United Distillers UK PLC

Directors' report and financial statements

135736

30 June 1999

Contents

Directors' report

The directors present their annual report and the audited financial statements for the year ended 30 June 1999.

Principal activities

The company's principal activities are the marketing and sale of spirits. The directors foresee no changes in the company's activities.

Business review

During the year, the company's base at Cherybank, Perth was closed and its operations were transferred to Harlow as part of the group's reorganisation following the merger of Grand Metropolitan PLC and Guinness PLC. As a result of the transfer, the company incurred costs of £4.3m in the year.

With effect from 30 June 1999, the company ceased to trade. During the course of the financial year, its businesses, both in the UK and in Europe, and its assets and liabilities were transferred to other members of the group.

Year 2000

The Year 2000 problem refers to the inability of some information systems and computerised equipment to handle four-digit years, causing them to generate inaccurate information and potentially to fail. The Diageo group established a compliance programme in each of its main business units (UDV, Pillsbury, Guinness, Burger King) and subsidiaries to investigate and manage potential impacts. The programmes were co-ordinated at Group level with regular status reports to the Diageo board.

All critical systems and processes were declared Year 2000 Ready in September 1999, and to date no major issues have been identified. Procedures are in place to monitor developments and will continue for as long as the Year 2000 risk remains.

The cost of managing the Year 2000 problem is estimated to be £66 million of which £62 million has been charged to the profit and loss account since the start of the programme.

The full cost of managing the Year 2000 problem for United Distillers UK PLC has not been identified separately, but is included within the overall programme cost shown in the annual report of the ultimate parent company, Diageo plc.

Proposed introduction of the Euro

In accordance with the Treaty on European Union, signed at Maastricht on 7 February 1992, the third stage of Economic and Monetary Union (EMU) commenced on 1 January 1999. The Diageo group's euro-readiness is being managed as a discrete business project. The Group expects to have systems and procedures in place which will enable it to conduct euro transactions appropriate to local market requirements.

The Diageo group is also working actively with key business suppliers, joint distribution arrangement partners and customers. In addition, monetary union may have a significant impact on macroeconomic factors, including interest and foreign exchange rates.

Key commercial risks, such as pricing transparency, have been analysed, with a view to reducing any impact through active management over the transition period and beyond. However, there can be no assurance that the euro will not have a negative impact. The impact of future entry to EMU of other European countries (particularly the UK) has been similarly analysed.

The cost associated with the euro-readiness project for United Distillers UK PLC has not been identified separately but is included within the overall project cost in the annual report of the ultimate parent company, Diageo plc.

Directors' report *(continued)*

Proposed dividend

An interim dividend of £1,640 per share was paid during the year.

Policy and practice on payment of creditors

Given the international nature of the Diageo Group's operations, there is no standard code in respect of payments to suppliers. Companies are responsible for agreeing terms and conditions for their business transactions when orders for goods and services are placed, ensuring that suppliers are aware of the terms of payment and including the relevant terms in contracts where appropriate. These arrangements are adhered to when making payments, subject to the terms and conditions being met by the supplier.

At the year end, there were nil days *(1998: 9 days)* purchases in trade creditors.

Directors and directors' interests

The directors who held office during the year were as follows:

MC Keiller	(resigned 16 November 1998)
JC Long	(resigned 16 November 1998)
IK Meakins	
GL Thompson	(resigned 16 June 1999)
RH Myddelton	(appointed 16 November 1998)
SM Bunn	(appointed 16 November 1998)
NC Rose	(resigned 1 July 1999)
PK Bentley	(appointed 1 July 1999)

None of the directors who held office at the end of the financial year had any disclosable interest in the shares of the company.

The directors who held office at the end of the financial year had the following beneficial interests in the shares of Diageo plc, according to the register of directors' interests:

	Ordinary shares of 28 101/108p (1)	Ordinary shares of 28 101/108p (1)	RSP Awards (2)	Guinness LTIP (2)	Diageo LTIP (3)	Diageo LTIP (3)
					Performance cycle commencing	
	1.7.98 or date of appointment	30.6.99	30.6.99	30.6.99	1.1.98	1.1.99
IK Meakins	3,819	2,635	-	17,139	21,098	25,578
RH Myddelton	20,049	19,519	18,081	-	18,524	16,844
NC Rose	3,572	3,572	19,550	-	36,021	32,752

(1) **Ordinary Shares**

Interests in ordinary shares at 1 July 1998, or date of appointment where applicable, include B shares converted at a rate of 70.993915 ordinary shares to every 100 B shares, although the conversion actually occurred on 1 August 1998.

