirect subsidiaries, Diageo maintains operations in more than 180 countries. Diageo's American Depository Shares are registered with the Commission pursuant to Section 12(b) of the Exchange Act and trade on the New York Stock Exchange under the symbol DEO. As a foreign private issuer, Diageo files annual reports with the Commission on Form 20-F.

¹ The findings herein are made pursuant to Respondent's Offer and are not binding on any other person or entity in this or any other proceeding.

Other Relevant Entities

Diageo India Pvt. Ltd. (“DI”) is a wholly-owned indirect subsidiary of Diageo, and is based in Mumbai, India. Throughout the relevant period, Diageo incorporated DI’s financial results into the consolidated financial statements that it filed with the Commission.

Diageo Moet Hennessy Thailand (“DT”) is a joint venture of Diageo, and is based in Bangkok, Thailand. Throughout the relevant period, Diageo had an indirect majority economic interest in, and operational control of, DT and incorporated DT’s financial results into the consolidated financial statements that it filed with the Commission.

Diageo Korea Co. Ltd. (“DK”) is a wholly-owned indirect subsidiary of Diageo, and is based in Seoul, South Korea. Throughout the relevant period, Diageo incorporated DK’s financial results into the consolidated financial statements that it filed with the Commission.

Facts

A. Background

Diageo’s history of rapid multinational expansion through mergers and acquisitions contributed to defects in its FCPA compliance programs. Diageo was formed in 1997 from the merger of Guinness plc and Grand Metropolitan plc. As a result of that merger, Diageo acquired its Indian subsidiary, DI, and an indirect majority economic interest in, and operational control of, its Thai joint venture, DT. Diageo acquired its South Korean subsidiary, DK, in 2001 as part of a larger acquisition of the spirits and wine business of The Seagram Company Ltd. At the time of these acquisitions, Diageo recognized that its new subsidiaries had weak compliance policies, procedures, and controls. Nevertheless, Diageo failed to make sufficient improvements to these programs until mid-2008 in response to the discovery of the illicit payments described below.

B. India

For many years, Diageo, through DI, engaged in a pervasive practice of making illicit direct and indirect payments to government officials throughout India to obtain and retain liquor sales. As a result, Diageo was unjustly enriched by \$11,306,081 from increased sales.

Payments to Employees of Government Liquor Stores

From at least 2003 through June 2009, DI paid an estimated \$792,310 in improper cash payments through its third-party distributors to 900 or more employees of government liquor stores in and around New Delhi. DI also paid an estimated \$186,299 (representing 23% of the payments) in “cash service fees” to the distributors as compensation for advancing the funds. DI made the payments to increase government sales orders of its products, and to secure favorable product placement and promotion within the stores.

Although the improper payments continued for at least six years, it was not until July 2009 that DI instructed its distributors to discontinue them.

DI failed properly to account for either its reimbursement of the illicit payments or the associated “cash service fees.” DI’s distributors sought recompense by either submitting debit notes or requesting increases in their per-case commissions. Each of the debit notes falsified or obscured the nature of the payments by purporting to be for “market scheme settlement,” “deposit[s] with Delhi Excise,” “incentives,” “special incentives,” or “promotions.” By recording its reimbursement of the debit notes as “promotion” or “special incentive” expenses in innocuously labeled accounts – “Promotions-Outlet,” “Promotions,” “Secondary,” or “Trade Incentives” – DI concealed the underlying payments’ purpose and recipients. Nor did DI’s practice of recording the increased per-case commissions under the generic rubric of “commissions” in any way indicate that they constituted reimbursement for cash payments to government employees.

Payments to Employees of India’s Canteen Stores Department

During the same six-year period (2003 – 2009), Diageo, through DI, also reimbursed an estimated \$530,955, and made plans to reimburse an additional \$79,364, in improper cash payments made by third-party sales promoters to government employees of the Indian military’s Canteen Stores Department (“CSD”). The payments, made with DI’s knowledge and authorization, were designed to: (i) foster the promotion of Diageo products in the CSD’s canteen stores (analogous to the U.S. military’s post exchanges); (ii) obtain initial listings and annual label registrations for Diageo brands, price revision approvals, and favorable factory inspection reports; (iii) secure the release of seized shipments of Diageo products; and (iv) promote good will through the distribution of Diwali and New Year’s holiday gifts to CSD employees.