Directors' report *(continued)*

Directors and directors' interests *(continued)*

(2) **The Guinness LTIP and The Grand Metropolitan Restricted Share Plan (RSP)**

Awards over shares were granted to senior executives, with eventual transfer dependent on the performance of total shareholder return (TSR) against a comparator group of companies at the end of three years after the date of grant. Following the merger, performance targets attached to the Guinness awards granted in 1996 were waived. The 1997 awards granted by Grand Metropolitan and Guinness are now dependent upon the performance of Diageo's TSR against comparator groups of companies.

(3) **The Diageo LTIP (LTIP)**

Under the Diageo LTIP, approved in August 1998, eligible senior executives are granted a conditional right to receive shares or, exceptionally, a cash sum. The rights vest after the end of a three year period following the date of grant (the "performance cycle") provided a performance test is achieved and subject to the discretion of the trustees who operate the LTIP. The performance test is a comparison of the annualised percentage growth in Diageo's share price (assuming all dividends and capital distributions are re-invested) known as total shareholder return (TSR) with the TSRs of a defined peer group of 20 companies over a three year period. The remuneration committee will not recommend the release of awards if there has not been an underlying improvement in the financial performance of Diageo. The first LTIP performance cycle runs from 1 January 1998 to 31 December 2000 and the second from 1 January 1999 to 31 December 2001. Awards of shares will be released, subject to the performance test and the discretion of the trustees, in March 2001 and March 2002 respectively. The number of awards shown will only be released if Diageo reaches position five within the peer group (upper quartile). At position four 125% of the original awards will vest and, at position three or above, 150%. At position ten (median position), 50% of the awards will vest. Between median and upper quartile, vesting will be calculated on a straight line basis. Awards will lapse if Diageo does not reach position ten.

According to the register of directors' interests, no rights to subscribe for shares in or debentures of the company were granted to any of the directors or their immediate families, or exercised by them, during the financial year.

The directors who held office at the end of the financial year had the following beneficial interests in the shares of the ultimate parent company, Diageo plc:

	Number of options during the year			
	At start of year or date of appointment	Granted	Exercised	At end of year
IK Meakins	56,934	-	29,607	27,327
RH Myddleton	207,522	-	3,168	204,354
NC Rose	176,320	-	-	176,320

The directors held the above options under Grand Metropolitan PLC and Diageo plc share option schemes at prices between 314p and 494p per share exercisable by 2006. No options lapsed and no awards vested during the year.

The mid-market share price of Diageo plc shares fluctuated between 480.5p and 778.5p per share during the year. The mid-market share price on 30 June 1999 was 662.5p.

At 30 June 1999 the directors had an interest in 22,444,659 shares and 3,123,181 shares subject to call options held by trusts to satisfy grants made under ex-Grant Metropolitan incentive plans, ex-Guinness incentive plans and Diageo incentive plans and savings-related share option schemes.

Directors' report *(continued)*

Employees

The parent company is committed to the development of employee consultation and, thereby, to their greater involvement in the company's operations. The directors continue to place a high priority on good communications practices at all levels. Responsibility for ensuring that company employees are informed of and, where appropriate, consulted upon matters of concern affecting their immediate jobs rests with departmental managers with support from the personnel function. On-site job discussions between managers and employees are encouraged.

On a wider basis, the parent company provides more general information to and for its employees concerning its performance and on economic and other matters affecting it. The methods used to disseminate such information are bulletins and related publications, including a monthly house journal. In addition, a twice yearly video presentation for employees sets out world-wide developments of the company, its products and its people. Information is also communicated when employees participate in induction or training courses, or by the circulation of information personally to all employees. The company has continued to maintain these practices during the year.

It is the policy of the parent company to encourage employees to participate in a SAYE share option scheme. It is also parent company policy to enable employees to benefit from the contribution they have made to the generation of improved profits. This is done by way of a profit sharing scheme, paid in ordinary shares of Diageo plc, in which all employees are entitled to participate.

The company continues to support initiatives by employees in fund-raising events to assist registered charitable organisations by matching the value of the support so raised.

The company's managers are instructed to give sympathetic consideration, when recruiting, to applications from disabled persons and to bear in mind the special needs of disabled employees in regard to training, structure of company premises and facilities and to ensure that disabled employees are not adversely affected in their career opportunities. Employees who become disabled and are unable to continue in their existing jobs are given the opportunity to be retrained for suitable alternative employment.

It is recognised that the company's continuing success depends upon the quality of its employees, and its policies are designed to attract, retain and motivate the best staff. This is achieved by offering equal opportunities regardless of sex, race, religion or disability.

Political and charitable contributions

The company made no political contributions during the year. Donations to UK charities amounted to £2,793.

Auditors

In accordance with Section 384 of the Companies Act 1985, a resolution for the re-appointment of KPMG Audit Plc as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

By order of the board

MD Peters
Secretary

Edinburgh Park
5 Lochside Way
Edinburgh
EH12 9DT

20 APRIL 2000

Statement of directors' responsibilities

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

KPMG

KPMG Audit Plc
37 Hills Road
Cambridge CB2 1XL
United Kingdom

Report of the auditors to the members of United Distillers UK PLC

We have audited the financial statements on pages 7 to 18.

Respective responsibilities of directors and auditors

As described on page 5 the company's directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the company's affairs as 30 June 1999 and of its profit for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc — 25 April 2000

KPMG Audit Plc
Chartered Accountants
Registered Auditor

Profit and loss account

for the year ended 30 June 1999 (18 months ended 30 June 1998)

	Note	1999 £000	18 months ended 1998 £000
Turnover	2	408,781	835,116
Cost of sales		(244,990)	(511,503)
Gross profit		163,791	323,613
Net operating costs	3, 4	(71,048)	(201,615)
Operating profit		92,743	121,998
Loss on sale of fixed assets - continuing operations	5	(120)	-
Other interest receivable and similar income	9	4,876	304
Interest payable and similar charges	10	(619)	(10)
Profit on ordinary activities before taxation	6	96,880	122,292
Tax on profit on ordinary activities	11	(29,300)	(40,347)
Profit on ordinary activities after taxation		67,580	81,945
Dividends on equity and non-equity shares	12	(82,000)	-
Retained profit /(loss) for the year/18 month period		(14,420)	81,945

There were no recognised gains or losses in the year ended 30 June 1999 or in the 18 months ended 30 June 1998 other than the retained profit shown above.

All activities relate to operations which were transferred on 30 June 1999 to UDV (HP) Ltd, a fellow subsidiary of Diageo plc.

Balance sheet
at 30 June 1999 (31 December 1997)

	Note	1999 £000	£000	1998 £000	£000
Fixed assets					
Tangible assets	*13*		-		5,774
Investments	*14*		-		13
			-		5,787
Current assets					
Stocks	*15*	-		24,824	
Debtors	*16*	547,086		1,312,213	
Cash at bank and in hand		-		4,230	
		547,086		1,341,267	
Creditors: amounts falling due within one year (including convertible debt)	*17*	(479,211))		(1,264,759)	
Net current assets			67,875		76,508
Net assets			67,875		82,295
Capital and reserves					
Called up share capital	*19*		50		50
Profit and loss account	*20*		67,825		82,245
Equity shareholders' funds			67,875		82,295

These financial statements were approved by the board of directors on 20 APRIL 2000 and were signed on its behalf by:

R H Myddelton
Director

Note of historical cost profits and losses
for the year ended 30 June 1999

	1999 £000	1998 £000
Reported profit on ordinary activities before taxation	96,880	122,292
Difference between a historical cost depreciation charge and the actual depreciation charge calculated on the revalued amount	-	294
Historical cost profit on ordinary activities before taxation	96,880	122,586
Historical cost profit / (loss) for the year retained after taxation and dividends	(14,420)	82,239

Reconciliation of movements in shareholders' funds
for the year ended 30 June 1999

	1999 £000	1998 £000
Profit for the financial year/18 month period	67,580	81,945
Dividends	(82,000)	-
Net addition / (reduction) to shareholders' funds	(14,420)	81,945
Opening shareholders' funds	82,295	350
Closing shareholders' funds	67,875	82,295

Notes
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the company's financial statements.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards, and under the historical cost accounting rules, modified to include the revaluation of certain assets.

Under Financial Reporting Standard 1 the company is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the company in its own published consolidated financial statements.

As the company is a wholly owned subsidiary of Diageo plc, the company has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the group (or investees of the group qualifying as related parties). The consolidated financial statements of Diageo plc, within which this company is included, can be obtained from the address given in note 23.