DI’s accounting for its reimbursement of payments to CSD employees bore the same defects as that for the government liquor stores. From June 2003 through June 2007, DI’s sales promoters submitted debit notes mischaracterizing the payments as “business promotion expenses,” “miscellaneous expenses,” “expenses incurred on your behalf,” “factory expenses,” “travelling expenses,” or “telephone expenses.” DI recorded its reimbursements as “scheme” or “special scheme” payments. After June 2007, DI reimbursed the payments through increased per-case commissions which it recorded as “DIF – selling commission.” The nondescript terms used by DI on its books and records concealed the fact that DI was reimbursing its promoters for wrongful cash payments to CSD employees.

Payments to Label Registration and Excise Officials

Diageo failed to ensure that DI properly accounted for a number of additional, improper payments to government officials who controlled administrative functions vital to DI’s business. From at least 2003 through 2008, Diageo, through DI, reimbursed an estimated \$98,310 in cash payments made by its third-party promoters and distributors to government officials in the North Region of India and in the State of Assam for the purpose

of securing label registrations for Diageo products.² The distributors submitted debit notes to DI that described the payments as “special rebates” or as “an incentive for reaching sales targets.” DI recorded the reimbursements as “special rebates” or “trade incentives,” thereby masking the fact that they represented recompense for illicit payments to government employees.

In addition, from at least 2003 through June 2009, Diageo, through DI, paid an estimated \$78,622 in extra commissions to its distributors in the North Region to reimburse them for payments made to Excise officials to secure import permits and other administrative approvals. DI again hid the fact that it was reimbursing the distributors for improper payments to government employees by recording them on its books of account as “DIF – selling commission.”

C. Thailand

From April 2004 through July 2008, Diageo, through DT, retained the services of a Thai government and foreign political party official (the “Thai Official”) to lobby other Thai officials to adopt Diageo’s position in several multi-million dollar tax and customs disputes. For this retainer DT paid approximately \$12,000 per month for 49 months, for a total of \$599,322. DT compensated the Thai Official through 49 direct payments to a political consulting firm (the “Consulting Firm”) for which the Thai Official acted as a principal. Most, if not all, of the \$599,322 paid to the Consulting Firm was for the Thai Official’s services and accrued to his benefit.

The Thai Official served as a Thai government and/or political party official throughout the relevant period (April 2004 – July 2008) in which he received compensation from DT. At various times the Thai Official served as Deputy Secretary to the Prime Minister, Advisor to the Deputy Prime Minister, and Advisor to the Ministry of Agriculture and Cooperatives. The Thai Official also served on a committee of the ruling Thai Rak Thai political party, and as a member and/or advisor to several state-owned or state-controlled industrial and utility boards. DT’s senior management knew that the Thai Official was a government officer during its engagement of the Consulting Firm. The Thai Official was the brother of one of DT’s senior officers at that time. Several members of Diageo’s global and regional management attended meetings with the Thai Official and senior members of the Thai government.

The Thai Official provided extensive lobbying services on behalf of Diageo and DT in connection with several important tax and customs disputes that were pending between Diageo and the Thai government. For example, with respect to excise taxes,³ the Thai Official coordinated and attended numerous meetings between senior Thai government

² The North Region of India includes the following thirteen states: Bihar, Chandigarh, Chattisgarh, Delhi, Haryana, Punjab, Himachal Pradesh, Jammu, Jharkhand, Madhya Pradesh, Rajasthan, Uttar Pradesh, and Uttaranchal.

³ An excise tax refers to a tax on a good produced for sale, or sold, within a country.

officials and senior Diageo and DT management, including two meetings in April and May 2005 with Thailand's then Prime Minister. In May 2005, shortly following the meetings arranged by the Thai Official, the Prime Minister made a radio address publicly endorsing Diageo's position in favor of a "specific" approach (based on quantity) rather than an "ad valorem" approach (based on price) to calculating excise taxes.

On Diageo's behalf, the Thai Official also met repeatedly with senior commerce, finance, and customs authorities in charge of the transfer pricing and import tax disputes,⁴ as well as with members of the Thai parliament. The Thai Official's services contributed to Diageo's successful resolution of several components of these disputes. For example, during 2004 and 2005 Diageo and DT were actively engaged in a dispute with the Thai government over the appropriate transfer pricing formula applied to One Liter bottles of Johnnie Walker Red Label and Black Label Scotch whiskey. Based in part on the Thai Official's lobbying efforts, the Thai government accepted important aspects of DT's transfer pricing method and released over \$7 million in bank guarantees that DT had been required to post while the tax dispute was pending.