Fixed assets and depreciation

Depreciation is provided to write off the cost or valuation less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Freehold buildings	-	2-4% per annum
Plant, machinery and fittings	-	10-25% per annum
Motor vehicles	-	25% per annum

No depreciation is provided on freehold land.

Investments

Investments are stated at cost and amortised over their expected useful life.

Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling under hedging arrangements with Diageo plc. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

Stocks

Stocks are stated at the lower of cost and net realisable value.

Cost is based on transfer cost from Group companies and invoice cost for agency brands.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. Provision is made for deferred tax only to the extent that it is probable that an actual liability will crystallise.

Notes *(continued)*

1 Accounting policies (continued)

Advance corporation tax recoverable by deduction from future corporation tax is carried forward within deferred taxation or as ACT recoverable within debtors as appropriate.

Pension

The company is a member of a group pension scheme which is operated by its ultimate parent company, Diageo plc (note 22).

Contributions to the Group pension scheme are assessed by a qualified actuary based on the costs of providing pensions across all participating companies. Costs are not determined for each individual company and accordingly contributions are charged to the profit and loss account when they become payable.

Turnover

Turnover represents the amounts (excluding value added tax) derived from the provision of goods and services to customers, net of price list discounts but including Customs and Excise duty.

2 Analysis of turnover

	1999 £000	1998 £000
By geographical market		
UK	240,521	379,012
Republic of Ireland	961	2,419
Europe	167,299	453,685
	408,781	835,116

All sales were derived in the UK.

The company operates within one business segment.

3 Analysis of net operating costs

	1999 £000	1998 £000
Staff costs (note 8)	7,206	14,787
Depreciation	535	1,496
Administration expenses	31,614	142,935
Distribution costs	1,619	8,903
Other operating costs	30,074	33,494
	71,048	201,615

Notes *(continued)*

4 Exceptional costs

Included within operating costs are the following exceptional charges/(credits):

	1999 £000	1998 £000
Pension refund	(102)	-
Stock revaluation	(3,031)	-
Whisky revaluation	806	-
Merger costs	4,335	8,182
	2,008	8,182

The company received a pension refund in the year due to a contributions holiday being introduced during the year.

Stock revaluation occurred as a result of an adjustment to standard stock costings.

Whisky revaluation resulted from the company no longer charging interest as a cost of stock during the maturation period.

Merger costs were incurred in relation to the transfer of operations from the company's former base at Cherybank, in Perth, to Harlow as a result of the group's reorganisation.

5 Loss on sale of fixed assets

The loss incurred on the sale of fixed assets arose from the sale of computers and motor vehicles in the year.

6 Profit on ordinary activities before taxation

	1999 £000	1998 £000
Profit on ordinary activities before taxation is stated		
after charging		
Auditors' remuneration:		
Audit	5	40
Other services - fees paid to the auditor and its associates	-	20
Depreciation and other amounts written off tangible fixed assets:		
Owned	535	1,496
Exchange losses	27	-
after crediting		
Exchange gains	-	101

Notes *(continued)*

7 Remuneration of directors

None of the directors received any emoluments from the company. A management charge of £16,925,000 *(1998: £79,841,000)* was paid by United Distillers UK plc to United Distillers and Vintners (ER) Limited which includes charges for services provided by certain of the directors.

Directors' interests are set out in the directors' report.

8 Staff numbers and costs

The company did not employ any staff during the year. All employees previously employed by United Distillers UK plc had their contracts terminated and reinstated with UDV (HP) Limited. Staff costs incurred in the year have been recharged from UDV (HP) Limited.

The average number of persons employed by the company (including directors) during the year, analysed by category, was as follows:

	Number of employees 1999	1998
Sales, marketing and administration	Nil	284

The aggregate payroll costs of these persons (recharged from UDV (HP) Ltd in 1999) were as follows:

	1999 £000	1998 £000
Wages and salaries	5,886	12,289
Social security costs	482	1,083
Other pension costs	116	1,415
	6,484	14,787

9 Other interest receivable and similar income

	1999 £000	1998 £000
Net exchange gains	27	304
Other	4,849	-
	4,876	304

Of the above amount, £4,849,000 *(1998: £nil)* was payable to group undertakings.

Notes *(continued)*

10 Interest payable and similar charges

	1999 £000	1998 £000
On bank loans and overdrafts	619	10
	619	10

Of the above amount, £619,000 *(1998: £nil)* was payable to group undertakings.

11 Taxation

	1999 £000	1998 £000
UK corporation tax at 30.75% *(1998: 31.3%)*	29,300	39,895
Adjustment relating to an earlier year	-	452
	29,300	40,347

12 Dividends and other appropriations

	1999 £000	1998 £000
Equity shares:		
Interim dividend paid	82,000	-
	82,000	-

Notes *(continued)*

13 Tangible fixed assets

	Freehold Land and buildings £000	Plant, machinery and fittings £000	Motor vehicles £000	Total £000
Cost or valuation				
At beginning of year	3,731	2,933	2,027	8,691
Disposals	(3,731)	(2,933)	(2,027)	(8,691)
At end of year	-	-	-	-
Depreciation				
At beginning of year	406	2,133	378	2,917
Charge for year	-	63	472	535
On disposals	(406)	(2,196)	(850)	(3,452)
At end of year	-	-	-	-
Net book value				
At 30 June 1999	-	-	-	-
At 30 June 1998	3,325	800	1,649	5,774

The amounts shown under cost or valuation include the following:

	30 June 1999 £000	30 June 1998 £000
At cost	-	4,960
At valuation 1992	-	3,731
	-	8,691

If stated under historical cost principles, the amounts would be:

	30 June 1999 £000	30 June 1998 £000
Historical cost	-	13,278
Aggregate depreciation	-	(3,211)
	-	10,067

Notes *(continued)*

14 *Fixed asset investments*

	Other £000
Cost	
At beginning of year	13
Disposals	(13)
At end of year	-
Provisions	
At beginning of year	-
Made during the year	3
On disposals	(3)
At end of year	-
Net book value	
At 30 June 1999	-
At 30 June 1998	13

15 Stocks

	1999 £000	1998 £000
Finished goods and goods for resale	-	24,824

16 Debtors

	1999 £000	1998 £000
Trade debtors	-	38,756
Amounts owed by group undertakings	546,751	1,270,538
Other debtors	-	2,396
Prepayments and accrued income	335	523
	547,086	1,312,213

Notes *(continued)*

17 Creditors: amounts falling due within one year

	1999 £000	1998 £000
Trade creditors	-	2,821
Amounts owed to group undertakings	451,832	1,220,877
Corporation tax	18,303	10,497
Other creditors including taxation and social security	8,976	15,452
Accruals and deferred income	100	15,112
	479,211	1,264,759

18 Provisions for liabilities and charges

The amounts provided for deferred taxation and the amounts not provided are set out below:

	1999		1998	
	Provided £000	Unprovided £000	Provided £000	Unprovided £000
Difference between accumulated depreciation and amortisation and capital allowances	-	-	-	(85)
Provisions allowable for tax in future years	-	-	-	(1,012)
	-	-	-	(1,097)

19 Called up share capital

	1999 £000	1998 £000
Authorised		
Equity: Ordinary shares of £1 each	50	50
Allotted, called up and fully paid		
Equity: Ordinary shares of £1 each	50	50

Notes *(continued)*

20 Reserves

	Profit and loss account £000
At beginning of year	82,245
Retained loss for the year	(14,420)
At end of year	67,825

21 Commitments

There were no capital commitments or annual commitments under non-cancellable operating leases at the end of the financial year *(1998: £nil)*.

22 Pension scheme

The company is a member of a group pension scheme which is operated by its ultimate parent undertaking Diageo plc. The scheme is a defined benefit scheme and is administered by trustees and maintained independently of the finances of Diageo plc and its subsidiaries (the Group).

A valuation of the scheme was performed in 1995 by the actuaries and details of the valuation are included in the accounts of Diageo plc. Contributions in the year to 30 June 1999 attributable to the company amounted to £159,000 *(1998: £1,415,000)*.

All employees formerly employed by UD UK plc have taken new contracts of service with UDV (HP) Limited. There is no change in the pension rights of these employees.

23 Ultimate parent company and parent undertaking of larger group of which the company is a member

United Distillers and Vintners (ER) Limited is the immediate parent company of United Distillers UK PLC. Diageo plc is the ultimate parent company. Diageo plc is both the smallest and largest group to consolidate the accounts and is also the ultimate controlling party. Both parent companies are incorporated in Great Britain. Copies of the group accounts can be obtained from Diageo plc, 8 Henrietta Place, London, W1M 9AG.