DT improperly accounted for the monthly retainer that it paid to the Thai Official through his Consulting Firm. The bulk of the payments assumed the form of monthly disbursements of \$11,989 to the Consulting Firm for advisory fees and out-of-pocket expenditures. Approximately \$15,169 of the payments was for reimbursement of entertainment expenses, including those incurred on behalf of government officials. DT recorded the payments under one of the following generically-labeled accounts: (i) "Outside Services"; (ii) Corporate Social Responsibility"; (iii) Corporate Communications"; (iv) "EA [External Affairs] Project"; or (v) "Stakeholder Engagement." Typically, DT charged payments to the Consulting Firm against the same account for a period of time, and then switched to another account without any discernible rationale for the change in accounting treatment. DT's books and records did not reflect the fact that DT was paying a Thai government and political party official to lobby in connection with multimillion dollar tax and customs disputes.

D. South Korea

Reward Payment to a Korean Customs Official

As in Thailand, Diageo had significant tax and customs issues in South Korea. In April 2003, DK, under Diageo's direction, requested from South Korea a more advantageous formula for calculating the transfer pricing, for tax purposes, of Windsor Scotch whiskey that DK was importing into South Korea. As part of those negotiations, DK also sought tens of millions of dollars in tax rebates based on a claim that DK had overpaid under the then existing transfer pricing formula. In April 2004, following a year of intense negotiations and

⁴ Transfer pricing refers to the cost that individual entities within multinational firms charge for the goods and services that they supply to one another.

lobbying by DK, the South Korean government granted DK a rebate of approximately \$50 million.⁵

In July 2004, three months after DK received the tax rebates, a DK manager (the “Manager”) paid an apparent reward of 100 million KRW (\$86,339) to a Korean Customs Service official (the “Customs Official”) who had played a key role in the transfer pricing negotiations. With the approval of DK’s then chief financial officer, the Manager generated 60 million KRW (\$51,802) of the payment by means of a surreptitious cash kickback scheme. The Manager solicited an inflated invoice from DK’s third-party customs brokerage firm (the “Customs Broker”), which had provided DK with consulting services during the transfer pricing negotiations. As orchestrated, DK paid an inflated invoice amount to the Customs Broker, which then gave 60 million KRW (\$51,802) in cash back to the Manager. The Manager funded the remaining 40 million KRW (\$34,537) of the total reward amount from personal sources. The Manager then provided the Customs Official with 100 million KRW (\$86,339) in the form of ten bank checks of approximately 10 million KRW (\$8,634) each.

Diageo, through DK, improperly and falsely accounted for the cash reward payment to the Customs Official. DK booked the invoice from the Customs Broker which it had used to fund 60% of the payment to a general ledger account for professional services and consulting fees. DK also described the expense as relating to the Customs Broker’s work on the transfer pricing negotiations. DK’s books and records, however, do not reveal that DK solicited the invoice to generate a cash payment to the Customs Official, or that the Customs Broker had failed to render the full services reflected on the invoice. Nor do DK’s books and records show that the Manager had personally funded the remainder of the cash reward.

Payments for Travel and Entertainment for Korean Customs Service Officials

During the course of the transfer pricing negotiations in 2003 and 2004, DK also paid \$109,253 in travel and entertainment costs for Korean customs and other government officials. Some of these expenses were unapproved and constituted improper inducements of the South Korean officials. For example, in December 2003, the Customs Official and several official colleagues traveled to Scotland with DK employees. The purported reason for the trip was to inspect Diageo’s Windsor Scotch production facilities as part of the transfer pricing negotiations. During the course of this apparently legitimate trip, DK’s chief financial officer and the Manager took the South Korean officials on a purely recreational side-trip to Prague and Budapest.

DK failed properly to account for the \$109,253 in travel and entertainment related expenses. The company booked 46 of the related accounting entries to a general ledger account entitled “Entertainment – Customer,” thereby hiding the fact that it was furnishing the travel and entertainment to government officials. DK intended the false accounting treatment to prevent the South Korean authorities, including the Korean National Tax

⁵ The South Korean government is currently in the process of reevaluating the appropriate transfer price for Diageo’s Windsor Scotch whiskey.

Service, from detecting the officials' acceptance of the travel and entertainment. DK failed to record an additional seven expenses related to entertainment connected to the transfer pricing project. Diageo also failed to implement a system of internal accounting controls that reasonably could have prevented DK's concealment of these expenditures.

Gift Payments to Military Officials

From at least 2002 through at least 2006, Diageo, through DK, routinely made hundreds of small payments to South Korean military officers for the purpose of obtaining or maintaining business and securing a competitive business advantage. The payments assumed two forms: (i) holiday and vacation gifts known as "rice cake" payments; and (ii) business development gifts, called "Mokjuksaupbi" payments.

Rice cake payments were customary and traditional presents that Diageo, through DK, provided to scores of military officers – many of whom were responsible for procuring liquor – several times each year during holidays and vacations. From 2002 through 2006, DK made approximately 400 rice cake payments, totaling at least \$64,184, in the form of cash or gift certificates ranging in value between \$100 and \$300 per recipient. In October 2004, a senior officer within Diageo's global compliance department explicitly approved the practice of making rice cake payments after a DK employee explained that the company would face a competitive disadvantage if it refrained.

Over the same four-year period, Diageo, through DK, also spent approximately \$165,287 on hundreds of non-traditional, non-seasonal gifts and entertainment for the military. Of these so-called "Mokjuksaupbi" payments (a term that was broadly intended by DK to refer to "payments for relationships with customers"), approximately \$106,051 were for the purpose of influencing specific purchasing decisions. For example, in 2003, DK personnel requested approval of approximately \$2,600 to entertain army personnel "for their cooperation" in connection with the re-selection of Windsor Scotch.

Diageo failed to ensure that DK properly accounted for the rice cake and Mokjuksaupbi payments. During 2002 and 2003, DK used fake vendor invoices to generate cash for the rice cake payments and, in 2002, failed to record any of the rice cake payments on its general ledger. DK incorrectly recorded subsequent rice cake payments, and all of the Mokjuksaupbi payments, under general ledger accounts for expenses such as sales, promotion, or customer entertainment. Diageo thereby concealed the fact that it was providing gifts to military personnel from South Korean government auditors.

FCPA Violations

Section 13(b)(2)(A) of the Exchange Act requires public companies to make and keep books, records, and accounts that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the issuer's assets.

Diageo's books and records did not accurately reflect illicit payments that it made, through its subsidiaries, to Indian, Thai, and South Korean government and military officials.

Instead, Diageo, through DI, DT, and DK, disguised the improper payments as legitimate vendor expenses or recorded them under misleading rubrics such as “factory expenses,” “telephone expenses,” “shareholder stake,” and “sales support.” In several instances, the illicit payments were not recorded at all. As a result, Diageo violated Section 13(b)(2)(A) of the Exchange Act.

Section 13(b)(2)(B) of the Exchange Act requires companies to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions: (i) are executed in accordance with management’s general or specific authorization; and (ii) are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria applicable to such statements, and to maintain accountability for assets.

As evidenced by the extent and duration of the wrongful payments and their improper recordation, Diageo failed to devise and maintain sufficient internal accounting controls. Accordingly, Diageo violated Section 13(b)(2)(B) of the Exchange Act.

Diageo’s Cooperation and Remedial Efforts

In determining to accept the Offer, the Commission considered the cooperation afforded the Commission staff and certain remedial measures undertaken by Diageo, including employee termination and significant enhancements to its compliance program.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Diageo’s Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent Diageo cease and desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act;

B. Respondent shall, within 30 days of the entry of this Order, pay disgorgement of \$11,306,081 and prejudgment interest of \$2,067,739 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to SEC Rule of Practice 600. Payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier’s check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Securities and Exchange Commission, Office of Financial Management, 100 F St., NE, Stop 6042, Washington, DC 20549; and (D) submitted under cover letter that identifies Diageo plc as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Scott F. Weisman, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549.

C. Respondent shall, within 30 days of the entry of this Order, pay a civil money penalty in the amount of \$3,000,000 to the United States Treasury. If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. 3717. Payment shall be: (A) made by wire transfer, United States postal money order, certified check, bank cashier's check or bank money order; (B) made payable to the Securities and Exchange Commission; (C) hand-delivered or mailed to the Securities and Exchange Commission, Office of Financial Management, 100 F St., NE, Stop 6042, Washington, DC 20549; and (D) submitted under cover letter that identifies Diageo plc as a Respondent in these proceedings, the file number of these proceedings, a copy of which cover letter and money order or check shall be sent to Scott F. Weisman, Assistant Director, Division of Enforcement, Securities and Exchange Commission, 100 F Street, N.E., Washington, DC 20549.

D. Respondent acknowledges that the Commission is not imposing a civil penalty in excess of \$3,000,000 based upon its cooperation in a Commission investigation. If at any time following the entry of the Order, the Division of Enforcement ("Division") obtains information indicating that Respondent knowingly provided materially false or misleading information or materials to the Commission or in a related proceeding, the Division may, at its sole discretion and without prior notice to the Respondent, petition the Commission to reopen this matter and seek an order directing that the Respondent pay an additional civil penalty. Respondent may not, by way of defense to any resulting administrative proceeding: (1) contest the findings in the Order; or (2) assert any defense to liability or remedy, including, but not limited to, any statute of limitations defense.

By the Commission.

Elizabeth M. Murphy
Secretary